JM FINANCIAL

Colgate-Palmolive India | HOLD

Broadly inline; Some stability seen in toothpaste market-share

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Colgate's operating performance was expectedly muted in 1QFY18 with volumes down 5% YoY (vs expectation of -4%). Net sales realisation growth, though, was much lower than what we expected (details below) which resulted in a c.3% revenue decline (vs forecast of 3% growth). The company surprisingly effected a 7.9% cut in A&P spends which helped drive a 5% operating profit growth. The key positive highlight, though, was the stability in toothpaste market share (on sequential comparison) at 54.3% after witnessing continuous decline since mid-2015. On the negative side, toothbrush seems to have lost share after consecutive quarters of gain for a significant stretch of time. Colgate seems to have increased focus on its Palmolive personal-care business which witnessed some launches in the male-grooming space during the quarter. We like Colgate's business model but at 43-44x NTM earnings, upside on the stock appears limited, given subdued business momentum.

- **3rd consecutive quarter of sharp decline in volumes, led this time by trade destocking on GST transition:** Colgate's 1QFY18 sales declined 2.8% to INR11.1bn but EBITDA and adjusted net profit still grew 5% and 2.3% to INR2.2bn and INR1.3bn respectively on the back of significant expansion in operating margin (150bps) – some investors believe this is an area that needs careful monitoring to see whether Colgate's famed obsession with volumes and market-shares has given way to margin/profitability focus instead. Volumes fell 5% YoY during the quarter – a weaker performance compared to HUL, GCPL (both reported flattish volume) but better than 7-9% decline reported by Marico, Bajaj Corp. 1QFY18 was the third consecutive quarter of volume decline – attributable this time round to trade destocking pre-GST implementation. Despite volume performance being broadly on expected lines, value-sales declined vs our expectation of a growth therein due to higher promotions and trade incentives given in the month of May to incentivise the channel – this negated the effect of a significant part of the price-hikes taken in recent months. Colgate has since passed on the benefits of GST (lower tax-incidence, input-tax credits) through 8-9% retail-price reduction in key toothpaste and toothbrush SKUs.
- **Pace of GPM expansion moderated due to higher trade incentives and promotions:** Colgate's GPM expanded 45bps – much lower than our expectation and a rather sharp moderation vs 129bps expansion seen during Jan-Mar'17. Growth in net sales realisation decelerated significantly (2-2.5% vs 5-6% in the preceding quarter) despite further price hikes - management attributed this to increased spends on trade incentives, promotions to deal with disruptions caused in the trade in anticipation of the transition to GST (Jul 1st). EBITDA margin, though, witnessed a sharp 148bps expansion which was helped by 8% lower ad-spends – a surprise given the high competitive intensity in the space.
- **Toothpaste market share stable on sequential comparison, as per our workings:** Colgate's toothpaste volume market share for 1QFY18 stood at 54.3% - 80bps lower vs 55.1% share clocked in FY17. As per our calculations, Colgate's toothpaste market share has sustained at similar levels for the past two quarters - quite a relief given that it has otherwise been losing share for the past 1.5-2 years now. The toothbrush business, on the other hand, has reported some erosion in market share to 45% for 1QFY18 vs 47.4% in FY17. The company has launched two new variants in toothbrush segment - one being targeted at the bottom-of-the-pyramid which appears to be a response to this loss.

Recommendation and Price Target	
Current Reco.	HOLD
Previous Reco.	HOLD
Current Price Target (12M)	1,135
Upside/(Downside)	+4.8%
Previous Price Target	940
Change	+20.7%

Key Data – CLGT IN	
Current Market Price	Rs1,083
Market cap (bn)	Rs294.6/US$4.6
Free Float	43%
Shares in issue (mn)	272.0
Diluted share (mn)	272.0
3-mon avg daily val (mn)	Rs414.8/US$0.4
52-week range	1,139/861
Sensex/Nifty	32,477/10,082
Rs/US$	63.7

Price Performance

%	1M	6M	12M
Absolute	-4.4	20.0	15.7
Relative*	-7.4	5.1	-0.6

* To the BSE Sensex

Financial Summary (Rs mn)

Y/E March	FY16A*	FY17A	FY18E	FY19E	FY20E
Net Sales	43,190	44,898	49,648	55,585	62,761
Sales growth (%)	9.2*	4.0	10.6	12.0	12.9
EBITDA	9,385	9,449	10,693	12,225	14,091
EBITDA (%)	21.7	21.0	21.5	22.0	22.5
Adjusted net profit	5,708	5,613	6,402	7,405	8,662
EPS (INR)	21.0	20.6	23.5	27.2	31.8
EPS growth (%)	2.1	-1.7	14.1	15.7	17.0
ROIC (%)	97.0	66.3	63.1	72.1	89.6
ROE (%)	63.4	48.7	45.0	45.3	49.2
PE (x)	51.6	52.5	46.0	39.8	34.0
Price/Book Value (x)	28.6	23.1	18.7	17.3	16.2
EV/EBITDA (x)	31.0	30.8	27.0	23.5	20.2
Dividend Yield (%)	0.9	0.9	1.4	1.9	2.2

Source: Company data, JM Financial. Note: Valuations as of 03/Aug/2017. *Note: FY16 growth impacted by Ind-AS transition.

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Exhibit 1. 1QFY18 result snapshot (Rs mn)

	1QFY18	1QFY17	YoY chg	1QFY18E	% var
Sales incl excise	**11,099**	**11,415**	**-2.8%**	**11,726**	**-5.3%**
Other Operating Income	87	76	15.0%	85	2.6%
Total Revenue	11,186	11,491	-2.7%	11,810	-5.3%
Gross Profit	**6,110**	**6,234**	**-2.0%**	**6,550**	**-6.7%**
Gross Profit Margin %	55.1%	54.6%	45 bps	55.9%	-81 bps
Staff Cost	727	739	-1.6%	797	-8.8%
A&P	1,434	1,556	-7.9%	1,636	-12.4%
Other Expenses	1,818	1,901	-4.4%	1,923	-5.4%
EBITDA	**2,218**	**2,113**	**5.0%**	**2,279**	**-2.6%**
EBITDA margin %	20.0%	18.5%	148 bps	19.4%	55 bps
Depreciation	373	316	17.9%	346	7.8%
EBIT	**1,845**	**1,796**	**2.7%**	**1,933**	**-4.5%**
EBIT margin %	16.6%	15.7%	89 bps	16.5%	14 bps
Net Financial Other Income	125	101	23.5%	76	63.3%
PBT	**1,970**	**1,897**	**3.8%**	**2,009**	**-1.9%**
Tax	606	640	-5.3%	683	-11%
Net Profit	**1,364**	**1,257**	**8.5%**	**1,326**	**2.9%**
Adjusted Net Profit	**1,286**	**1,257**	**2.3%**	**1,326**	**-3.0%**

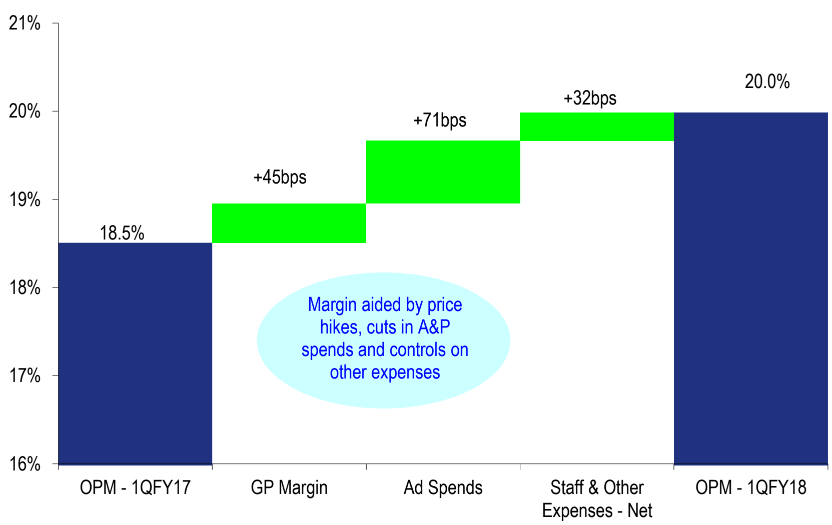
Source: Company, JM Financial

Exhibit 2. Costs breakdown

% of sales	1QFY18	1QFY17	1QFY18E
Cost of Goods Sold	44.9%	45.4%	44.1%
Staff Cost	6.6%	6.5%	6.8%
Advertisement	12.9%	13.6%	14.0%
Other Expenses	16.4%	16.7%	16.4%

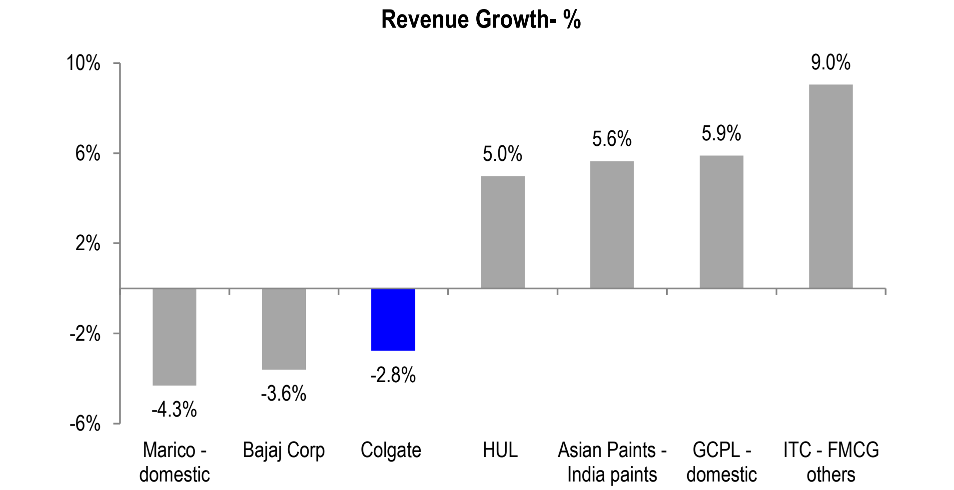
Source: Company, JM Financial

Exhibit 3. Operating margin movement – 1QFY18



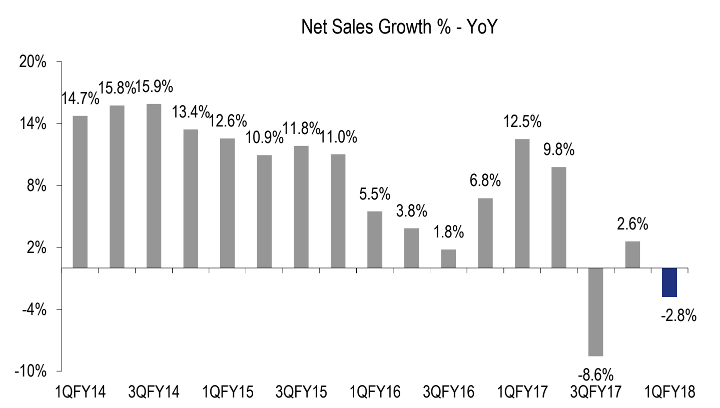
Source: Company, JM Financial

Exhibit 4. Sales growth trend relative to peers



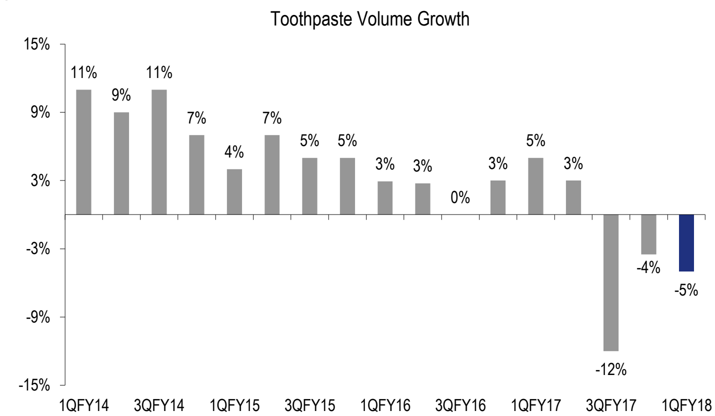
Source: Company, JM Financial

Exhibit 5. Quarterly sales growth trend



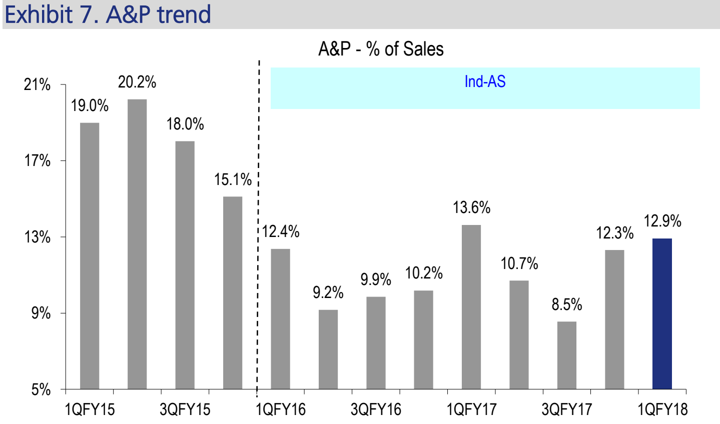
Source: Company, JM Financial

Exhibit 6. Toothpaste volume growth trend



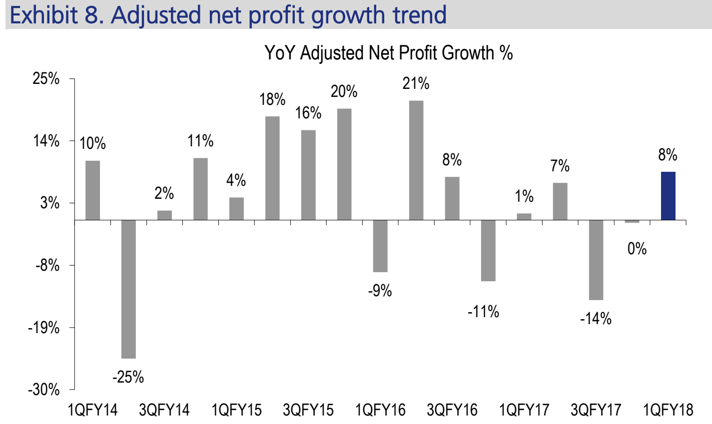
Source: Company, JM Financial

Exhibit 7. A&P trend



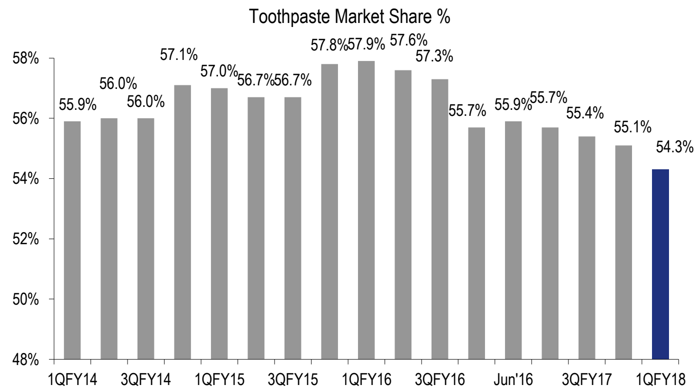
Source: Company, JM Financial

Exhibit 8. Adjusted net profit growth trend



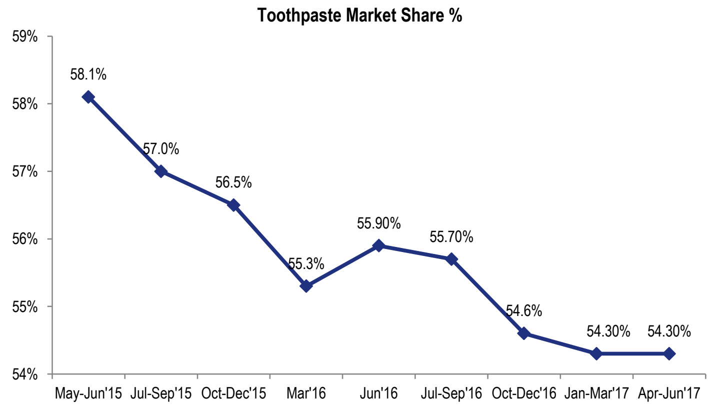
Source: Company, JM Financial

Exhibit 9. Colgate - toothpaste market share trend



Source: Company, JM Financial

Exhibit 10. Toothpaste market share – similar on sequential basis



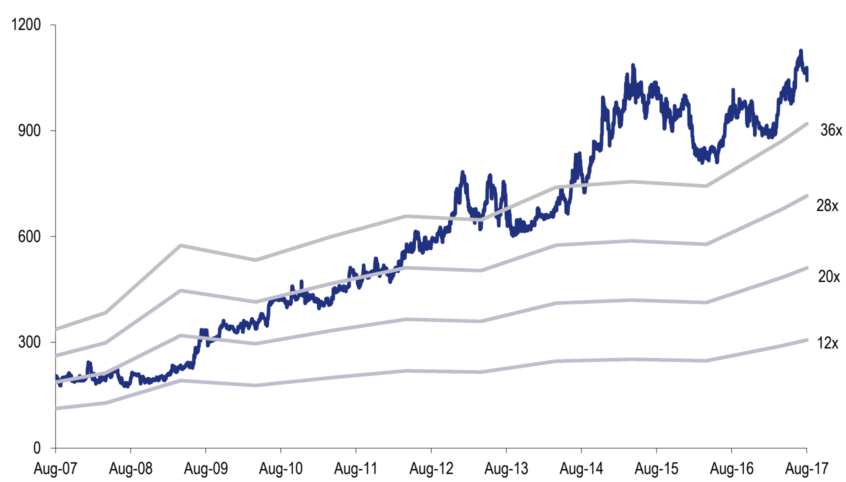
Source: Company, JM Financial

Exhibit 11. Summary of estimate changes (Rs mn)

	FY18	FY19	FY20
Current			
Sales	49,648	55,585	62,761
EBITDA	10,693	12,225	14,091
Adjusted Net Profit	6,402	7,405	8,662
EPS – Rs	23.5	27.2	31.8
Earlier			
Sales	50,411	56,958	NA
EBITDA	10,979	12,720	NA
Adjusted Net Profit	6,608	7,754	NA
EPS - Rs	24.3	28.5	NA
Change - %			
Sales	-1.5%	-2.4%	NA
EBITDA	-2.6%	-3.9%	NA
Adjusted Net Profit	-3.1%	-4.5%	NA
EPS	-3.1%	-4.5%	NA

Source: Company, JM Financial

Exhibit 12. Colgate one-year forward PE band



Source: Company, JM Financial

Financial Tables (Standalone)

Profit & Loss Statement					(INRmn)
Y/E March	FY16A*	FY17A	FY18E	FY19E	FY20E
Net sales (Net of excise)	**43,190**	**44,898**	**49,648**	**55,585**	**62,761**
Growth (%)	9.2%	4.0%	10.6%	12.0%	12.9%
Other Operating Income	301	304	336	376	424
Total Revenue	**43,491**	**45,202**	**49,984**	**55,961**	**63,185**
Cost of Goods Sold/Op. Exp.	19,572	20,147	22,208	24,671	27,624
Personnel cost	2,624	2,885	3,131	3,494	3,932
Other expenses	11,910	12,721	13,953	15,571	17,537
EBITDA	**9,385**	**9,449**	**10,693**	**12,225**	**14,091**
EBITDA (%)	21.7%	21.0%	21.5%	22.0%	22.5%
EBITDA Growth (%)	14.1%	0.7%	13.2%	14.3%	15.3%
Depn & Amort	1,114	1,332	1,586	1,819	1,996
EBIT	8,271	8,116	9,107	10,406	12,094
Other Income	395	398	535	745	950
Finance Cost	0	0	0	0	0
PBT before Excep & Forex	8,666	8,514	9,641	11,151	13,044
Excep & forex Inc/Loss(-)	-313	0	0	0	0
PBT	8,353	8,514	9,641	11,151	13,044
Taxes	2,541	2,740	3,239	3,746	4,382
Extraordinary Inc/Loss(-)	0	0	0	0	0
Assoc. Profit/Min. Int.(-)	0	0	0	0	0
Reported Net profit	5,812	5,774	6,402	7,405	8,662
Adjusted Net Profit	**5,708**	**5,613**	**6,402**	**7,405**	**8,662**
Net Margin (%)	13.2%	12.5%	12.9%	13.3%	13.8%
Diluted share capital (mn)	272.0	272.0	272.0	272.0	272.0
Diluted EPS (Rs)	**21.0**	**20.6**	**23.5**	**27.2**	**31.8**
Diluted EPS Growth	2.1%	-1.7%	14.1%	15.7%	17.0%
Total Dividend + Tax	3,274	3,289	5,122	6,664	7,796
Dividend Per Share (Rs)	10.0	10.0	15.6	20.4	23.8

Source: Company, JM Financial

Balance Sheet					(INRmn)
Y/E March	FY16A*	FY17A	FY18E	FY19E	FY20E
Shareholders' Fund	10,310	12,738	15,726	16,980	18,224
Share capital	272	272	272	272	272
Reserves & Surplus	10,038	12,466	15,454	16,708	17,952
Preference Share Capital	0	0	0	0	0
Minority Interest	0	0	0	0	0
Total Loans	0	0	0	0	0
Def. Tax Liab / Assets (-)	97	275	49	-213	-518
Total - Equity & Liab	**10,407**	**13,013**	**15,775**	**16,768**	**17,706**
Net Fixed Assets	10,865	12,747	13,661	13,842	13,346
Gross Fixed Assets	11,184	13,517	16,017	18,017	19,517
Intangible Assets	0	0	0	0	0
Less: Depn. & Amort.	1,103	2,435	4,021	5,840	7,837
Capital WIP	784	1,666	1,666	1,666	1,666
Investments	312	312	374	449	538
Current Assets	8,852	10,175	13,091	15,175	18,146
Inventories	2,915	2,926	3,235	3,655	4,127
Sundry Debtors	1,015	1,299	1,028	1,151	1,300
Cash & Bank Balances	2,887	2,943	5,669	7,053	9,237
Loans & Advances	1,021	1,770	1,859	1,952	2,049
Other Current Assets	1,013	1,238	1,300	1,365	1,433
Current Liab. & Prov.	9,622	10,221	11,351	12,698	14,324
Current Liabilities	7,918	8,669	9,527	10,605	11,904
Provisions & Others	1,703	1,552	1,824	2,093	2,420
Net Current Assets	-770	-46	1,739	2,477	3,821
Application of Funds	**10,407**	**13,013**	**15,775**	**16,768**	**17,706**

Source: Company, JM Financial

Cash Flow Statement					(INRmn)
Y/E March	FY16A*	FY17A	FY18E	FY19E	FY20E
Profit before Tax	8,353	8,514	9,641	11,151	13,044
Depn. & Amort.	1,114	1,332	1,586	1,819	1,996
Net Interest Exp. / Inc. (-)	-395	-398	-534	-745	-950
Inc (-) / Dec in WCap.	156	311	773	505	662
Others	183	135	-226	-261	-306
Taxes Paid	-2,524	-3,014	-3,071	-3,604	-4,205
Operating Cash Flow	**6,887**	**6,880**	**8,169**	**8,864**	**10,243**
Capex	-2,713	-3,212	-2,500	-2,000	-1,500
Free Cash Flow	*4,175*	*3,668*	*5,669*	*6,864*	*8,743*
-Inc/dec in investments	70	0	-62	-75	-90
Other current assets	277	-209	535	745	950
Investing Cash Flow	**-2,366**	**-3,422**	**-2,028**	**-1,330**	**-639**
Inc/(dec) in capital	0	0	0	0	0
Dividend+Tax Thereon	-3,758	-3,270	-3,415	-6,150	-7,419
Inc/dec in loans	0	0	0	0	0
Other assets	-157	-135	0	0	0
Financing Cash Flow	**-3,914**	**-3,405**	**-3,415**	**-6,150**	**-7,419**
Inc / Dec (-) in Cash	607	53	2,726	1,384	2,184
Opening cash balance	2,280	2,890	2,943	5,669	7,053
Closing cash balance	2,887	2,943	5,669	7,053	9,237

Source: Company, JM Financial

Dupont Analysis					
Y/E March	FY16A*	FY17A	FY18E	FY19E	FY20E
Net Margin	13.2%	12.5%	12.9%	13.3%	13.8%
Asset Turnover (x)	4.8	3.8	3.4	3.4	3.6
Leverage Factor (x)	1.0	1.0	1.0	1.0	1.0
RoE	63.4%	48.7%	45.0%	45.3%	49.2%

Key Ratios					
Y/E March	FY16A*	FY17A	FY18E	FY19E	FY20E
BV/Share (INR)	37.9	46.8	57.8	62.4	67.0
ROIC (%)	97.0%	66.3%	63.1%	72.1%	89.6%
ROE (%)	63.4%	48.7%	45.0%	45.3%	49.2%
Net Debt-equity ratio (x)	-0.3	-0.3	-0.4	-0.4	-0.5
PER	51.6	52.5	46.0	39.8	34.0
PBV	28.6	23.1	18.7	17.3	16.2
EV/EBITDA	31.0	30.8	27.0	23.5	20.2
EV/Net Sales	6.7	6.5	5.8	5.2	4.5
Debtor days	9	11	8	8	8
Inventory days	25	24	24	24	24
Creditor days	85	89	89	89	89

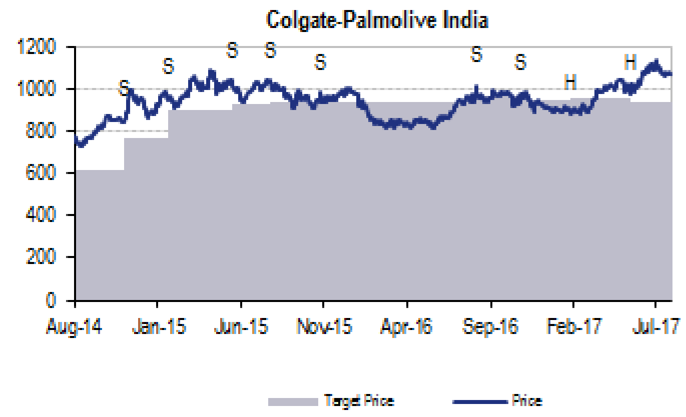
Source: Company, JM Financial

*Note: Sales growth for FY16 shown in above impacted by Ind-AS transition. FY16 LTL Sales , EBITDA and adjusted EPS grew 4.5%, 13.3% and 1.3% respectively

History of Earnings Estimate and Target Price

Date	FY17E EPS (Rs)	% Chg.	FY18E EPS (Rs)	% Chg.	Target Price	% Chg.
26-May-14					611	
5-Nov-14	27.5				765	25.2
23-Jan-15	28.1	2.2			893	16.7
19-May-15	28.0	-0.4	32.3		923	3.4
30-Jul-15	27.5	-1.8	31.7	-1.9	940	1.8
29-Oct-15	26.8	-2.5	30.7	-3.2	940	0.0
8-Aug-16	24.0	-10.4	27.8	-9.4	960	2.1
28-Oct-16	23.8	-0.8	27.5	-1.1	945	-1.6
29-Jan-17	23.8	0.1	27.5	0.1	950	0.5
16-May-17	23.8	0.0	27.5	0.0	940	-1.1

Recommendation History



APPENDIX I

JM Financial Institutional Securities Limited

Corporate Identity Number: U65192MH1995PLC092522
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Rating	Meaning
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Sell	Price expected to move downwards by more than 10%

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