

Sector: Consumer Goods
Result Update

	Change
Reco: Buy	↑
CMP: Rs. 742	
Price Target: Rs. 865	↑

↑ Upgrade ↔ No change ↓ Downgrade

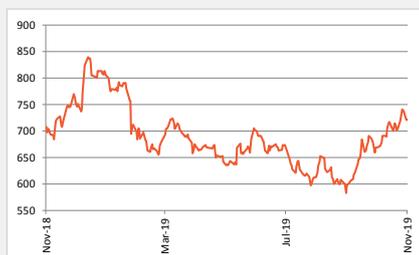
Company details

Market cap:	Rs. 75,855 cr
52-week high/low:	Rs. 848/577
NSE volume: (No of shares)	10.4 lakh
BSE code:	532424
NSE code:	GODREJCP
Sharekhan code:	GODREJCP
Free float: (No of shares)	37.6 cr

Shareholding (%)

Promoters	63.2
FII	27.8
DII	2.3
Others	6.7

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	7.9	17.8	13.2	3.4
Relative to Sensex	0.9	7.2	8.6	-11.3

Sharekhan Research, Bloomberg

Godrej Consumer Products (GCPL) registered decent operating performance in Q2FY2020. Consolidated revenue stood flat at Rs. 2,608.2 crore while benign input prices aided in 362 BPS improvement in OPM. Operating profit grew by 18% during the quarter. The domestic volume growth stood at 7% better than 5% volume growth achieved in Q1FY2020 (the soaps category volumes witnessed little higher than mid-single digit growth). Household Insecticide (HI) posted recovery in performance with 4% growth (driven by high-single-digit volume growth). Indonesia business continues to perform well with double-digit growth in revenue and EBIDTA, while GAUM (Africa) business saw 380 BPS improvement in margin. The management expects domestic volume growth to scale up in H2FY2020 with improvement in the demand environment and HI category is expected to post better growth due to new product launches and receding threat of illegal incense sticks. The hair colour category is expected to see improvement in performance with re-launch of Godrej Hair Crème in the coming quarters. On the other hand, better performance in geographies such as Indonesia and Africa will drive international business performance (with higher operating margins on a y-o-y basis).

Key positives

- Domestic business volumes grew 7%, led by the strong performance of new launches, consumer offers and effective marketing campaigns.
- Recovery was witnessed in the HI category as the category grew by 4% y-o-y driven by high-single-digit volume growth after lull of past twelve quarters.
- Benign input prices helped consolidated gross margins improve by 381 bps, which along with efficiencies drove up OPM by 362 bps in the domestic business.
- The Indonesia business grew by 38% y-o-y in constant currency (CC) terms; adjusted EBITDA margin grew by 380 bps for the GAUM business and 470 bps for the Latin America (LatAm) and SAARC business.

Key negatives

- The soaps category declined by 4% y-o-y mainly due price cuts and consumer offers.
- Growth in the hair colour category was soft impacted by a general slowdown and soft performance of Godrej Expert Rich Crème.

Our Call

Valuation – Upgraded to Buy with revised Price Target of Rs. 865: We have broadly maintained our earnings estimates for FY2020 and FY2021. We have introduced FY2022 earnings estimates in this note. The company is focusing on improving its volume growth through innovations, enhancing the distribution reach and adequate brand building and promotional activities in the near term. Benign input prices would help the company clock better margins in the near term. The receding of concerns hovering around domestic HI business (45% of total domestic business) and international geographies performing well gives us improved earnings visibility in the near term. Hence, with modest P/E upgrade and roll over factor (valuing stock at 40x average of FY2021/22 earnings), we upgrade our rating on the stock to Buy from Hold with revised price target (PT) of Rs. 865.

Key Risks

- Fluctuation in currencies of key international markets including Africa and Indonesia will affect growth and profitability of international business.
- Increase in prices of key raw materials such as palm oil would affect the profitability and earnings growth.

Valuation (consolidated)

Particulars	FY18	FY19	FY20E	FY21E	FY22E
Revenues	9,937	10,314	10,639	12,413	14,105
OPM (%)	21.1	20.7	22.0	22.5	22.8
Adjusted PAT	1,493	1,479	1,656	2,031	2,380
% YoY growth	14.2	-1.0	12.0	22.7	17.2
Adjusted EPS (Rs.)	14.6	14.5	16.2	19.9	23.3
P/E (x)	50.8	51.3	45.8	37.3	31.9
P/B (x)	8.1	10.4	8.7	7.3	6.0
EV/EBIDTA (x)	26.3	37.4	33.8	27.9	23.8
RoNW (%)	25.8	21.9	20.8	21.2	20.6
RoCE (%)	17.4	17.5	18.2	20.3	21.3

Source: Company; Sharekhan estimates

Revenue stood flat; domestic business disappoints: Q2FY2020 consolidated revenue grew by just 2% y-o-y on a comparable basis whereas the reported revenue stood flat at Rs. 2,630 crore largely owing to a 4% decline in the international business. Sales volumes grew by 7% in Q2FY2020 (better than our expectation), sequentially higher than 5% volume growth in Q1FY2020. On a comparable basis, the international business revenue grew by 4% y-o-y (7% in CC terms). Gross margins improved by 381 bps to 56.6% on benign input prices and improving product mix. OPM expanded by 362 BPS to 21.9% driven by operating efficiencies. Operating profit grew by 18.5% y-o-y to Rs. 576.5 crore. Despite, a higher incidence of tax, strong operating performance resulted in 12.6% growth in the adjusted PAT to Rs. 416.5 crore. There was a one-time exceptional gain of Rs. 194.2 crore due to change in earn out liability and Rs. 76.4 crore due to one-time gain for sale of UK business in the base quarter (Q2FY2019). This resulted in a decline in reported PAT by 28% y-o-y to Rs. 413.9 crore in Q2FY2020 as against Rs. 577.7 crore in Q2FY2019.

HI category witnessed recovery; hair colours reported a soft quarter:

- ◆ **Soaps – Volume growth to sustain due to price cuts:** The domestic soaps category declined by 4% y-o-y mainly due to price offs and consumer offers. However, the category reported higher than mid-single-digit volume growth. It has been consistently gaining market share, gaining 60 bps in the quarter. The company focused on enhancing the brand recall through marketing initiatives with regional launches. Consumer offers will help volume growth to sustain, but price cuts would affect revenue growth in the near term. However the company has indicated that there won't be any further pricing cuts unless competition step in and take some aggressive pricing actions.
- ◆ **Hair colour – Soft quarter:** Hair colour category revenue grew by just 2% y-o-y, affected by general slowdown in the domestic market and soft performance of Godrej Expert Rich Crème. The company re-launched Expert Crème hair colour in the domestic market and Godrej Anoop Ayurvedic anti hair fall oil on the e-commerce platform. Godrej Expert Easy 5 minute shampoo hair colour is scaling up well in the South and the company launched it nationally at the fag end of the quarter. Expert Crème has low penetration of 13% and hence the re-launch of the product should help the category to post better growth in the near term.
- ◆ **HI –Recovery seen:** The HI category witnessed recovery during the quarter with revenue growing by 4% y-o-y driven by higher than mid-single-digit volume growth. The price-offs in liquid vapouriser augured well for the category driving volumes and market share gains. In addition to price-offs, the threat of illegal incense sticks has been gradually receding as the government is taking stringent regulatory measures to control them. The association has several actions against illegal players including conducting raids in their manufacturing units. The association is planning to put a media advertisement and would also put advertisement in the movie theatres to educate against the illegal sticks. Also the companies are educating the wholesales and other trade partners about after effects of usage of illegal sticks. On the other hand, the company recently launched Good Knight Gold Flash in south and HIT Rat Glue pad in select markets along with HIT Anti Mosquito Racquet on the e-commerce channel. It expects good traction for Good Knight Gold Flash in the coming quarters. Overall HI category should post improved performance in the coming quarters.

International business affected by unfavourable currency movements

Revenue from international business grew by 4% y-o-y on a comparable basis to Rs. 1,144 crore (7% growth in CC terms) driven by 38% growth in LatAm and SAARC regions and 13% growth in Indonesia (in CC terms). Indonesia revenue grew by 17% y-o-y to Rs. 425 crore driven by growth in HI, air fresheners and baby wipes whereas adjusted EBITDA margin expanded by 50 bps led by strong gross margin expansion. Business in the GAUM cluster reported subdued performance with revenue declining by 6% y-o-y (declined by 2% in CC terms) to Rs. 591 crore affected by an unfavourable macro-environment in certain African markets. However, adjusted EBITDA margin improved by 380 bps. Other regions (including LatAm and SAARC) recorded a strong growth of 24% y-o-y in revenue to Rs. 128 crore and an adjusted margin expansion of 470 bps. Operating margins of the India business improved by 40 bps y-o-y to 26.3%, while margins of the international business expanded by 320 bps y-o-y to 16.1%.

Results (Consolidated)

Particular	Rs cr				
	Q2FY20	Q2FY19	Y-o-Y (%)	Q1FY20	Q-o-Q (%)
Total revenue	2630.2	2659.2	-1.1	2348.8	12.0
Raw material cost	1141.8	1255.8	-9.1	1007.0	13.4
Employee cost	266.5	256.9	3.7	265.3	0.5
Advertisement & Publicity	213.3	255.9	-16.6	192.9	10.6
Other expenses	432.0	404.2	6.9	424.7	1.7
Total operating expenses	2053.7	2172.7	-5.5	1889.9	8.7
Operating profit	576.5	486.5	18.5	458.9	25.6
Other income	26.6	26.0	2.2	21.4	24.2
Interest expense	53.1	61.2	-13.2	55.1	-3.6
Forex gain / (loss)	-4.6	0.3	-	-3.3	-
Depreciation	47.7	42.6	12.1	47.3	0.8
Profit before tax	497.6	409.0	21.7	374.6	32.8
Tax	86.9	39.2	-	85.3	1.9
Adjusted PAT (before MI)	416.5	369.8	12.6	289.3	44.0
Minority interest (MI)	0.3	0.1	-	0.2	-
Extraordinary item	-2.9	207.8	-	118.1	-
Reported PAT	413.9	577.7	-28.4	407.6	1.5
EPS (Rs.)	4.1	3.6	12.6	2.8	44.0
			BPS		BPS
GPM (%)	56.6	52.8	381	57.1	-54
OPM (%)	21.9	18.3	362	19.5	238

Source: Company; Sharekhan Research

Results (Standalone)

Particulars	Rs cr				
	Q2FY20	Q2FY19	Y-o-Y (%)	Q1FY20	Q-o-Q (%)
Total revenue	1521.3	1507.6	0.9	1315.4	15.7
Operating Profit	400.7	391.0	2.5	308.5	29.9
Adjusted Net profit	334.6	295.8	13.1	240.1	39.4
GPM (%)	58.3	59.3	-107 BPS	58.6	-37 BPS
OPM (%)	26.3	25.9	41 BPS	23.5	288 BPS

Source: Company; Sharekhan Research

Segmental Performance

Particulars	Rs cr				
	Q2FY20	Q2FY19	Y-o-Y (%)	Q1FY20	Q-o-Q (%)
Soap	491	512	-4.1	556	-11.7
Hair Colour	160	158	1.3	181	-11.6
Liquid Detergents	179	164	9.1	146	22.6
Household Insecticides (HI)	683	658	3.8	427	60.0

Source: Company; Sharekhan Research

Region-wise Performance

Particulars	Rs cr				
	Q2FY20	Q2FY19	Y-o-Y (%)	Q1FY20	Q-o-Q (%)
Revenue					
Indonesia	426	364	17.1	372	14.6
GAUM	591	631	-6.3	562	5.1
Others	128	191	-33.0	131	-2.4
Total	1145	1186	-3.4	1065	7.5
EBITDA					
Indonesia	106	88	19.9	88	20.5
GAUM	50	-15	-	47	8.2
Others	4	6	-32.4	-2	-
Total	160	79	103.2	133	20.5
EBITDA Margins - Reported (%)					
Indonesia	24.0	24.2	-22 BPS	23.6	43 BPS
GAUM	8.5	-	-	8.3	24 BPS
Others	2.9	2.9	-	-	-

Source: Company; Sharekhan Research

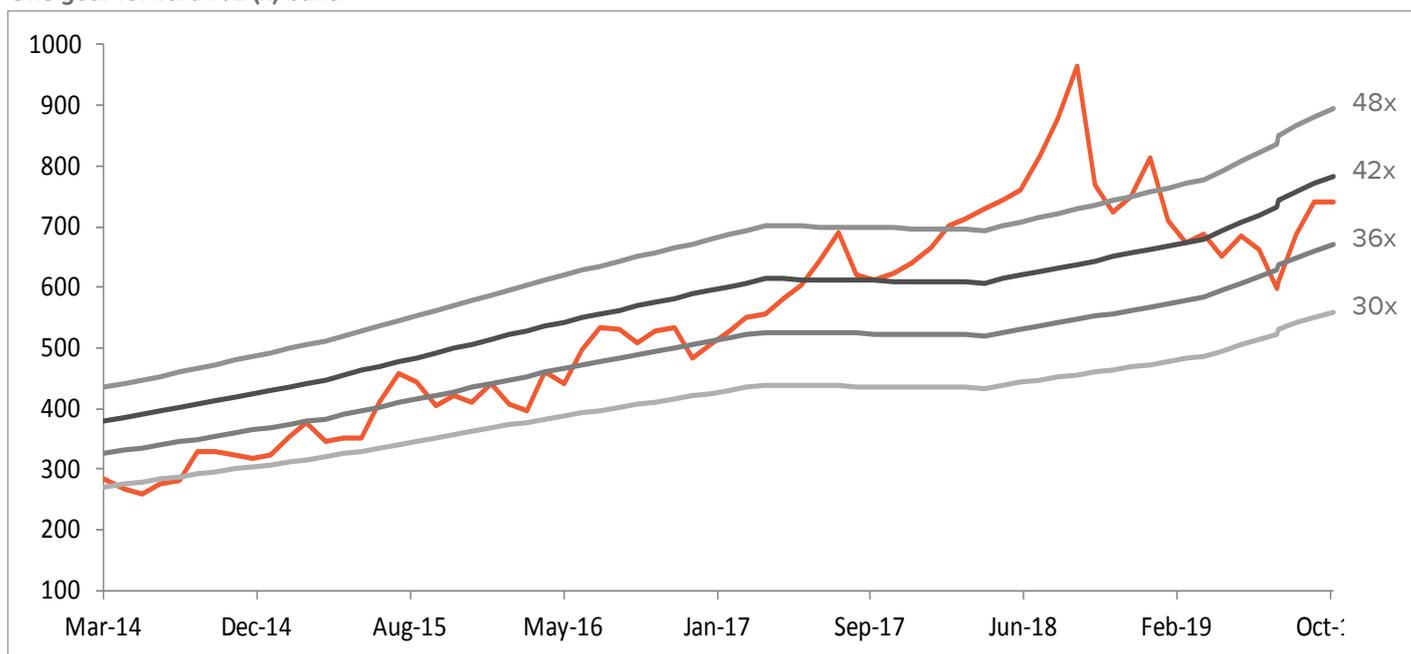
Outlook – Domestic volume growth to remain at 6-8% in H2FY2020

GCPL's domestic volume growth improved to 7% in Q2FY2020 from 5% in Q1FY2020. The management expects domestic volume growth to scale up in H2FY2020 with over improvement in the demand environment. The HI category is expected to post better growth due to new product launches and receding threat of illegal incense sticks. The hair Colour category is expected to see improvement in the performance with re-launch Godrej Hair crème in the coming quarters. We expect domestic volume growth to sustain in the range 6-8% in H2FY2020 and will gradually improve with increase in the scale of HI and hair colour business. On the other hand, better performance in geographies such as Indonesia and Africa will drive international business performance. The Indonesia business will continue to post double digit revenue growth and would see expansion in the OPM in the coming years. Africa business would see gradual improvement in the sales growth but margin expansion should sustain because various cost saving programmes undertaken. We expect consolidated OPM to stand 22-23% in the near term.

Valuation – Upgraded to Buy with revised Price Target of Rs. 865

We have broadly maintained our earnings estimates for FY2020 and FY2021. We have introduced FY2022 earnings estimates in this note. The company is focusing on improving its volume growth through innovations, enhancing the distribution reach and adequate brand building and promotional activities in the near term. Benign input prices would help the company clock better margins in the near term. The receding of concerns hovering around domestic HI business (45% of total domestic business) and international geographies performing well gives us improved earnings visibility in the near term. Hence, with modest P/E upgrade and roll over factor (valuing stock at 40x average of FY2021/22 earnings), we upgrade our rating on the stock to Buy from Hold with revised price target (PT) of Rs. 865.

One year forward P/E (x) band



Source: Sharekhan Research

Peer valuation

Companies	P/E (x)			EV/EBIDTA (x)			RoCE (%)		
	FY19	FY20E	FY21E	FY19	FY20E	FY21E	FY19	FY20E	FY21E
HUL	76.0	61.9	52.1	53.8	44.7	38.6	113.2	108.7	95.9
Dabur India	56.3	50.8	42.4	47.1	41.8	34.9	28.1	29.4	30.0
Marico India	50.1	41.7	35.1	36.6	30.6	25.4	40.9	42.2	43.7
Godrej Consumer Products	51.3	45.8	37.3	37.4	33.8	27.9	17.5	18.2	20.3

Source: Company, Sharekhan estimates

About company

Godrej Consumer Products (GCPL) is a leading emerging market company with a turnover of more than Rs. 10,000 crore. The group enjoys the patronage of 1.15 billion consumers globally across businesses. GCPL is present in key product categories such as soaps, hair colours and household insecticides. The company's power brands include Godrej No.1 soap, Godrej expert range of hair colours and Good Knight, among others. GCPL operates internationally in Indonesia, Latin America and GAUM (Africa, USA and Middle East) regions.

Investment theme

GCPL has a '3 by 3' approach to international expansion by building presence in '3' emerging markets (Asia, Africa and Latin America) across '3' categories (home care, personal wash and hair care products). It has a leadership position in most categories in the domestic and international markets. Sustained innovation, cross pollination, enhanced distribution reach and a foray into new categories have remained the company's key growth pillars. However, a slowdown in the HI category and subdued performance in the international market has affected earnings in the near term.

Key Risks

- ◆ Currency fluctuation in key international markets including Africa and Indonesia will affect earnings performance.
- ◆ Increase in prices of key raw materials such as palm oil would affect the profitability and earnings growth.
- ◆ Increased competition in highly penetrated categories such as soaps would threaten revenue growth or any competition from illegal entrants in HI category would affect category performance.

Additional Data

Key management personnel

Adi Gogrej	Chairman
Nisaba Godrej	Executive Chairperson
Vivek Gambhir	Managing Director and CEO
V Srinivasan Vishwanathan	CFO and Company Secretary

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Godrej Seeds & Genetics	27.4
2	Godrej Industries Ltd	23.8
3	Godrej & Boyce Manufacturing Co Ltd	7.3
4	Temasek Holdings Pvt Ltd	2.5
5	Commonwealth Bank Of Australia	2
6	Arisaig India Fund	1.5
7	Vanguard Group Inc	1.4
8	Naoroji Rishad	1.3
9	RKN Enterprises	1.3
10	Capital Group Cos Inc	1.3

Source: Bloomberg

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Compliance Officer: Mr. Joby John Meledan; Tel: 022-61150000; email id: compliance@sharekhan.com;

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