Godrej Consumer Products

Improving business visibility

Consumer Goods	Sharekhan code: GODREJCP	Company Update

3R MATRIX	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)	✓		

\+ Positive = Neutral - Negative

Reco/View	Change
Reco: **Buy**	↔
CMP: **Rs. 706**	
Price Target: **850**	↑

↑ Upgrade ↔ Maintain ↓ Downgrade

Company details

Market cap:	Rs. 72,176 cr
52-week high/low:	Rs. 772/425
NSE volume: (No of shares)	12.5 lakh
BSE code:	532424
NSE code:	GODREJCP
Free float: (No of shares)	37.6 cr

Shareholding (%)

Promoters	63.2
FII	26.8
DII	3.2
Others	6.8

Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	3.6	1.7	38.9	9.3
Relative to Sensex	1.0	-15.8	13.7	3.4

Sharekhan Research, Bloomberg

Summary

- Reiterate Buy on Godrej Consumer Products (GCPL) with a revised price target of Rs. 850. Discounted valuations of 37x/32x FY2022E/23E EPS to large peers, long-term growth prospects and focus on strengthening balance sheet make it a better play in the FMCG space.
- Household Insecticides will maintain good run in domestic market led by share gains and better penetration in rural markets; soaps regained growth momentum on improved supply and strong traction in key brands.
- Africa has recovered from lows with the region quickly exiting the pandemic situation; operational performance to be better in Q2.
- New leadership's focus on driving growth through faster innovations, cross pollination and shortening working capital cycle augurs well.

Godrej Consumer Products (GCPL) clocked relatively better numbers in Q1FY2021 compared with other consumer goods companies, driven by a strong recovery in Household Insecticides (HI) category in India (27% growth). Operating performance is expected to improve in Q2FY2021 with domestic soaps segment regaining growth momentum largely led by improvement in supply chain and micro-market initiatives undertaken by GCPL to gain market share. The HI category's growth would normalise to low-double digits on back of better demand. Hygiene products continue to get good traction in the domestic market and hence contribution of new products would sustain at 4-5% with growth in the mid-teens. On the international front, Indonesia continued to clock good performance till July-August. However, the impact of localised lockdowns in key markets (including Jakarta) needs to be keenly monitored in the coming days. Africa meanwhile quickly recovered from the pandemic and with opening up of economies in key countries such as Kenya, Nigeria and South Africa, GPCL's performance in the region is also improving sequentially. Though raw material prices have remained volatile, the management is confident of achieving higher operating margins (OPM) on y-o-y basis on the back of several initiatives (including stringent ad-spends) which might lead to a cost saving of 400-500 bps. Some savings might be ploughed back to consumers in the form of promotional offerings/discounts. OPM is likely to expand by ~150 bps over FY2020-23E to 23%. The company is focusing on reducing working capital through efficient supply chain management, closely working with channel partners and bringing facilities closer to the market. The benefits of such measures would be seen in the coming years, which will help in improving cash flows and reducing debt on books (company maintained target of reducing debt by Rs. 200-250 crore per annum). Overall, we expect GCPL's revenue and PAT to grow at a CAGR of 9.3% and 16% over FY2020-23 (FY2021 revenue growth is expected to be low due to COVID-led disruptions).

Our Call

View: Retain Buy with revised price target of Rs. 850: Market share gains in HI category (both in India and Indonesia); sustained innovation (hygiene products gaining good traction), cross-pollination (plans to launch HI products of the Indian basket in Africa soon) and expansion in distribution network are some key growth levers for GCPL in medium to long term. We have introduced FY2023E estimates in this note. We expect GCPL's revenue and PAT to clock a CAGR of 9% and 16% over FY2020-23. The stock is trading at discounted valuation of 37x/32x its FY2022E23E earnings which is at a 20-22% discount to large peers such as HUL. We maintain our Buy recommendation on the stock with a revised price target of Rs. 850.

Key risk

Any slowdown in the growth of HI business and slow recovery in performance of the Africa business would act as a key risk to our earnings estimates.

Valuation (consolidated) Rs cr

Particulars	FY19	FY20	FY21E	FY22E	FY23E
Revenue	10,314	9,911	10,606	11,712	12,938
OPM (%)	20.7	21.6	21.8	22.7	23.1
Adjusted PAT	1,479	1,462	1,662	1,975	2,276
Adjusted EPS (Rs.)	14.5	14.3	16.3	19.3	22.3
P/E (x)	48.8	49.3	43.4	36.5	31.7
P/B (x)	9.9	9.1	8.4	7.5	6.6
EV/EBIDTA (x)	35.7	35.3	32.7	28.3	25.0
RoNW (%)	21.9	19.3	20.2	21.8	22.3
RoCE (%)	17.5	16.6	17.3	19.3	20.5

Source: Company; Sharekhan estimates

Key highlights of our interaction with Mr. Sameer Shah, CFO - India, SAARC & Head Investor Relations

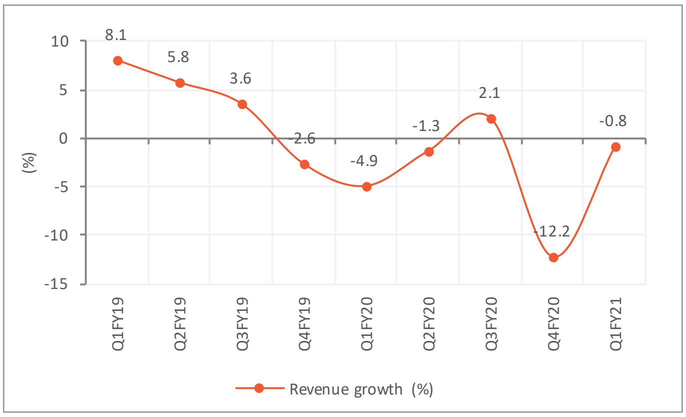
- **Soap sales revive:** Revenue of the domestic soaps category had declined by 2% y-o-y in Q1FY2021 mainly affected by lockdown in the initial part of the quarter, impacting demand. A good revival was seen as supply chain challenges ended. New launches such as Godrej Protekt health soap and Cinthol Health+ range under the health and hygiene categories are scaling up fast and gaining good traction. A continued focus on health and hygiene categories, scale-up of the Protekt brand, widening of distribution reach and micro-marketing initiatives will help to gain market share and drive growth in the medium term.
- **Hair colour segment is recovering gradually:** Revenue from hair colour products declined by 18% y-o-y in Q1FY2021, as this category is discretionary in nature and faced the brunt of the lockdown in April. Sequential improvement was witnessed in hair colour segment as most of the products are at the bottom-of-pyramid price points. With the unlocking, people have started to move out and usage of personal care category products has increased sequentially. Godrej Expert Easy 5-minute shampoo hair colour is performing well post the national scale-up. Godrej Expert Rich Crème continues to perform well by leveraging Do-It-Yourself (DIY) trends through influencers. Given its discretionary nature, the category would take some time to fully recover.
- **Growth in HI to stabilise:** The HI category saw strong resurgence registering a strong growth of 27% y-o-y in Q1FY2021, driven by strong underlying consumer demand in electrical and burning product formats. The mid-20% kind of growth rate seen in the HI category will normalise in the coming quarters and would stabilise in the near term. Growth was witnessed across board in both burning and liquid formats, which is expected to sustain. The recently-launched Good Knight Gold Flash liquid vaporiser continues to receive an excellent response after its national scale-up. Receding threat of illegal incense sticks that were affected by supply chain disruptions will help GCPL gain market share in the HI category. Increased penetration, especially in rural, penetration in other formats, innovation, market share gains and distribution expansion will help drive growth in teh HI segment in the medium to long term.
- **Hygiene portfolio gained good traction:** The company scaled up its Godrej Protekt brand to a complete hygiene portfolio in Q1FY2021 which comprises kitchen protection, personal protection and home protection. The company also added health & hygiene variants in other categories such as air-fresheners and sanitisers, fabric sanitisers and bathroom and floor cleaners to make the category more relevant. GCPL registered a strong 15% growth in hygiene products in Q1FY2021, driven by innovation as the company launched 45 products in this portfolio, across geographies. The hygiene portfolio is performing well with good traction received by the new launches. The company already had base level portfolio in the hygiene segment and expects the contribution from the portfolio to stabilise at 4-5% of total revenues.
- **Growth momentum to continue in Indonesia;** sequential improvement seen in Africa: International business revenue declined by 9% y-o-y in Q1FY2021. Indonesia posted better performance in Q1FY2021 and business is stable. The company gained market share in HI in Indonesia. The newly-launched Saniter range of health & hygiene products is gaining strong traction. Sequential improvement was witnessed in Africa as the region is out of lockdown, channels have improved and consumers are buying again. Recovery was faster than India in places such as South Africa, Nigeria, etc. GCPL is expecting significant competitive advantage in the region and performance is expected to be much better in Q2. Strategies are largely in place by the new head in Africa to drive sustainable growth. Latin America is looking good and the company's strategy is to focus on profitability over growth.

Other highlights

- GCPL had witnessed resilient performance with a 3% growth in domestic volumes and 5% growth in India and Indonesia each in Q1FY2021. Demand improved sequentially and the company has started operating at near-normal levels.
- The company has started operating at optimum capacity and availability of products has improved. Products that were earlier available in only modern trade and e-Commerce channels have now been extended to general trade as well as chemists.
- The company is looking to ramp-up capacity for the powder to liquid hand wash product.
- No significant capex is expected to be incurred in the coming quarters.
- Working capital cycle is expected to remain stable. Inventories might increase to ensure better availability. However, efficient supply chain management, working with channel partners, bringing vendors closer to facilities and bringing facilities closer to markets will keep the core working capital stable in the near to medium term.
- The company has rationalised SKUs in Africa. However, there is no intention of rationalising the portfolio in India.
- Gross margins might see some volatility in the coming quarters. However, GCPL's focus on reducing ad-spends and other cost-saving measures will help overall operating margins to sustain. The company is expecting a cost saving target of 4-5% of sales in the near term in the India business.
- Debt has come down from March 2020 levels and the management has maintained its debt reduction target of Rs. 60-70 crore every quarter.

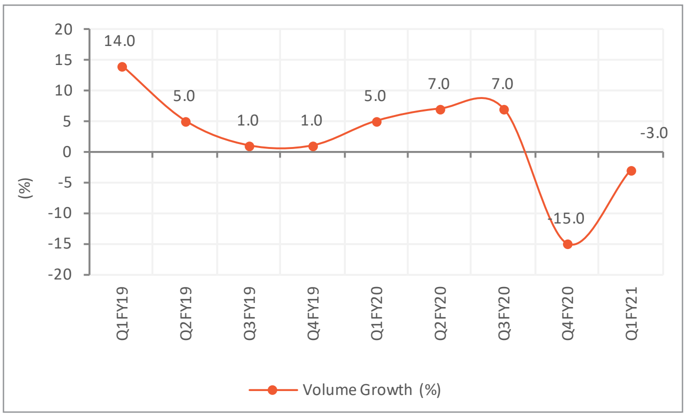
Financials in charts

Revenue recovered in Q1FY2021



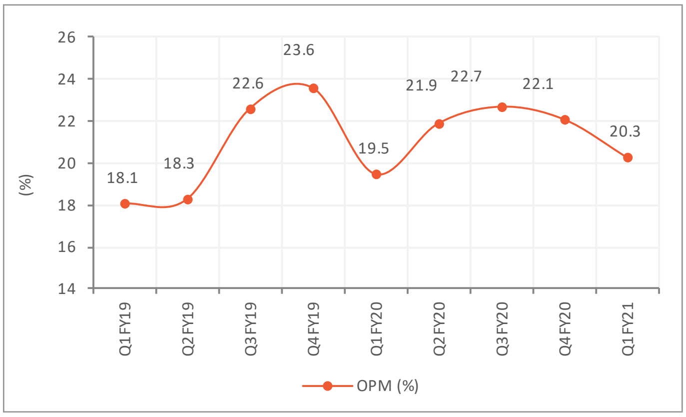
Source: Company, Sharekhan Research

Volumes declined by 3% in Q1FY2021



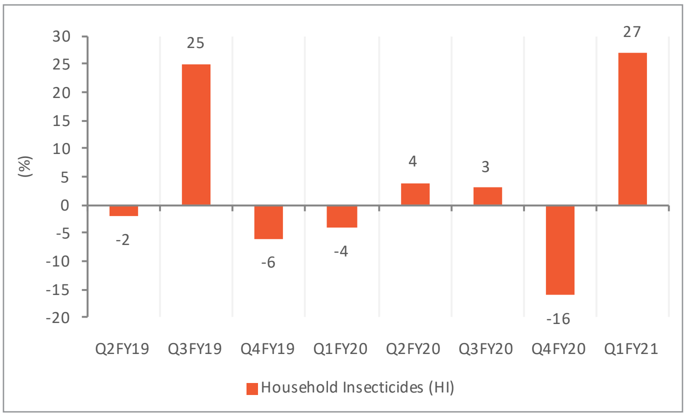
Source: Company, Sharekhan Research

OPM improved y-o-y to 20.3% in Q1FY2021



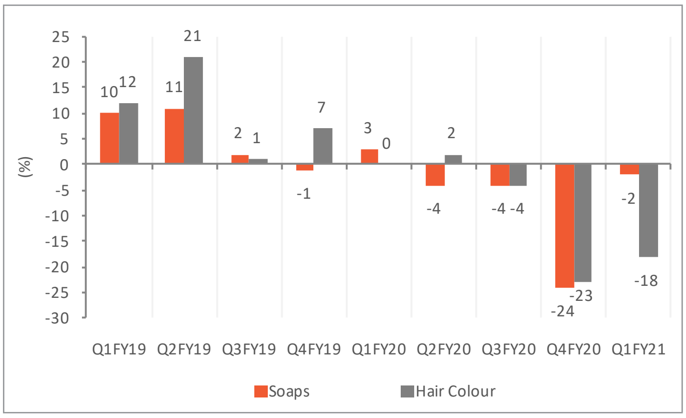
Source: Company, Sharekhan Research

HI category witnessed strong growth in Q1FY2021



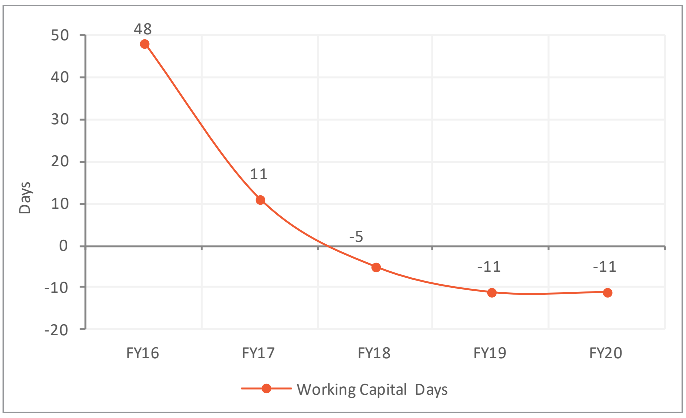
Source: Company, Sharekhan Research

Soaps saw recovery, Hair colour was subdued



Source: Company, Sharekhan Research

Working capital cycle remained stable



Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector View – Supply chain back to normal; HI category becoming more regulated

Consumer goods companies saw strong revival in June with production and supply recovering to 90% of pre-COVID levels. With a strong pick in rural demand, general trade normalising in the business and higher sales through online channels, we expect normalisation of business performance from Q2FY2021. The domestic HI category is getting more regulated with the government increasing awareness about illegal incense sticks through various media platforms and promoting use of branded products. This will help branded players in HI category gain market share from illegal players. This will also help the penetration of HI category to improve in the rural market. 1) Sustained demand for branded foods, hygiene and HI products; 2) pick-up in rural demand; 3) new launches and 4) focus on expansion of distribution reach are some of the near-term growth catalysts. Most of the key input prices (barring palm oil, raw tea and coffee) have remained benign. This along with cost-saving initiatives would help consumer goods companies post better margins in the coming quarters.

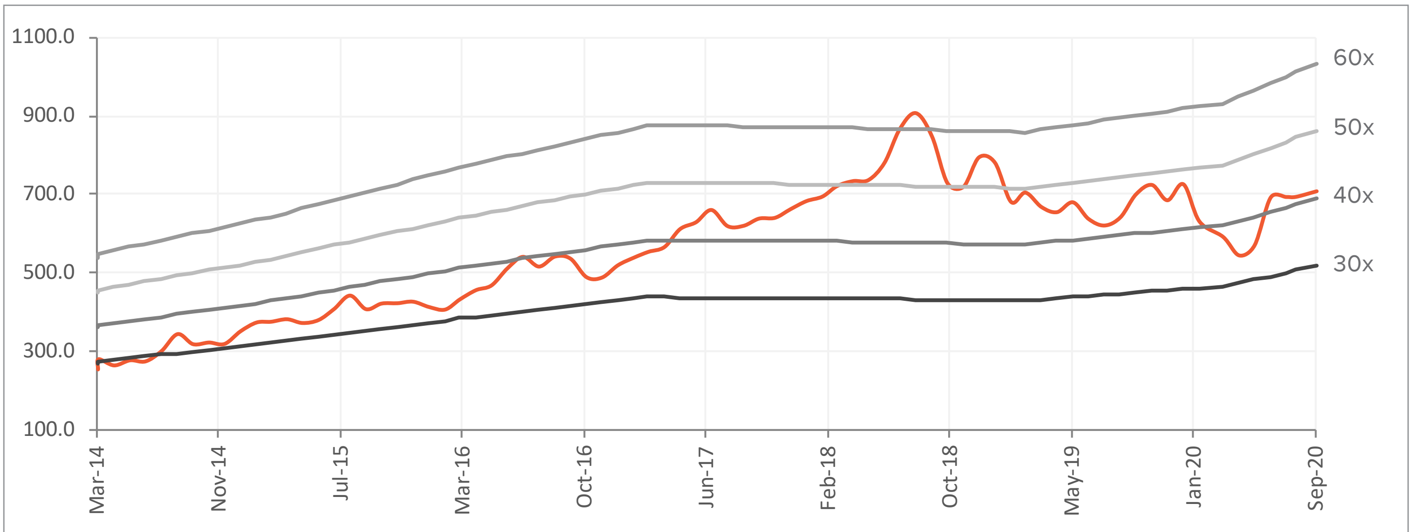
■ Company Outlook – Near-term growth prospects intact

Q2FY2021 performance is expected to be much better than Q1 driven by recovery in the core domestic soaps category; sustained growth in HI category, strong traction in hygiene products and recovery in Africa. Cost-saving initiatives and judicious ad-spends would help OPM remain high y-o-y despite volatile raw material prices. The business fundamentals to get normalised by Q3 and strong recovery is anticipated in FY2022. A better revenue mix would help consistent improvement in OPM (likely to reach 23% by FY023). This along with better working capital management would help cash flows to improve in the coming years. The company aims to reduce debt by Rs. 200-250 crore per annum.

■ View – Retain Buy with revised price target of Rs. 850

Market share gains in HI category (both in India and Indonesia); sustained innovation (hygiene products gaining good traction), cross-pollination (plans to launch HI products of the Indian basket in Africa soon) and expansion in distribution network are some key growth levers for GCPL in medium to long term. We have introduced FY2023E estimates in this note. We expect GCPL's revenue and PAT to clock a CAGR of 9% and 16% over FY2020-23. The stock is trading at discounted valuation of 37x/32x its FY2022E23E earnings which is at a 20-22% discount to large peers such as HUL. We maintain our Buy recommendation on the stock with a revised price target of Rs. 850.

One-year forward P/E (x) band



Source: Sharekhan Research

Peer Comparison

Particulars	P/E (x)			EV/EBIDTA (x)			RoCE (%)		
	FY20	FY21E	FY22E	FY20	FY21E	FY22E	FY20	FY21E	FY22E
Hindustan Unilever	66.7	58.3	46.9	47.3	41.0	35.0	105.2	39.7	28.4
Dabur India	58.6	54.4	43.2	49.0	44.1	34.7	27.0	26.5	29.5
Marico India	44.0	42.6	35.5	31.9	30.4	25.5	41.3	40.7	43.1
Godrej Consumer Products	49.3	43.4	36.5	35.3	32.7	28.3	16.6	17.3	19.3

Source: Company, Sharekhan estimates

About company

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 colour and household insecticides. The company's power brands include Godrej No.1 soap, Godrej expert range of hair colours and Good Knight. GCPL operates internationally in Indonesia, Latin America and GAUM (Africa, U.S. 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). The company has a leadership position in most categories in the domestic and international markets. Sustained innovation, cross pollination, enhanced distribution reach and foray into new categories have remained the company's key growth pillars. The company has started seeing recovery in key domestic categories such as HI and international markets (including Indonesia and Africa), which will drive earnings growth in the near term.

Key Risks

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

Additional Data

Key management personnel

Nisaba Godrej	Chairperson & Managing Director
Adi Godrej	Chairman
V Srinivasan	CFO and Company Secretary

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	First State Investments ICVC	2.7
2	Temasek Holdings Pte Ltd	2.5
3	First State Global Umbrella Fund	2.1
4	Capital Group Cos Inc	1.4
5	Vanguard Group Inc	1.3
6	Arisaig India Fund Limited	1
7	Republic of Singapore	1
8	BlackRock Inc	1
9	Mitsubishi UFJ Financial Group Inc	0.7
10	Kotak Mahindra Asset Management Co	0.7

Source: Bloomberg

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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