

Initiating Coverage Godrej Consumer Products Ltd

7-October-2020



Godrej Consumer Products Ltd

Industry	LTP	Base Case Fair Value	Bull Case Fair Value	Recommendation	Time Horizon
FMCG	Rs. 740.6	Rs. 758	Rs. 809	Buy on dips to Rs 696-700 band and add more on dips to Rs.641-645 band	2 quarters

HDFC Scrip Code	GODCON
BSE Code	532424
NSE Code	GODREJCP
Bloomberg	GCPL:IN
CMP Oct 6, 2020	740.6
Equity Capital (cr)	102
Face Value (Rs)	1
Eq- Share O/S(cr)	102
Market Cap (Rscr)	76957
Book Value (Rs)	77.3
Avg.52 Wk Volume	396079591
52 Week High	772
52 Week Low	425

Share holding Pattern % (June 30, 2020)	
Promoters	63.24
Institutions	29.98
Non Institutions	6.78
Total	100.0

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Our Take:

Godrej Consumer Products Ltd (GCPL) is a part of the over 123-year-old Godrej Group. The group enjoys the patronage of 1.15 billion consumers globally across its businesses. GCPL is present in emerging markets of Asia, Africa and Latin America and the company's product portfolio ranges from home care, personal care to hair care. 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 ranks second in soap products in India, first in air freshener products in India and Indonesia, and is the leader in wet tissue products in Indonesia. Given the nature of daily essentials that the company has been manufacturing for years and its presence in major emerging economies, there is growth visibility seen just on the basis of macro factors like demographics, geography, etc. The company has a strong product portfolio and brand established with a very capable management. International business accounts for ~45% of its turnover.

Valuations & Recommendation:

We believe there is tremendous potential for long-term growth in emerging markets. This will power global consumption and growth over the next couple of decades. GCPL moved from 50% soaps portfolio in FY09 to a more balanced, strategic portfolio over the last decade. The company has centered its growth strategy on targeting these markets and the emergent consuming class. As incomes increase, purchasing power improves and these markets will mature. The new distribution systems will enable greater reach and, to leverage this, GCPL is ramping up their go-to-market strategy. GCPL launched 45 products across geographies in Q1FY21 and plans to launch more products in Household insecticide (HI) portfolio. Domestic HI business, which has struggled, (revenue has declined 1% on CAGR basis over FY16-20) could see strong rebound owing to consumers' increasing preference for disease prevention products (in wake of COVID-19 breakout). The management is focusing on value proposition offers to consumers and consistent innovative launches to gain market share. The company's business recorded strong sequential recovery across most of its markets and expects to deliver close to low double-digit year-on-year constant currency sales growth in July-September. The business fundamentals could get normalized by Q3 and a strong recovery is anticipated in FY2022. The management commentary suggests a sharp revival in structural earnings momentum after 3 odd years of flat growth. GCPL has grown dividend payouts at a fast rate even as its RoE remains at a high level. We believe the company is a good play in the FMCG sector. Investors can buy the stock on dips to Rs.696-700 band (40x FY22E EPS) and add more in the Rs.641-645 band (37x FY22E EPS) for a base case fair value of Rs.758 (43.5x FY22E EPS) and a bull case fair value of Rs.809 (46.5x FY22E EPS) over the next two quarters.

Financial Summary (Rs Cr)

Particulars (Rs cr)	Q1FY21	Q1FY20	YoY-%	Q4FY20	QoQ-%	FY19	FY20	FY21E	FY22E
Net Revenues	2327	2349	(0.9)	2154	8.1	10314	9911	10456	11252
EBITDA	473	459	3.0	477	(0.8)	2118	2143	2297	2503
APAT	317	300	5.9	329	(3.5)	1466	1473	1595	1779
Diluted EPS (Rs)	3.1	2.9	5.9	3.2	(3.5)	14.35	14.42	15.60	17.40
P/E (x)						52.69	52.44	48.45	43.45
EV/EBITDA						27.06	36.65	34.09	31.13
RoE-%						21.67	19.42	15.60	17.40

(Source: Company, HDFC sec)

Long term Triggers

Resurgence of Household Insecticides

In the last couple of years, GCPL has been impacted by unorganised incense sticks players. Government has increased awareness about illegal incense sticks through various media platforms and is promoting the use of branded products. Unorganised players are facing a tough time due to supply chain challenges and increase in import duty on raw bamboo sticks (from 10 to 25%) leading to market share gains for organised players. In order to penetrate this market further the company has launched a full naturals range of coils, incense sticks, fly spray, liquid vapouriser, and personal mosquito repellent products on offer. GCPL is trying to drive penetration with lower price point products, drive premiumisation with very efficacious and safe electrical products, as well as meet the consumer need for natural-based products. The company's largest, most profitable format is liquid vaporisers. Last year, GCPL launched Goodknight Gold Flash, the most powerful liquid vapouriser and the only one with visible vapours. The company under Good Knight and HIT brands now has products in burning, aerosol, electric, personal, and non mosquito formats. Such aggressive product launches with multiple delivery formats will lead to market share gains for GCPL from the unorganized players and other organized players.

Long Term De-risking of Portfolio

In fiscal year 2010, 23% of GCPL's revenues were derived from international businesses. GCPL's operations are now spread across 5 continents. In fiscal year 2020, it is 46%, with Indonesia and Africa accounting for 41% of total revenues. The company has also moved from an over 50% soaps portfolio in 2010 to a more balanced and strategic category portfolio over the last decade. Today, GCPL has three core categories, namely household insecticides, personal wash, and hair care. GCPL has also entered into a new category to serve the hair

care needs of African women. Air care, which GCPL forayed into a few years ago in India, has now become the fourth global category for the company. Today, personal wash accounts for 22% of total revenues, hair care 31% and household insecticides 28% of total revenues. Even with the two main geographies of India and Indonesia, the company has a very well diversified portfolio with no category accounting for more than 40% of total revenues. The product and geographical portfolio of the company has been diversified to a great extent in the past decade there by de-risking the business model. This has been done in a slow and organic manner and shows management's ability to execute plans over the long-term horizon.

Strong Brand Positioning

GCPL is ranked among the largest household insecticide and hair care players in the emerging markets. GCPL ranks second in soap products in India, first in air freshener products in India and Indonesia, and is the leader in wet tissue products in Indonesia. 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. GCPL has three +Rs.1000 crore brands in Good Knight, Darling and No.1. Three brands in the Rs. 500-1000 crore bracket in HIT, Cinthol and Godrej Expert. The top 10 brands contribute to 70% of total revenues. Altogether, GCPL has 12 brands which are market leaders in their categories, and 7 other brands that are no.2 in their categories.

D2C and E-com sales to grow in the future

D2C (Direct to Consumer) selling through GCPL's own websites provides the company with incredibly rich consumer data. In order to capitalise on this opportunity, GCPL has forayed into the world of D2C with three of its India brands (Cinthol, BLUNT and Godrej aer). The initial traction has been very encouraging, and the management plans to roll out this approach to other brands that will benefit from closer consumer connect. This will enable the company to study consumer trends, and better analyze the product viability and acceptability.

In FY20, GCPL saw a 77% increase in its e-commerce business. E-commerce represents a strong opportunity for the company to win in a fast-growing channel and leverage the unique reach of this channel for bringing innovative products and brands to market. GCPL has set up an independent e-commerce business unit in India with separate P&L accountability and fully functional capabilities across sales, marketing, innovation, supply chain, and finance. This structure will deliver the agility and consumer focus required to win in this fast-evolving space. The team is now fully operational and seeing results with over 75% year-on-year growth. GCPL has also created a

dedicated e-commerce team in the USA that has shown success over a short period of time (over 125% growth year-on-year). In Indonesia too, the company has recorded a 78% increase in its e-commerce business. In Africa, GCPL's Dry Hair and Wet Hair categories are a natural fit for digital engagement and e-commerce traction. The company's black hair information and inspiration platform, www.blackhairhub.com, hosts African blogger and consumer-generated content on its social media handles and website. It is a perfect medium to gain consumer insight as well as to promote GCPL's products.

Growing Distribution

In India, GCPL has deepened penetration in traditional trade. The management has guided on expansion of direct presence to 80,000 villages over the next 3 years, focusing on sub 5,000 population villages in key states. The company currently has rural direct distribution reach through 8 million outlets in India across 66,000 villages. Cash and carry channels in India grew by 22% in the last fiscal. In Bangladesh, the company is expanding direct reach to 1,00,000 outlets and driving sales force automation through handheld devices for salespeople. In Sri Lanka, the company is building its own distribution network, which is backed by a distributor management system and sales force automation. In Indonesia, GCPL continues to build on a go-to-market transformation. Consequently, the number of active outlets has increased by 17%, thereby resulting in 1,10,000 monthly outlet transactions. This was enabled by significant additions to the number of salespeople on ground and, productivity improvements.

Through improved collaborations with regional distributor partners, GCPL has enhanced focus on general trade and local modern trade channels. The company has shifted the coverage of key accounts in modern trade to third-party logistics partners. In Nigeria, where trade is largely unorganised and wholesale-led, GCPL is scaling up reach through a more intensive redistribution network. The company is driving higher same-store throughputs with improvements in range and quality of execution. Generating demand through new product seeding models will help initial retail penetration. In Kenya, the company is scaling up distribution expansion through a combination of various models (sub-distributor, van sales, and wholesale-assist). GCPL has shifted focus significantly from primary sales to secondary sales, through strong partnerships with distributors and by monitoring the distributor ERP system. For frontline sales in dry hair care, where product knowledge is a key differentiator, it has a ready talent pool from blue collar factory workers. In South Africa, GCPL has piloted a 'Perfect Stores' programme to increase sales by enhancing shopper experience and maximising shopper conversion opportunities. This was done across the top 40 stores that contribute 80% to the company's turnover, and it was activated through impactful branded point-of-sale communication and trained beauty advisors. Such initiatives have helped and will continue to help the company to grow its distribution reach and gain market share.

Short term Triggers

Innovation in Products

GCPL has increased new launches by the company in the recent times with many new innovative products offered at very competitive price points. GCPL launched 45 products across geographies in Q1 and plans to launch more products in Household insecticide portfolio. Last year, the company launched its “one rupee” paper-based mosquito repellent, Goodknight Fast Card in order to drive penetration and reach in rural India where electricity is a problem and people cannot use electric mosquito repellents. Godrej Expert Rich Crème, a hair color in a sachet, offered by the company is sold for just Rs 30 and compares in quality to much higher priced products. GCPL has also launched Mr. Magic hand wash, which is the first powder-to-liquid hand wash in the world, and is sold at Rs 15 price point. The product has the potential to build out and democratise sanitation and hand washing across emerging countries. Amongst existing categories, GCPL has launched new products in air care with dual benefits of sanitation and air care. In response to COVID-19, GCPL launched sanitiser products across its India and SAARC, Indonesia, Africa, Latin America, and USA businesses in just a few weeks. In many markets, GCPL was a new entrant in the category thereby giving the company a lot of bandwidth for future expansion. Further innovation across categories will auger well for the company as it will ensure its stronghold in the markets it is a leader in at the same time, capturing share in new markets.

Accelerating New Launches

Within the last two years, GCPL has doubled its product launches in India and increased its focus on premiumisation. With the launch of India’s first smart air freshener, GCPL has paved the way for affordable and advanced connected devices in the FMCG domain. Riding on trends in health and wellness, the company has incubated premium portfolios in organic baby care and 100% natural household insecticides. The growing significance of e-commerce as a channel, has resulted in new products specifically co-created and launched as e-commerce first products. In Africa, compared with the previous year, new products launched by the company in wet hair care have multiplied in revenue, thereby leading to a two-fold increase in the wet hair innovation rates. New styles in dry hair care, as led by braids and crochets, are fashion-forward and draw from emerging trends. GCPL’s Indonesia business also sharply grew its Other Pests portfolio in household insecticides, with the launch of new roach and rodent solutions. Following the unprecedented spread of the COVID-19 pandemic, and the need for greater availability of essential hand hygiene products, GCPL launched new sanitiser and hand wash ranges in record speed, ranging from 10 days to a month. In India and Bangladesh, the company has launched new alcohol-based protekt hand sanitisers; in Indonesia GCPL launched an entire range of hand sanitisers called Saniter; in Kenya, the company added to their Lavik portfolio with hand sanitisers and hand washes; in South Africa, the company launched new protekt hand washes; in Argentina, it

introduced hand washes and hand sanitisers; and in the USA, it initiated a new range of hand sanitisers. These new products at this time of need will drive growth for the company.

Having presence in multiple countries/continents will help GCPL as international operations of FMCG companies are expected to be impacted much lesser from COVID compared to Indian operations.

What could go wrong

Competition risk arising from 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 with the growth of the hyper-local formats of Reliance Retail and the new ecom hypermarts poses a risk to the industry dynamics in the medium-term.

Labour risk arising out of shortages due to industrial disputes and attrition of key staff or health and safety-related risks in manufacturing operations and frontline distribution teams

Currency risk as the company has over 40% of its revenues from foreign operations with presence in 5 continents. Currency fluctuation in key international markets including Africa and Indonesia will affect earnings performance.

Economic risk exists in the territories GCPL operates in. Continued enforcement of lockdown if daily new cases are not contained will slow the recovery in business. 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 GCPL saw muted sales, EBITDA and PAT growth in FY19, FY20 and FY21E 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.

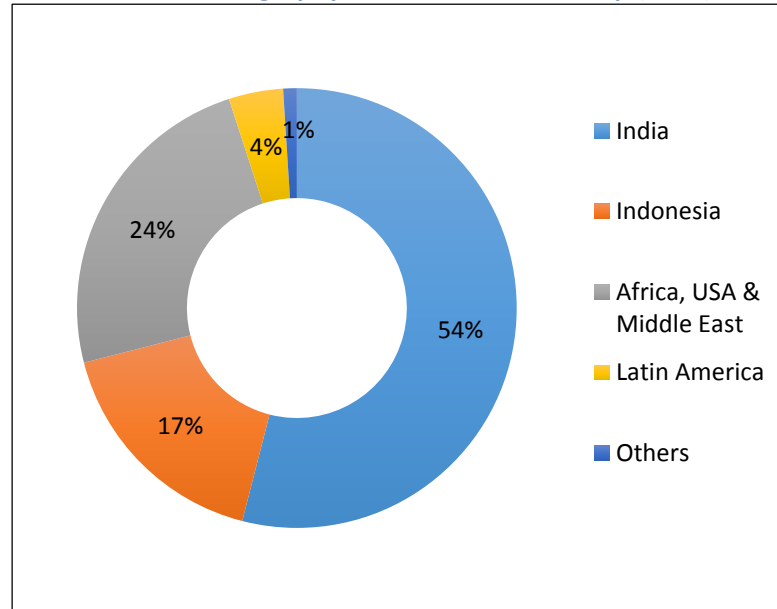
Foreign markets The Africa business has been giving pain over the last few quarters. GCPL has hired the ex-CEO of Nestle Nigeria as the new head of Africa business. The new regional CEO is well versed with the region for decades and the management has strong turnaround expectations from him. On the recent trends, GCPL has seen a sequential improvement in the performance.

Intangible Assets As a result of numerous acquisitions over the past few years, intangibles assets (including goodwill) have remained high at ~Rs.8000 cr which is more than 100% of its net worth.

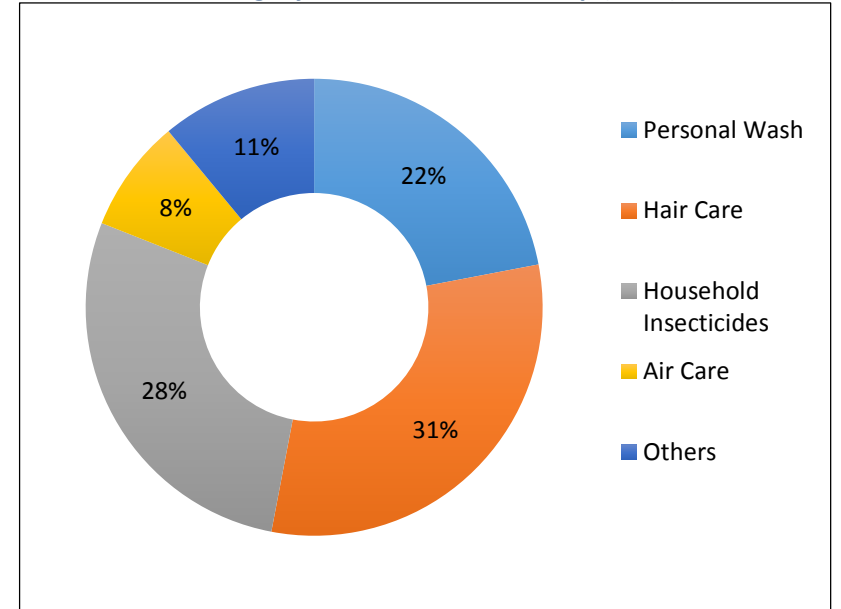
About Company

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Geography Wise Revenue Breakup (FY20)



Category Wise Revenue Breakup (FY20)



Godrej Consumer Products Ltd

Financials

Income Statement

(Rs Cr)	FY18	FY19	FY20	FY21E	FY22E
Net Revenues	9847	10314	9911	10456	11252
Growth (%)	6.25	4.70	-3.90	5.21	7.07
Operating Expenses	7780	8197	7768	8159	8749
EBITDA	2067	2118	2143	2297	2503
Growth (%)	8.93	2.38	1.20	6.70	8.22
EBITDA Margin (%)	20.99	20.53	21.63	21.97	22.25
Depreciation	156	170	197	208	215
EBIT	1911	1948	1946	2089	2288
Other Income	108	109	112	133	155
Interest expenses	161	224	217	177	163
PBT	2038	2085	1760	2045	2280
Tax	405	-256	264	450	502
APAT	1487	1466	1473	1595	1779
Growth (%)	10.38	-1.41	0.46	7.69	10.32
EPS	14.55	14.35	14.42	15.60	17.40

Balance Sheet

As at March	FY18	FY19	FY20	FY21E	FY22E
SOURCE OF FUNDS					
Share Capital	68	102	102	102	102
Reserves	6190	7165	7796	7844	8090
Shareholders' Funds	6258	7267	7898	7946	8192
Long Term Debt	2380	2605	2145	1945	1845
Short Term Debt	154	271	519	519	519
Net Deferred Taxes	195	-473	-570	-570	-570
Long Term Provisions & Others	855	330	290	290	290
Minority Interest	0	0	0	0	0
Total Source of Funds	9842	10000	10282	10130	10277
APPLICATION OF FUNDS					
Net Block	3598	3753	3893	3835	3770
CWIP	82	51	56	56	56
Other Non-Current Assets	296	210	213	213	213
Total Non Current Assets	3976	4014	4163	4104	4039
Goodwill	4719	4918	5339	5328	5307
Inventories	1578	1559	1703	1600	1719
Trade Receivables	1246	1293	1157	1319	1417
Cash & Equivalents	1816	1376	1407	1439	1728
Other Current Assets	530	461	541	574	616
Total Current Assets	5169	4688	4808	4932	5480
Trade Payables	2353	2540	2480	2591	2784
Other Current Liab & Provisions	1669	1081	1547	1643	1765
Total Current Liabilities	4022	3621	4028	4234	4549
Net Current Assets	1147	1068	780	698	931
Total Application of Funds	9842	10000	10282	10130	10277

Godrej Consumer Products Ltd

Cash Flow Statement

(Rs Cr)	FY18	FY19	FY20	FY21E	FY22E
Reported PBT	1858.2	1832.1	1840.9	2045.1	2280.3
Non-operating & EO items	-28.7	-45.6	-50.1	0.0	0.0
Interest Expenses	160.7	224.3	217.4	177.0	163.2
Depreciation	155.7	170.0	197.3	208.3	215.0
Working Capital Change	-15.5	0.6	-261.3	114.6	55.4
Tax Paid	-392.8	-435.1	-344.1	-449.9	-501.7
OPERATING CASH FLOW (a)	1737.7	1746.3	1600.1	2095.0	2212.3
Capex	-311.5	-207.7	-152.0	-150.0	-150.0
Free Cash Flow	1426.2	1538.5	1448.1	1945.0	2062.3
Investments	-94.8	367.2	-438.2	-50.0	-50.0
Non-operating income	66.5	92.1	57.0	0.0	0.0
INVESTING CASH FLOW (b)	-339.8	251.6	-533.3	-200.0	-200.0
Debt Issuance / (Repaid)	-487.6	-344.7	-128.0	-200.0	-100.0
Interest Expenses	-157.8	-214.7	-151.9	-177.0	-163.2
FCFE	780.8	979.2	1168.2	1568.1	1799.1
Share Capital Issuance	-0.7	-0.7	0.0	0.0	0.0
Dividend	-737.9	-1478.6	-985.9	-1547.5	-1532.3
Others	0.0	0.0	0.0	0.0	0.0
FINANCING CASH FLOW (c)	-1384.0	-2038.7	-1265.8	-1924.4	-1795.5
NET CASH FLOW (a+b+c)	13.9	-40.9	-198.9	-29.4	216.8

Key Ratios

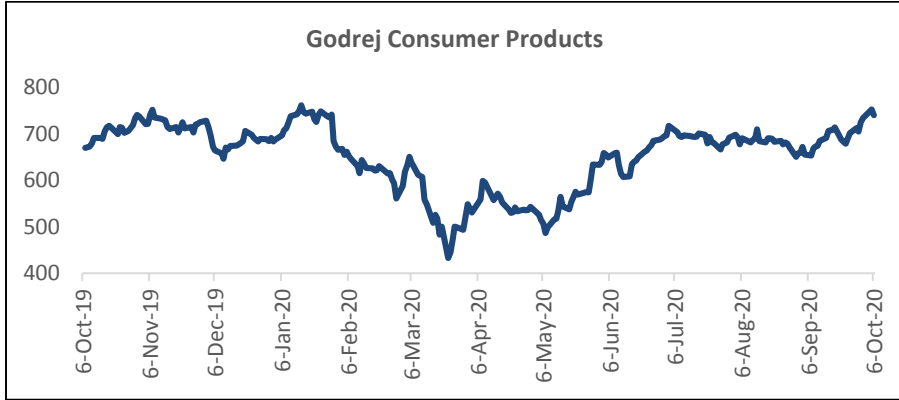
(Rs Cr)	FY18	FY19	FY20	FY21E	FY22E
EBITDA Margin	21.0	20.5	21.6	22.0	22.2
EBIT Margin	20.5	19.9	20.8	20.0	20.3
APAT Margin	15.1	14.2	14.9	15.3	15.8
RoE	25.7	21.7	19.4	15.6	17.4
RoCE	16.8	17.1	15.5	16.3	18.0
Solvency Ratio					
Net Debt/EBITDA (x)	0	1	1	0	0
Net D/E	0.1	0.2	0.2	0.1	0.1
PER SHARE DATA					
EPS	14.6	14.3	14.4	15.6	17.4
CEPS	16.1	16.0	16.3	17.8	19.7
BV	61.3	71.1	77.3	77.9	80.5
Dividend	9.0	12.0	13.0	15.0	17.0
Turnover Ratios (days)	(27.9)	(10.6)	(25.7)	(25.7)	(25.7)
Debtor days	46.2	45.8	45.8	45.8	45.8
Inventory days	55.4	55.5	55.5	55.5	55.5
Creditors days	87.2	89.9	89.9	89.9	89.9
VALUATION					
P/E	51.9	52.7	52.4	48.5	43.5
P/BV	12.3	10.6	9.8	9.7	9.4
EV/EBITDA	30.1	27.1	36.6	34.1	31.1
EV / Revenues	5.7	5.5	7.9	7.5	6.9
Dividend Yield (%)	1.6	2.2	1.7	2.0	2.2

(Source: Company, HDFC sec)

Godrej Consumer Products Ltd



One Year Price Chart



(Source: Company, HDFC sec)

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