Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

# Godrej Consumer Products Ltd

## Domestic HI & Indonesia biz recovering well

| Consumer Goods | Sharekhan code: GODREJCP |
|---|---|
| **Reco/View: Buy** ↔ | CMP: **Rs. 972** |
| | Price Target: **Rs. 1,100** ↑ |

↑ Upgrade ↔ Maintain ↓ Downgrade

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

+ Positive = Neutral – Negative

**What has changed in 3R MATRIX**

| | Old | | New |
|---|---|---|---|
| RS | | ↔ | |
| RQ | | ↔ | |
| RV | | ↔ | |

**ESG Disclosure Score** NEW

ESG RISK RATING 26.88
Updated Mar 08, 2023

Medium Risk

| NEGL | LOW | MED | HIGH | SEVERE |
|---|---|---|---|---|
| 0-10 | 10-20 | 20-30 | 30-40 | 40+ |

*Source: Morningstar*

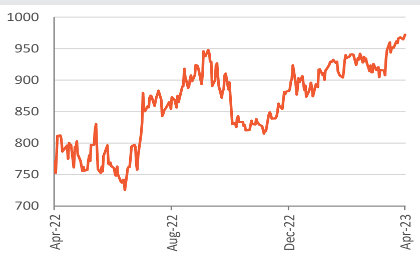
**Company details**

| | |
|---|---|
| Market cap: | Rs. 99,406 cr |
| 52-week high/low: | Rs. 973 / 709 |
| NSE volume: (No of shares) | 10.4 lakh |
| BSE code: | 532424 |
| NSE code: | GODREJCP |
| Free float: (No of shares) | 37.6 cr |

**Shareholding (%)**

| | |
|---|---|
| Promoters | 63.2 |
| FII | 24.4 |
| DII | 6.7 |
| Others | 5.6 |

**Price chart**




**Price performance**

| (%) | 1m | 3m | 6m | 12m |
|---|---|---|---|---|
| Absolute | 7.0 | 7.2 | 11.3 | 26.9 |
| Relative to Sensex | -0.9 | -1.1 | 2.5 | -0.8 |

*Sharekhan Research, Bloomberg*

**Summary**

- We re-iterate our Buy rating on Godrej Consumer Products (GCPL) with revised PT of Rs. 1,100. Improving growth prospects in key markets and discounted valuations against peers at 44.1x/37.5x its FY24E/25E EPS makes it's a good pick in the consumer goods space.
- GCPL is expected to achieve double-digit revenue growth in Q4FY2023 with good recovery in the domestic household insecticide (HI) category and good recovery in the Indonesia business.
- Gross margin and OPM are expected to improve on y-o-y basis due to lower input prices (palm oil prices are down by 36% y-o-y); OPM is expected to be around 18.0-18.5% in Q4.
- Key medium-term growth drivers for double digit revenue and earnings growth are 1) recovery in the domestic HI business 2) Indonesia business growing consistently and 3) Africa business growing in double digits.

**Godrej Consumer Products (GCPL) provided a glimpse of its improved performance in its pre-quarter update for Q4FY2023. Its business performed exceptionally well and delivered double-digit revenue growth beating its own expectation with steady consumer demand in domestic market. Q4FY23 will be the first quarter of double digit revenue growth (with volume growth of 4-5%) after six quarters of single-digit revenue growth. The growth was largely driven by double-digit growth in the domestic business and recovery in the Indonesia business. Lower input prices (including palm oil prices) will help the gross margins and OPM to improve on y-o-y basis during the quarter. Overall, we expect the company to deliver low double-digit revenue growth, while operating profit is expected to grow in high teens with margin expansion.**

- **Broad-based growth across categories in Q4:** GCPL expects broad-based double-digit revenue growth in Q4FY2023 with domestic business revenues growing in double digits, driven by mix of double-digit volume and value growth during the quarter. Both home care (including household insecticides) and personal care businesses registered double digit volume and value growth during the quarter. On the international front, Indonesia is expected to post recovery in the performance, while Africa business is expected to post high single-digit revenue growth affected by elections and impact of demonetisation in Nigeria. Overall, we expect consolidated revenues to grow by 11-12% in Q4FY2023.
- **Lower input prices to drive margins:** Palm oil prices were down by 36% y-o-y in Q4FY2023. This along with correction in the input prices would help GCPL's gross margins to expand on y-o-y basis. Though the ad spends are expected to be higher, the OPM is expected to remain high y-o-y. We expect OPM to be around 18.5% (40 bps higher y-o-y) and the operating profit to grow by 18% y-o-y in Q4. However, high incidence of tax will lead to high single digit PAT growth during the quarter.
- **Medium term drivers in place to achieve consistent growth:** GCPL's India business is expected to grow in low double-digit largely driven by improved volume growth in key categories. With corrective measures in place and improving macro environment, the Indonesia revenue growth is expected to improve in the coming quarters. The margins of the Indonesia business will gradually improve on the back of a better mix and operating leverage. Africa business will maintain double-digit revenue growth while EBIDTA margins are expected to reach mid-teens over the next two years. Overall, we expect GCPL's earnings to consistently grow in double-digit over the next two years.

**Our Call**

**View – Maintain Buy with a revised PT of Rs. 1,100:** GCPL registered good all-round recovery in the performance in Q4FY2023 with key businesses such as the domestic HI and Indonesia business registering sequential improvement in the performance. With strategies in place, management is confident of posting gradual recovery in sales in the coming quarters and targets to achieve double-digit growth over the two to three years (largely driven by improved sales volume). The company targets consistent improvement in OPM through premiumisation and operating efficiencies in the medium to long run. The stock is currently trading at attractive valuations of 44.1x/37.5x its FY2024E/FY2025E earnings. We maintain our Buy recommendation on the stock with a revised price target of Rs. 1,100.

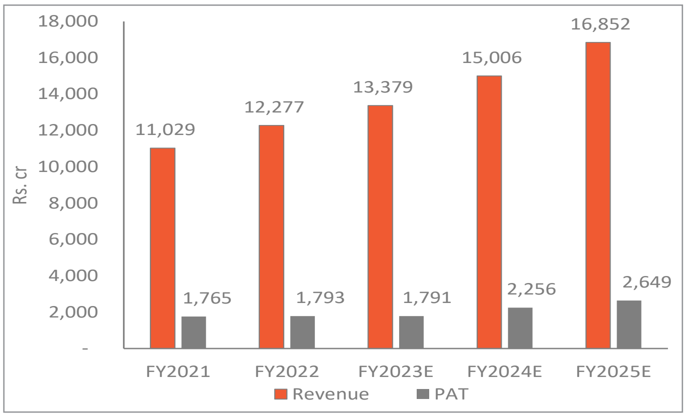
**Valuations (Consolidated)** Rs cr

| Particulars | FY21 | FY22 | FY23E | FY24E | FY25E |
|---|---|---|---|---|---|
| Revenue | 11,029 | 12,277 | 13,379 | 15,006 | 16,852 |
| OPM (%) | 22.2 | 20.3 | 18.3 | 20.2 | 20.8 |
| Adjusted PAT | 1,765 | 1,793 | 1,791 | 2,256 | 2,649 |
| Adjusted EPS (Rs.) | 17.3 | 17.5 | 17.5 | 22.1 | 25.9 |
| P/E (x) | 56.3 | 55.4 | 55.5 | 44.1 | 37.5 |
| P/B (x) | 10.5 | 8.6 | 7.9 | 7.1 | 6.3 |
| EV/EBITDA (x) | 41.4 | 40.5 | 41.1 | 33.0 | 28.1 |
| RoNW (%) | 20.4 | 17.1 | 14.9 | 17.0 | 17.8 |
| RoCE (%) | 18.3 | 17.3 | 15.9 | 18.7 | 20.0 |

*Source: Company; Sharekhan estimates*

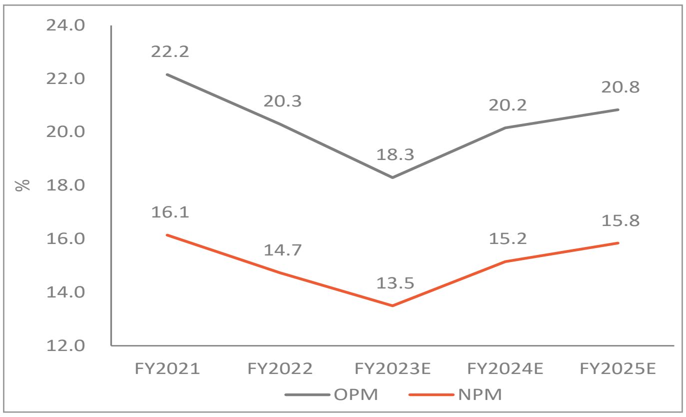
## Financials in charts

### Steady growth in revenue and PAT



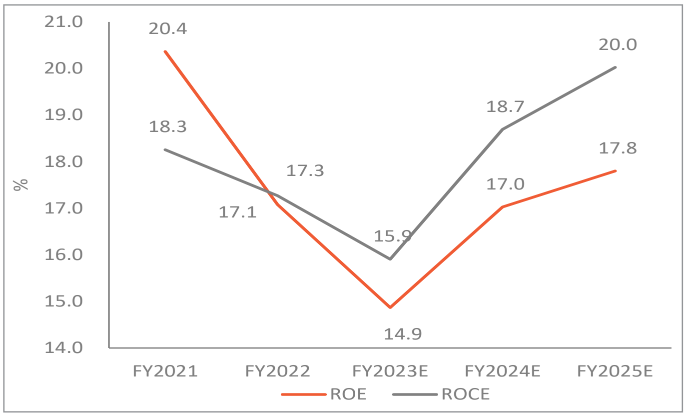

*Source: Company, Sharekhan Research*

### Margins to improve from current levels



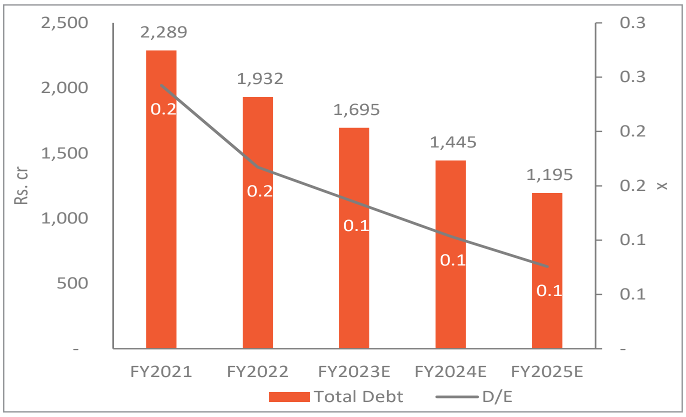

*Source: Company, Sharekhan Research*

### Return ratios to rise going ahead



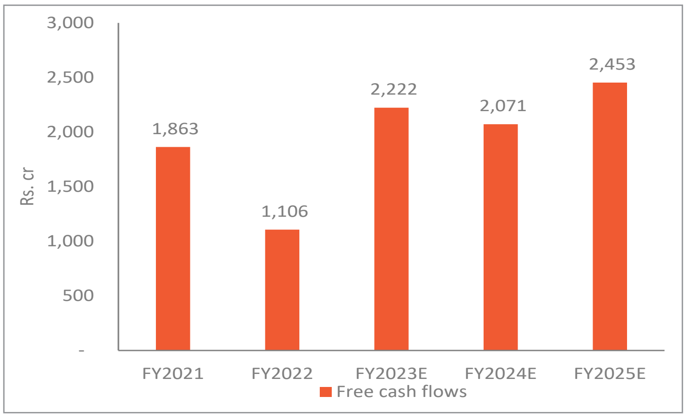

*Source: Company, Sharekhan Research*

### Improvement in debt position



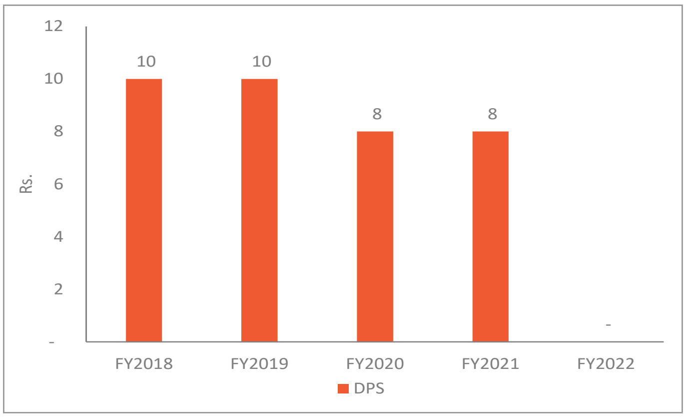

*Source: Company, Sharekhan Research*

### Significant free cash flow generation




*Source: Company, Sharekhan Research*

### Trend in dividend per share




*Source: Company, Sharekhan Research*

## Outlook and Valuation

### ■ Sector View – Rural recovery key for better growth ahead

A recovery in rural demand is key for consumer goods companies to post recovery in volume growth in the quarters ahead. Urban demand remained resilient with a good pick-up in modern trade, while the momentum in general trade continued to remain strong for the past 2-3 quarters. Out-of-home, packaged foods and edible oil categories witnessed good growth in recent times and will maintain momentum in the coming quarters. With the mercury rising in most parts of the country, demand for summer products is on the rise as trade channels are building up the inventory prior to the season. On the other hand, stable raw-material prices post the recent correction in some of the key inputs (including crude oil and vegetable oils) will help margins consistently improve in the coming quarters. Overall, we expect Q4FY2023 to be better compared to Q3 and the momentum to improve at the start of the next fiscal.

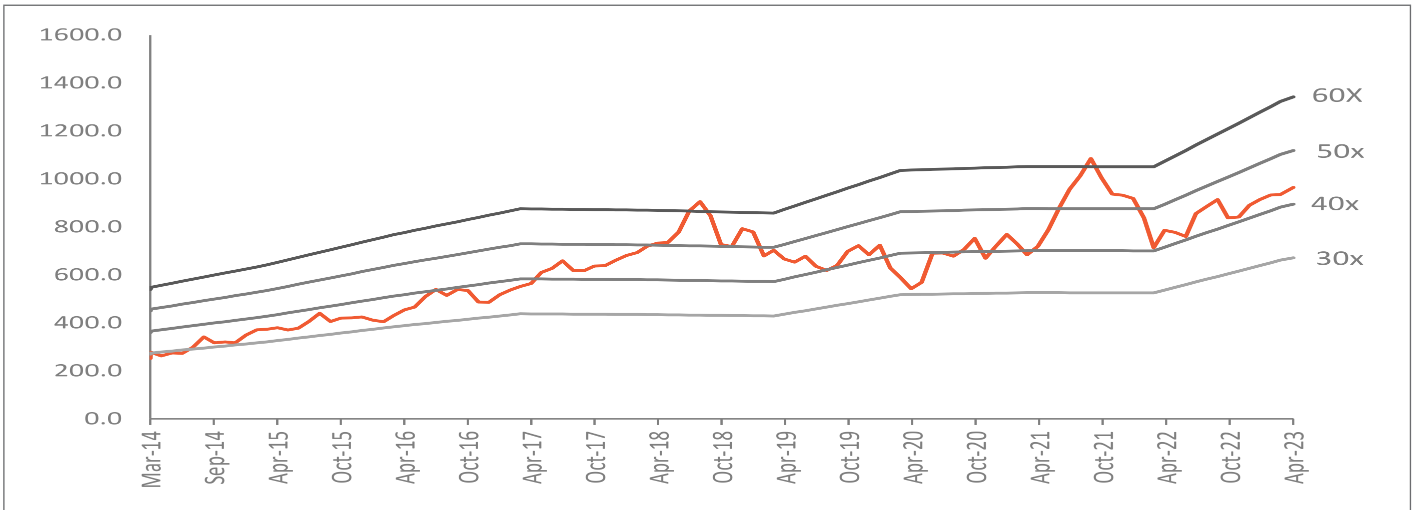
### ■ Company Outlook – Change in leadership likely to drive consistent growth in the long run

Under the new leadership of Mr. Sudhir Sitapati, the company will focus on achieving consistent double-digit revenue growth in the medium term. Improved penetration of HI in rural markets, sustained double-digit growth in Africa business, and recovery in Indonesia business are key medium-term revenue growth drivers for the company. The decline in key input prices (including palm oil and packaging material) would help in margin improvement in Q4. The company will pass on some benefits to consumers to improve sales volume. Management expects to maintain OPM on a y-o-y basis at around 20%. The management targets OPM to remain at 20-22% in the medium term.

### ■ Valuation – Maintain Buy with a revised PT of Rs. 1,100

GCPL registered good all-round recovery in the performance in Q4FY2023 with key businesses such as the domestic HI and Indonesia business registering sequential improvement in the performance. With strategies in place, management is confident of posting gradual recovery in sales in the coming quarters and targets to achieve double-digit growth over the two to three years (largely driven by improved sales volume). The company targets consistent improvement in OPM through premiumisation and operating efficiencies in the medium to long run. The stock is currently trading at attractive valuations of 44.1x/37.5x its FY2024E/FY2025E earnings. We maintain our Buy recommendation on the stock with a revised price target of Rs. 1,100.

**One-year forward PE band**




*Source: Sharekhan Research*

**Peer Comparison**

| Companies | P/E (x) | | | EV/EBITDA (x) | | | RoCE (%) | | |
|---|---|---|---|---|---|---|---|---|---|
| | FY22 | FY23E | FY24E | FY22 | FY23E | FY24E | FY22 | FY23E | FY24E |
| Hindustan Unilever | 68.6 | 63.5 | 53.6 | 48.0 | 44.3 | 37.7 | 24.1 | 25.9 | 30.1 |
| Dabur India | 53.2 | 50.3 | 40.5 | 43.1 | 41.9 | 34.0 | 26.3 | 25.6 | 29.8 |
| Godrej Consumer Products | 55.4 | 55.5 | 44.1 | 40.5 | 41.1 | 33.0 | 17.3 | 15.9 | 18.7 |

*Source: Company; Sharekhan Research*

## About the company

GCPL is a leading emerging market company with a turnover of more than Rs. 12,000 crore. The group enjoys the patronage of 1.2 billion consumers globally across businesses. GCPL is present in key product categories such as soaps, hair colour, and HI. 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 AUM (Africa, US, 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. Under the new leadership, the immediate focus of the company is to fill the gaps to achieve sustainable double-digit revenue growth in the medium term. Increased penetration, cross-pollination, simplifying business in key markets, and increased distribution are some of the key growth drivers in the medium term. Premiumisation, better revenue mix, and operating efficiencies would drive margins in the long run.

## 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**

| | |
|---|---|
| Adi Godrej | Chairman, Godrej Group |
| Nisaba Godrej | Chairperson |
| Sudhir Sitapati | Managing Director and CEO |
| Sameer Shah | Chief Financial Officer |
| Rahul Botadara | Company Secretary & Compliance Officer |

*Source: Company Website*

**Top 10 shareholders**

| Sr. No. | Holder Name | Holding (%) |
|---|---|---|
| 1 | First State Investments ICVC | 2.9 |
| 2 | BlackRock Inc | 1.8 |
| 3 | Vanguard Group Inc | 1.4 |
| 4 | Temasek Holdings Pte Ltd | 1.3 |
| 5 | Capital Group Cos | 1.2 |
| 6 | Republic of Singapore | 1.1 |
| 7 | EuroPacific Growth Fund | 1.0 |
| 8 | Republic of Singapore | 1.1 |
| 9 | Mitsubishi UFJ Financial Group Inc | 0.8 |
| 10 | Norges Bank | 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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