Colgate-Palmolive India

BSE SENSEX 40,165 | **S&P CNX** 11,891

CMP: INR1,534 TP: INR1,815 (+18%) Buy

Brushing up on some history

Revisiting successful impact of management change in India listed consumer MNCs

- Colgate-Palmolive India (CLGT) saw a change at the managing director (MD) level from 1st Aug'19. We believe that this change is promising based on prior examples seen at listed consumer MNCs in India. CLGT's peers such as HUVR, NEST and PGHH had witnessed significant underperformance in the past, but were revitalized with the advent of a new MD/CEO.
- Historically, despite taking its eyes off the ball on several occasions, CLGT has managed to get back on track. CLGT faced challenges in the form of (a) HUVR launching gel-based toothpaste in the late-1980s, (b) competition from price warriors, such as Ajanta, Amar, etc. in the mid-2000s, and (c) *Sensodyne* launch by GSK in the premium-end of the market in the latter part of that decade. However, CLGT recovered ground and emerged as the dominant market leader.
- Its distribution muscle (CLGT has the best direct reach after HUVR in the personal care business), concentration of ad-spends and having the most extensive category development efforts in the FMCG space provides CLGT with considerable moats to regain growth momentum.
- Notably, company carried out significant capacity expansion during FY14-18 but the latter part of the expansion coincided with a period of considerable underperformance in volumes, which meant significant underutilization of capacities. We believe that CLGT does not need any material capacity addition until FY22. Even a moderate volume momentum recovery should lead to higher gains at the EPS level.
- Further, from our channel checks, we understand that the aggression in terms of visibility and promotions has already commenced early in the new MD's tenure starting with modern trade and likely to expand to general trade later. CLGT's new MD has stated that volume growth/market share gains are the key focus areas for the company even if it impacts near-term profitability.
- Serendipitously, Colgate has emerged as a significant beneficiary of the corporate tax cuts unlike peers Dabur and Patanjali. While HUVR is also a beneficiary of the corporate tax cuts, its gains are spread across several categories. Also, we reckon that as a proportion of HUVR's revenues, oral care's contribution is only in mid-single-digits. Further, the tax cuts are expected to potentially free INR850m/INR1,100m over FY20/FY21. Thus, we believe that CLGT does not need to compromise as much on near-term EBITDA margins as was originally envisaged.
- Post the corporate tax cuts, we had elevated Colgate and Britannia to our top picks (along with HUVR and TTAN) in our note. We remain bullish on CLGT in the medium term given its reasonable valuations (40.9x FY21 EPS, huge discount to MNC peer multiples of 53x-61x), likely escalation in earnings momentum and sharp potential improvement in an already impressive ROCE, Targeting 45x September 2021, we maintain target price of INR1,815.

Stock Info

Bloomberg	CLGT IN
Equity Shares (m)	272
M.Cap.(INRb)/(USDb)	417.3 / 5.9
52-Week Range (INR)	1588 / 1080
1, 6, 12 Rel. Per (%)	-2/28/21
12M Avg Val (INR M)	639
Free float (%)	49.0

Financials Snapshot (INR b)

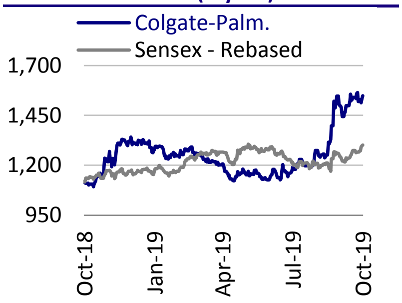
Y/E March	2019	2020E	2021E
Sales	44.6	47.3	53.8
EBITDA	12.4	12.4	15.2
Adj. PAT	7.5	8.2	10.2
Adj. EPS (INR)	27.4	30.1	37.5
EPS Gr. (%)	8.8	9.9	24.5
BV/Sh.(INR)	53.2	50.8	46.5
RoE (%)	50.1	57.9	77.1
RoCE (%)	47.9	54.2	71.6
Payout (%)	84.0	87.0	90.0
Valuations			
P/E (x)	56.0	51.0	40.9
P/B (x)	28.8	30.2	33.0

Shareholding pattern (%)

As On	Sep-19	Jun-19	Sep-18
Promoter	51.0	51.0	51.0
DII	11.6	10.5	13.3
FII	15.5	15.1	13.3
Others	22.0	23.4	22.4

FII Includes depository receipts

Stock Performance (1-year)



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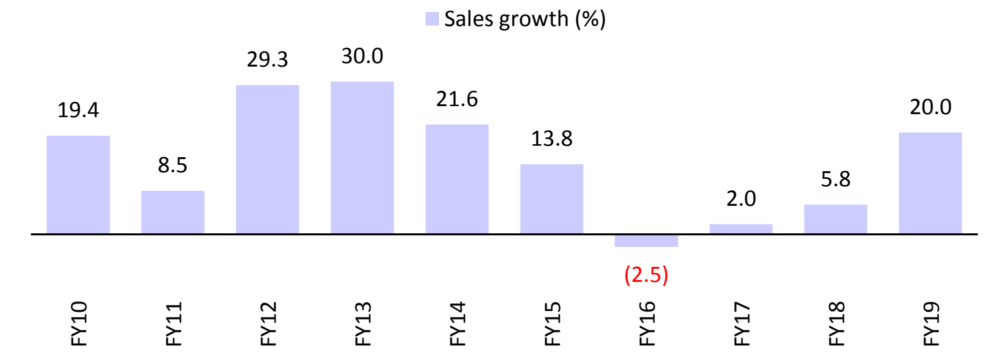
What happened in case of CLGT's other MNC peers?

P&G Hygiene and Healthcare (PGHH)

- The most recent instance of a change at the top level heralding a decisive change in strategy occurred in mid-2018 at PGHH. After Mr. AL Rajwani retired, the then Head of Indonesia, Mr. Madhusudan Gopalan, assumed charge as the new MD of PGHH (along with other P&G entities in India).

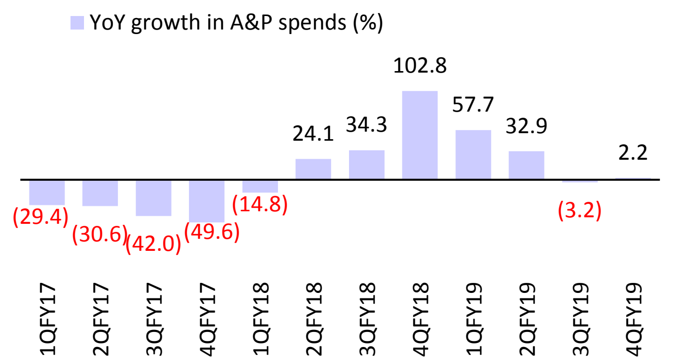
Exhibit 1: PGHH sales came under pressure between FY16- 18



Source: Company, MOFSL

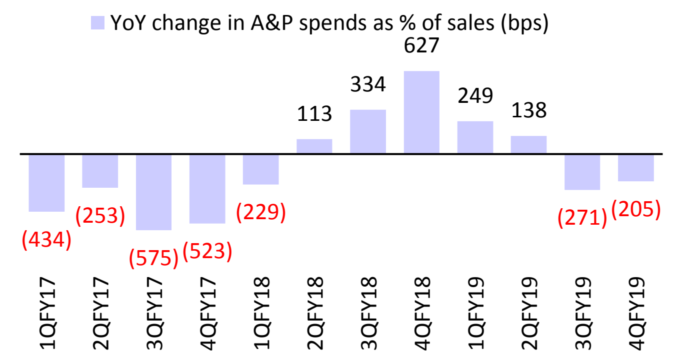
- After several years of impressive sales, growth had begun tapering off in FY17 and FY18. The new management followed an aggressive strategy to revitalize sales growth. We had discussed extensively the key elements of this new strategy in our detailed report in Jan'19; these include:
  - **Distribution expansion:** PGHH expanded the distribution network of *Vicks/Whisper* to 3.5m/2m outlets from 2m/1.4m outlets four years ago with significant thrust in the past two years.
  - **Sharp increase in ad-spends:** There has been a sharp increase in ad-spends to sales as well as absolute ad-spends in recent quarters.
  - 10% price cut was taken in the mid-segment brand *Whisper Choice Ultra.*
  - There were new launches in both *Whisper* and *Vicks*.

Exhibit 2: A&P spends grew sharply 2QFY18 onwards



PGHH has financial year ending June Source: Company, MOFSL

Exhibit 3: A&P spends as a % of sales grew in triple digits after 2QFY18



Source: Company, MOFSL

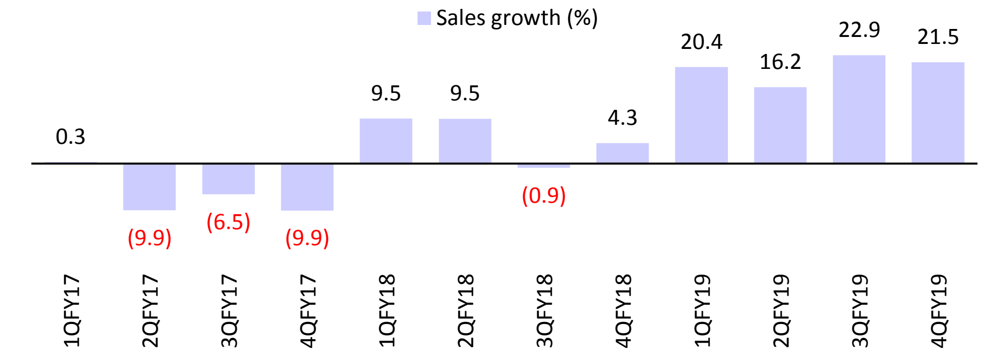
Exhibit 4: New launches in *Whisper* and *Vicks*

Whisper	Vicks
Whisper Choice Aloe Vera	
Whisper Ultra Soft	Vicks BabyRub
Whisper Daily Liners	

Source: MOFSL, Company

- Over the last four quarters, sales growth has taken off sharply. Even taking into account adjusted sales growth (for GST reduction on sanitary napkins) performance is impressive. While this has been at the cost of near-term profitability, notably due to increase in ad-spends, it was also due to absence of input tax credit on various costs. Starting mid-2018, growth has been revitalized and the rewards are likely to be reaped over the next few years.

Exhibit 5: PGHH's reported sales growth has seen a sharp jump in the last four quarters

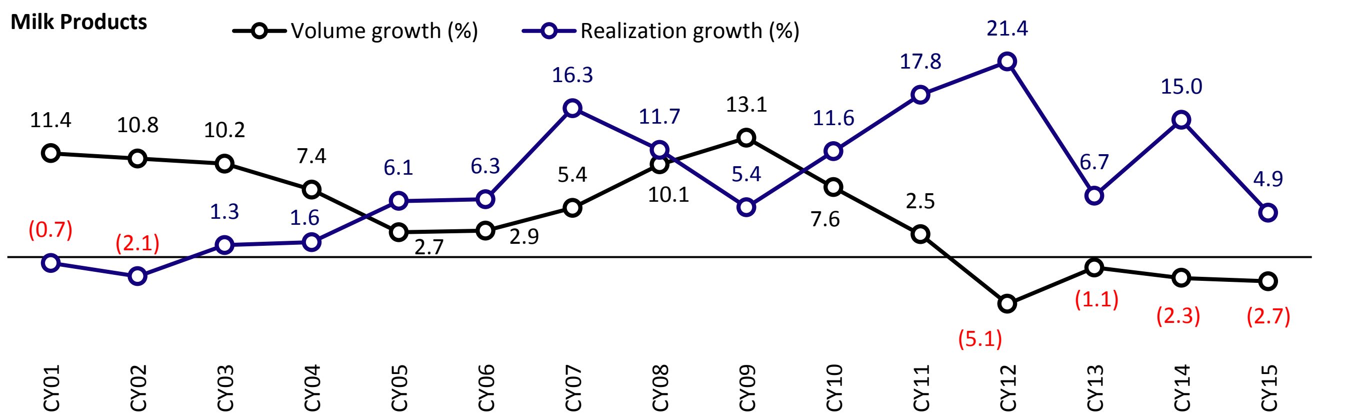


Source: Company, MOFSL

Nestle India

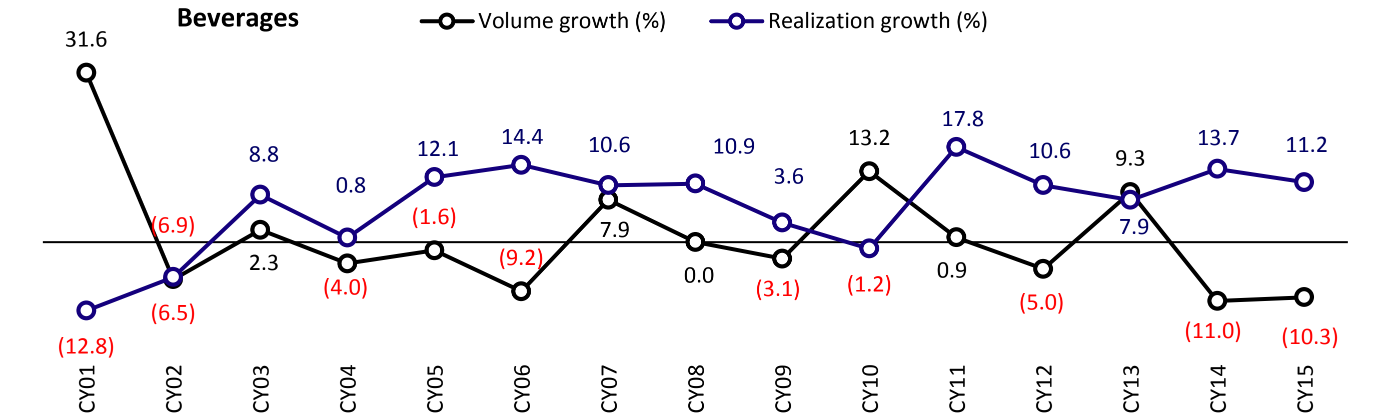
- When Mr. Suresh Narayanan was brought in amidst the *Maggi* crisis in mid-2015, his immediate task was to restore trust with the brand and prevent any impact on Nestle's other brands. His strategy, unveiled in the same year, focused not just on damage control but also encompassed restoring growth, which was moribund in other categories as well over the preceding seven years. Overt emphasis on profitability before his tenure was stunting growth. Barring Prepared Dishes & Cooking Aids, all other segments registered volume decline during CY14-15.

Exhibit 6: Milk products witnessed contraction in volume growth over CY12-15



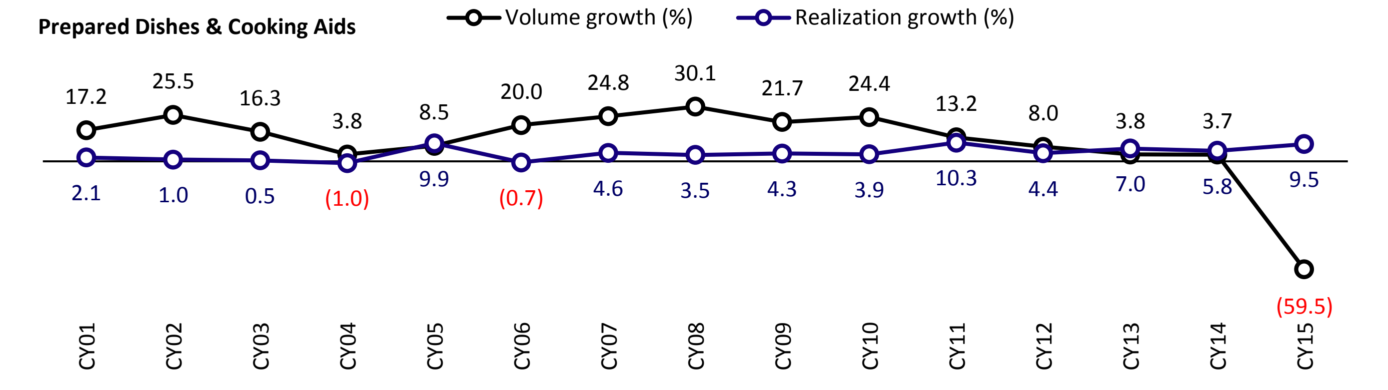
Source: Company, MOFSL

Exhibit 7: Volume growth for beverages sharply contracted during CY14-15



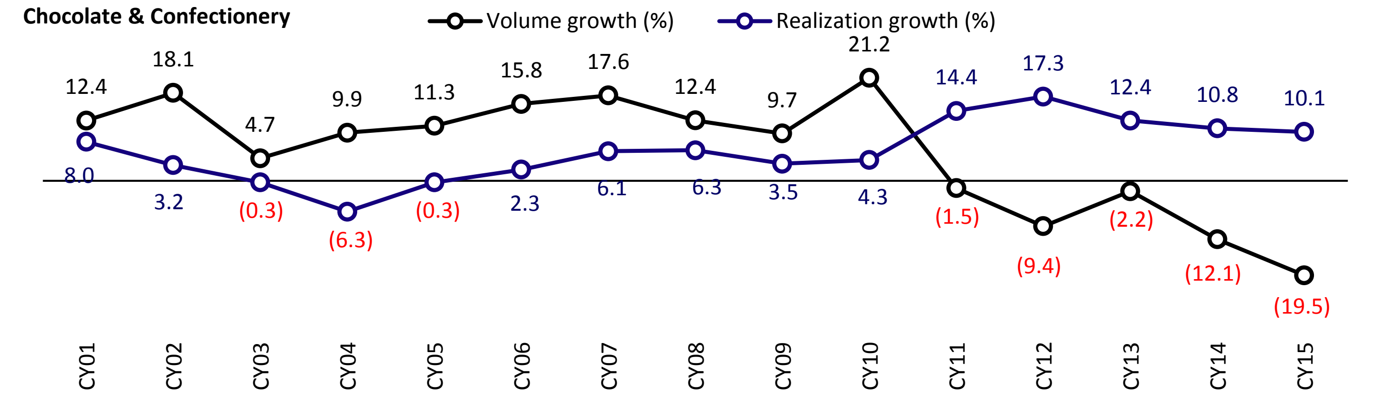
Source: Company, MOFSL

Exhibit 8: Prepared Dishes & Cooking Aids – sole segment that registered volume growth in CY11-14, but was impacted by the *Maggi* crisis in CY15



Source: Company, MOFSL

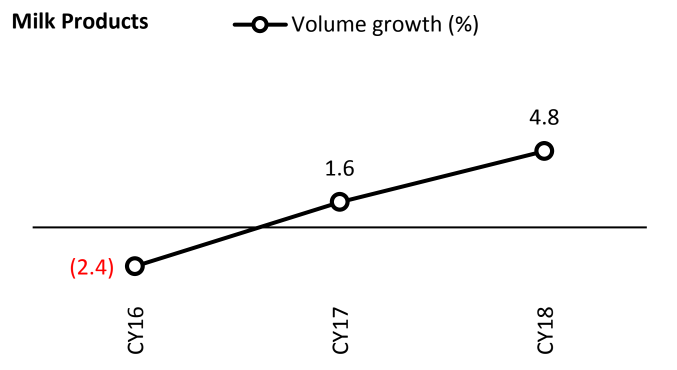
Exhibit 9: Chocolate & Confectionary witnessed volume decline for five consecutive years during CY11-15



Source: Company, MOFSL

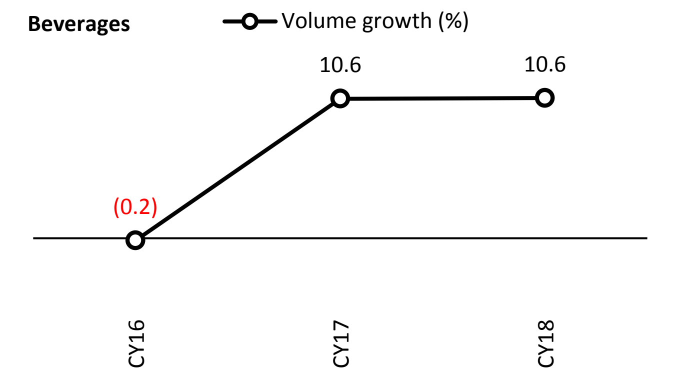
- While the campaign to restore trust back to *Maggi* was remarkably successful, the purview of our exercise is to see how growth was revitalized by management. Mr. Narayanan was successfully able to revitalize volume growth in all four categories, but in stages over the next four years.

Exhibit 10: Milk Product volumes started growing after CY17



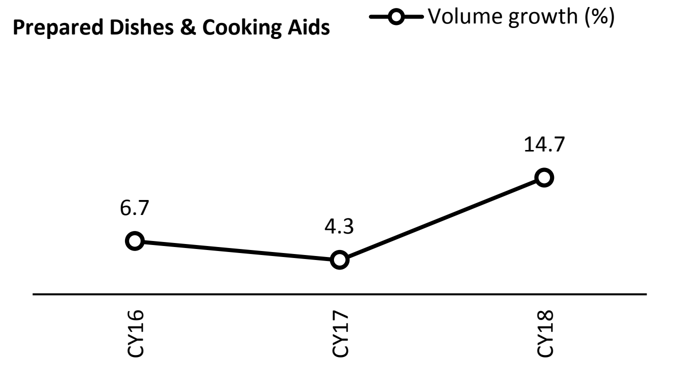
Source: Company, MOFSL

Exhibit 11: Beverage volumes jumped sharply after CY16



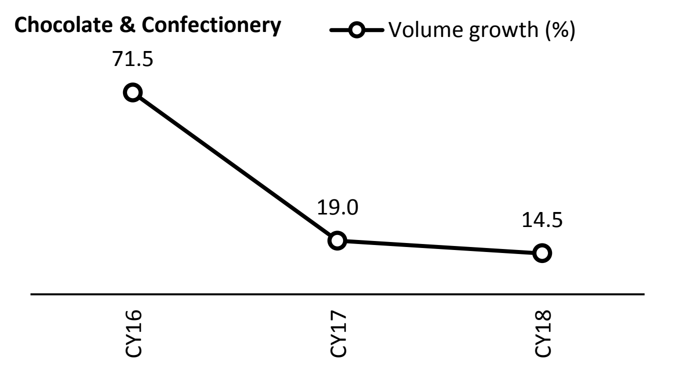
Source: Company, MOFSL

Exhibit 12: Recovered strongly from the *Maggi* crisis



Source: Company, MOFSL

Exhibit 13: Chocolates & Confectionary growing robustly



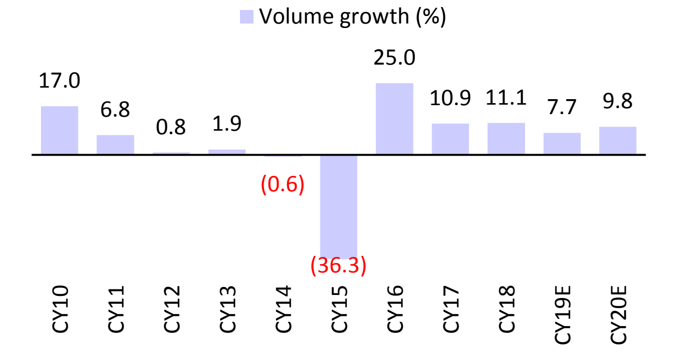
Source: Company, MOFSL

- While CY19 has not witnessed double-digit growth, sales growth of 8.9%/11.2% in 1QCY19/2QCY19 has been largely volume led.

What changed?

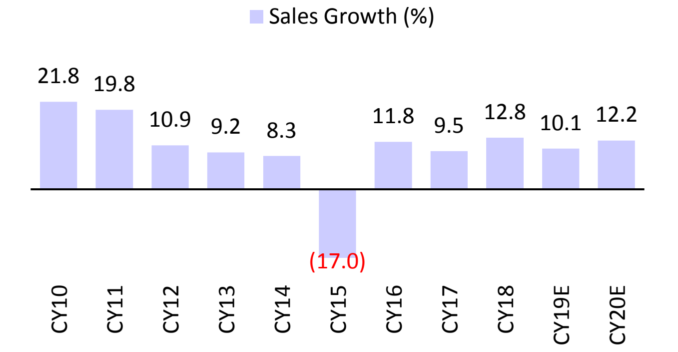
- Clear emphasis was laid on volume-led top line growth.
- Spate of new launches over this period.
- Particularly in the last year and a half, there was willingness to increase ad-spends.
- More recently, clearly stated plan to increase distribution from 4.6m outlets to 5.5-6m outlets.
- Importantly unlike HUVR, CLGT and PGHH (in sanitary napkins), Nestle India forms a small part of parent revenues (1.7%). Thus, it was crucial to obtain buy-in from the parent for the change in strategy, which the management of Nestle India was successfully able to achieve.

Exhibit 14: Strong jump in volumes post CY15



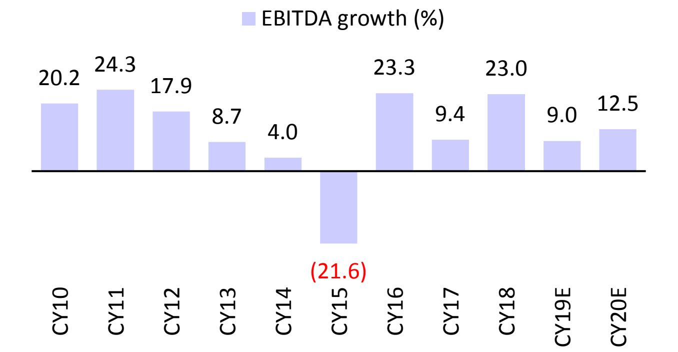
Source: Company, MOFSL

Exhibit 15: Sales growth in double-digits post CY15



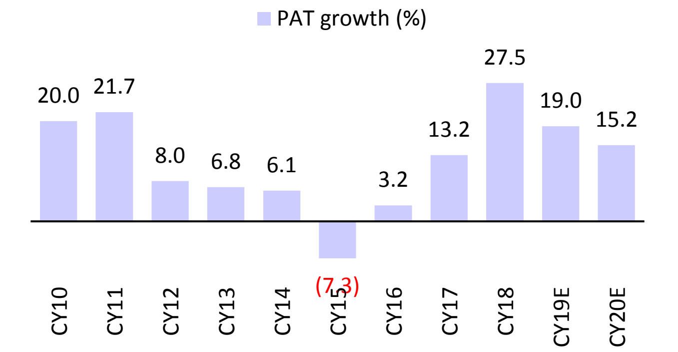
Source: Company, MOFSL

Exhibit 16: EBITDA registering healthy growth post CY15



Source: Company, MOFSL

Exhibit 17: PAT growth has been higher than EBITDA growth over the past two years and is likely to continue



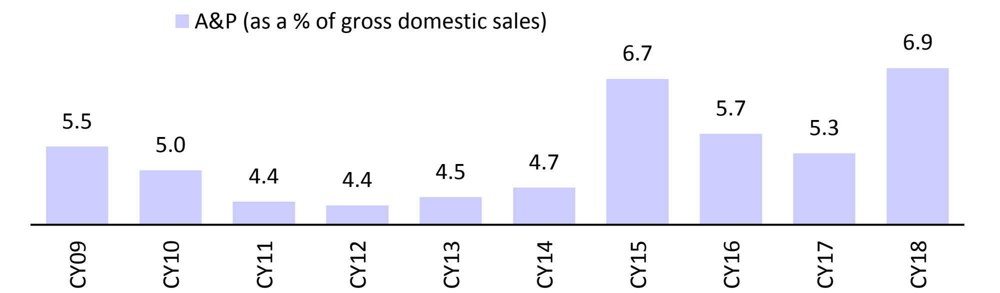
Source: Company, MOFSL

Exhibit 18: 61 products were launched by Nestle in the past 3 years; in this, company's success rate is a remarkable 70%

Year	CY12	CY13	CY14	CY15	CY16	CY17	CY18	CY19 (YTD)
No. of launches	9	6	7	3	19 (39 including variants and re-launches)	9 (17 including variants and re-launches)	14 (20 including variants)	2
1	Nestle Baby & Me	NAN PRO 1	Maggi Oats Noodles	Relaunched Maggi Noodles	Maggi Hot Heads 4 variants	Maggi Nutri-licious Noodles : 2 variants	Kitkat duo strawberry variant	Organic cereals
2	Cerelac Shishu Aahar	Maggi Hungrooo	Nestlé KitKat Senses Milk	Munch Nuts	Maggi No Onion No Garlic Masala	Maggi Masalas of India : 4 variants	Munch Crunch-O-Nuts	Maggi Fusian - 3 variants
3	Renovation of Lactogen	Maggi Magical Masala Noodles	Nestlé KitKat Senses Dark	Cerelac Stage 5	Maggi Hot Heads Cuppa Noodles	Nestle a+ Grekyo greek yogurts : 3 variants	Nesplus Breakfast cereals-4 variants	
4	Renovation of Cerelac	Nestle Munch 4*4	Nestlé KitKat Senses Extra Smooth		Maggi Cuppa Masala	Nan Excella Pro	Nescafe Ready-to-Drink Cans	
5	Maggi Healthy Soups	Nestle Munch convenient share bag pack	Nestle Masala Buttermilk		Maggi Cuppa Chilly Chow	Nestle Resource High Protein : 3 variants	Maggi Special Masala noodles	
6	Nestle Kitkat Dark Crisp Wafer Fingers	Nestle Alpino	Nestle Lassi		Maggi Cup-a-licious Soups 6 variants	Milo Ready-to-Drink beverage	Maggi dip & spread-2 variants	
7	Munch Rollz Wafer Tube		NAN Lo-Lac		Nestle a+ Grekyo 4 variants	KITKAT Dessert Delight	Kitkat Dessert Delight Brownie Kubes	
8	Relaunch of Nescafe Classic in a unique jar				Nestle Everyday Masala Fusion Dairy Whitener 6 variants	Milkybar (Re-launch)	Nescafé E-Smart Coffee Machine (all-in-one travel mug and coffee machine)	
9	Sunrise Strong				Nescafe RTD 3 variants	Milkybar Moosha	Maggi Nutri-licious Baked Noodles	
10					Ceregrow		Nestle Les Recettes De l'Atelier	
11					Nestle a+ Pro-grow		Nestle Everyday Chai life-3 variants	
12					Renovation of Cerelac with Iron		Nangrow	
13					Nescafe Sunrise Insta-filter		Nan Pro with DHA (Re-launch)	
14					Nestea Iced Tea 3 variants		Nan Excellapro (Re-launch)	
15					Nescafe Latte			
16					Kitkat Duo			
17					Nestle Munch Trio			
18					Barone Charge			
19					New Alpino			

Source: Company, MOFSL

Exhibit 19: Ad spends grew 160bp to 6.9% in CY18



Source: Company, MOFSL

Hindustan Unilever

From 1999-09, HUVR's stock price was flattish

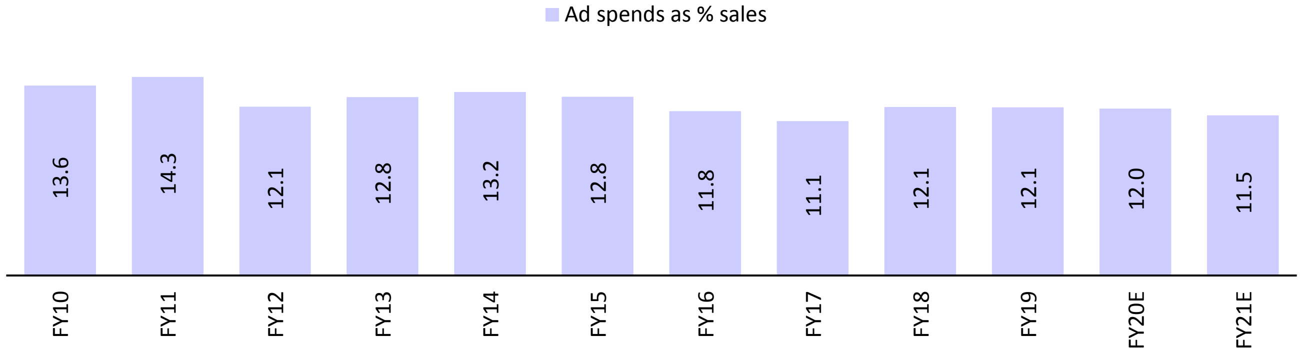
- During the early 1990s, HUVR saw exponential growth in the personal products business. From a mere INR750m business in 1991, it grew to an INR18b business by 2000 — registering CAGR of ~40%. The other key development in the early-1990s included a series of mergers and acquisitions. These included Tata Oil Mills, Kissan, Kwality, Lakmé, Brooke Bond, Lipton India and Pond's. However, the early-2000s was a period of consolidation for HUVR. During 2000-04, HUVR divested into various non-FMCG and commodity businesses such as animal feeds, specialty chemicals, mushrooms, etc. (about one-fourth of its sales were from these businesses), which were contributing only 10% to the company's profit. HUVR was also affected by the massive increase in competition from P&G in detergents and shampoos and Colgate in oral care. In addition, competition also intensified from Godrej Consumer, Reckitt & Benckiser and Wipro. This was partly due to HUVR taking their eyes off the ball and partly due to competitors wanting to increase market share even at the cost of the category's profitability.

Change in management

- In 2008, HUVR saw a major rejig in its key management; Mr. Douglas Baillie was replaced by Mr. Nitin Paranjpe as the MD & CEO. When Mr. Paranjpe took over, HUVR was going through one of its toughest phases. Revenue growth was in single-digits and Mr. Paul Polman, the CEO of Unilever Plc. had even declared its Indian arm an underperformer. HUVR's top team realized that it could no longer rely on its decades-old strategy of catering to the mass market; it concluded that getting growth back would require them to increasingly focus on consumers, their changing needs and aspirations. Mr. Paranjpe was responsible for steering HUVR from just a mass products company to a mass and premium products one. He was focused on restoring competitiveness across categories by taking actions such as:
  - **Investments in product quality, pricing and brand support.** HUVR started offering premium products with higher margins,
  - **Reducing cycle time from decision to execution** across some key processes in order to become far more responsive to the market place,
  - **Increasing focus on execution in the marketplace by starting Project IQ and Perfect Store initiative.** HUVR used technology to gather information on the buying behavior/pattern of customers (retail outlets) throughout the chain with every single urban outlet being covered to begin with. Parameter like what a shopkeeper purchased and the frequency were monitored. Each sales agent was given a tablet, which told him what to do at the store on that particular day. After the salesman, the merchandising agent would pay a visit. The merchandising agent too carried a tablet and based on information given by it would arrange stuff on shelves to make it a perfect store,
  - **Stepping up innovation intensity** (launched/ re-launched products) and A&P spends across categories,
  - **Focused on expanding distribution reach** – up 3.5x in four years. Company also expanded direct coverage from 0.9m outlets in 2009 to 3.2m outlets in 2013, and

- **Increasing focus on rural penetration** (number of rural outlets doubled to 2m during 2010-12).

Exhibit 20: HUVR stepped up innovation intensity and A&P spends across categories



Source: Company, MOFSL

Over 2009-19, HUVR's EPS grew ~12% and stock price exhibited ~21% CAGR

- Factors that led this growth include (a) despite its large size relative to peers, HUVR became far nimbler when it came to both being proactive and reactive to external stimuli, (2) company exhibited flexibility amid sharp material cost movements and launches by competitors, and (3) also focused on cost savings (6-stage approach for driving sustainable cost reduction and Symphony program).

Exhibit 21: EPS and market cap. CAGR

CAGR	EPS (%)	M.cap (%)
1999-2009*	9.6	4.5
2009*-FY19	12.2	21.0
FY17-FY20 YTD	19.1	27.3

Source: Company, MOFSL

**Prior to FY09 company followed Jan-Dec as FY, nos. have been annualized accordingly*

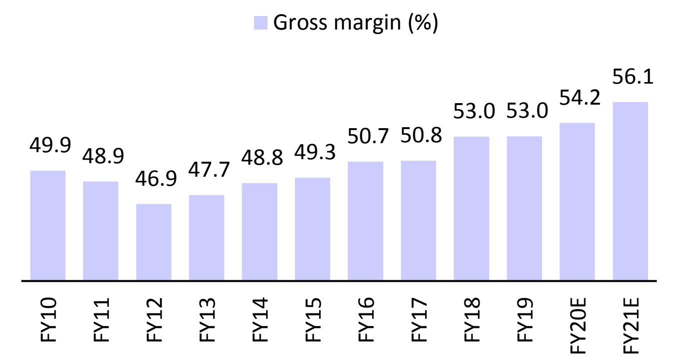
- In 2013, Mr. Sanjiv Mehta was appointed as CEO and MD of HUVR. During his tenure, he (1) rolled out two unique strategies i.e. WIMI and CCBT, (2) used artificial intelligence and technology to predict product movements, (3) started an e-commerce initiative and cut product development time, and (4) created a localization strategy that saw multiple product variants aimed at local tastes.

Four key trends emerged during Mr. Mehta's tenure, which resulted in an elevation in earnings growth trajectory, these include:

- **Winning in Many Indias - WIMI framework:** A concept that led to localization not only in terms of products, but also in distribution and supply chain. It essentially changed the sales structure from an existing 4-branch framework to 14-distinct consumer clusters based on consumption patterns and stages of economic development with each cluster being led by a new manager. The objective was to drive sharper execution in smaller markets, extract better value and throughput from existing coverage and drive growth in non-metro markets. Mr. Mehta also set up 15 Country Category Business Teams (CCBT) within the company to speed up decision-making and roll out innovations faster.

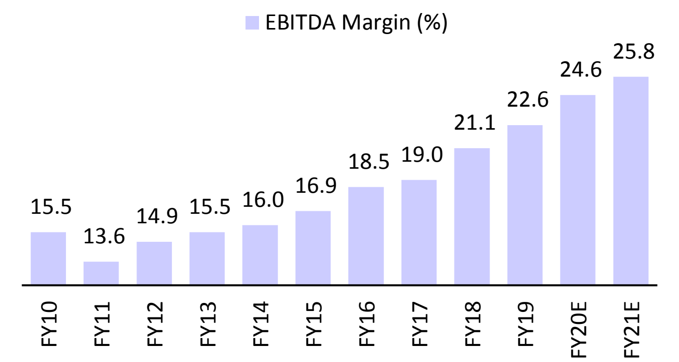
- **Continuous focus on premiumization:** Alongside localization and looking at India through the WIMI lens, HUVR tried to break the myth of a saturated Indian FMCG market by constantly pushing consumers to upgrade. Therefore, even when categories were penetrated, the scope to grow was massive in terms of upgrading consumers. Premiumization as a trend has not changed over the past few years, with 100-150bp shift every year from the mass and popular segments to the premium segment.
- **Recognition and strong execution on 'Naturals' as a key sub-segment across categories:** HUVR recognized and focused on the key 'Naturals' segment such as (1) *Lever Ayush* (master brand), (2) Specialist brands like *Indulekha*, and (3) Natural variants of existing large brands like *Fair & Lovely, Clinic Plus, Vim, Tresemme*, etc. This gave the company an enviable product portfolio to play the potential shift toward herbal products in key categories. Importantly, the company also straddles price points in this segment, from the INR1 *Clinic Plus* sachet to INR435 for *Indulekha.*
- **'Re-imagining HUVR' - Extensive plans to employ technology and create further entry barriers:** HUVR continued using artificial intelligence and technology to better predict product movements and stocking requirements, thereby offering customized solutions in order to stay ahead of the trends. Data analytics also gave the company enough understanding of what SKUs to sell in which store in the country and which areas need direct coverage. For e.g. product requirement to a *Kirana* store owner by launching '*Humara* Stores' or to traders by enabling them to place orders online (*Shikar* app) and not rely on distributors or have customized assortments according to the locality.

Exhibit 22: Gross margins improved as company started offering premium products



Source: Company, MOFSL

Exhibit 23: Margin improvement due to cost management initiatives



Source: Company, MOFSL

Increased focus on M&A also supported EPS growth: With access to impressive cash flows, ability to leverage on its best-of-breed distribution reach and nimbleness in all aspects of decision making, inorganic growth has become an important component of the top line and EPS growth for HUVR.

- In FY17, HUVR completed acquisition of the flagship brand '***Indulekha***' from Mosons Extractions Private Limited ('MEPL') and Mosons Enterprises, in order to strengthen its personal care portfolio. The acquisition brought them a premium ayurveda brand with strong credentials that complemented existing portfolio and strengthened their presence in the hair care category. The deal envisaged the acquisition of the trademarks *'Indulekha'* and *'Vayodha'*, intellectual property, design and knowhow.

- In FY19, HUVR entered into an agreement with Vijaykant Dairy and Food Products Limited (VDFPL) and its group companies to acquire the latter's ice cream and frozen desserts business consisting the flagship brand ***'Adityaa Milk'*** and the front-end distribution network across geographies. The acquisition was in line with the company's strategic intent to strengthen its position in the rapidly growing ice cream and frozen desserts market in India.
- In FY19, HUVR also proposed a merger of **GlaxoSmithKline Consumer Healthcare (GSK CH)** business into HUVR. This was in line with its ambition to build one of the largest Foods & Refreshment businesses in the country. The amalgamation of the two Companies – the combined knowledge and the strong portfolio, will give it a strong competitive edge.

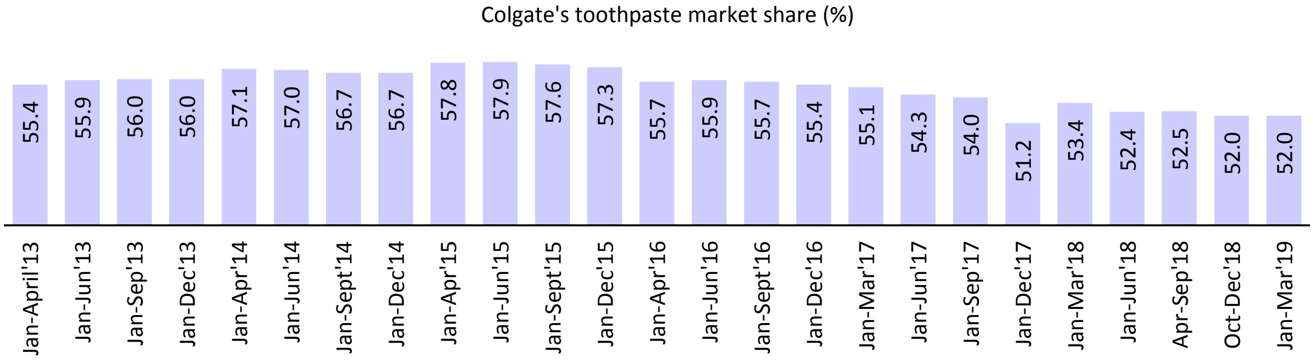
Mr. Ram Raghavan is the MD of Colgate-Palmolive India, and is providing strategic leadership to the business in India and South Asia, since Aug'19. He joined in 1997 and has over the years grown to handle multiple leadership roles. He has worked across diverse geographies and markets including Hong Kong, China, Canada and Latin America. In his previous stint at Latin America, he was instrumental in developing the platform-based innovation model supporting organic growth in Latin America. Prior to that, he served as MD of Colgate, China.

Colgate-Palmolive India

Focus back on volume growth

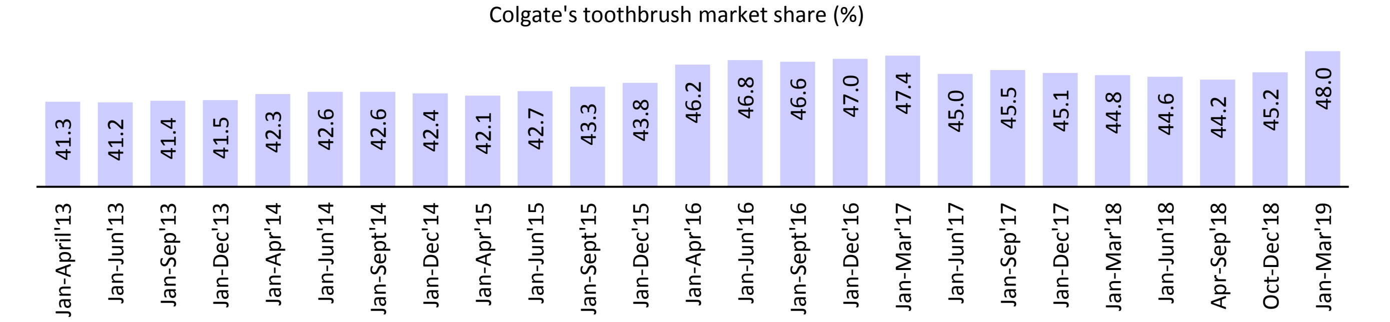
- After CLGT's new CEO – Mr. Ram Raghavan took over in Aug'19, CLGT's focus is back on volume-led growth (drive per capita consumption and frequency of purchase) even if it is at the cost of near-term profitability. His plan is to drive category growth (increasing usage in rural and not just driving penetration) and premiumization. Apart from this, he also plans to push its ayurvedic variants in North/South India to counter challenges from Patanjali by adopting a more consumer-centric approach in developing relevant 'Naturals' offerings. Additionally, he plans to add several toothpaste brands in the kids range to build long-term loyalty. He is also focusing on communicating the importance of brushing teeth twice-a-day to expand the market.
- While the strategy isn't new, we sense renewed aggression. Our channel checks indicate that signs of new found aggression is already visible, starting from modern trade, both in visibility as well as increased promotions. While the oral care segment's volume growth may not be in double-digits currently (as was the case until 2015), we believe that mid-single-digits volume growth is still possible. If Colgate is able to recoup some of its market share losses in the past three years, volume growth can be back in high single-digits.

Exhibit 24: Toothpaste market share has stabilized over the last few quarters



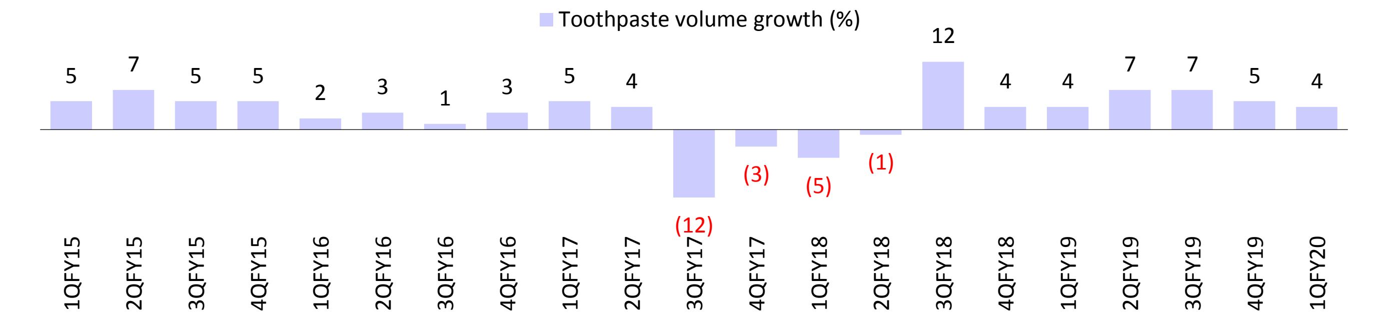
Source: Company, MOFSL

Exhibit 25: Colgate has gained market share in the smaller toothbrush segment in recent quarters



Source: Company, MOFSL

Exhibit 26: Volume growth is expected to increase under the new MD



Source: Company, MOFSL

CLGT - A key beneficiary of the corporate tax rate cuts

- CLGT was expected to pay taxes at a rate of ~33-34% for FY20E and FY21E before the announcement of the corporate tax cut by the government. Corporate tax cuts will add between INR850-1,150m to its profits.

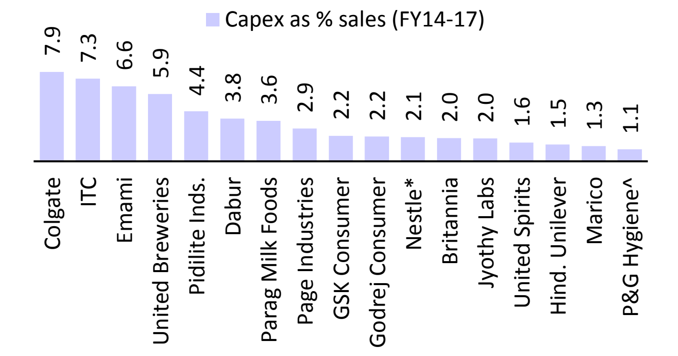
Profitability significantly higher than other oral care players like Dabur/Patanjali

- As mentioned in our note released after the announcement of the corporate tax cut, we need to assess the second-order effects of this measure. This includes the impact on (1) Relative basis (v/s peers) in categories where the company operates, and (2) Absolute profit and absolute savings v/s peers.
- We believe that CLGT is well placed in terms of both these factors given that Dabur and Patanjali will not see any material gains from the corporate tax cuts. CLGT can spend a significant part of the INR850-1,150m on incremental PAT by way of promotions/price-offs in an attempt to gain market share. Two points are important here:
  - **Gain further share or lead to further bleeding of peers:** None of its competitors would have such windfall gains, and if they choose to match CLGT's efforts on promotions and price-offs, they would end up bleeding further.
  - **Utilize/institutionalize multi-year benefit over peers:** Importantly, the corporate tax cuts offer multi-year benefits to CLGT, providing it with incremental benefit every year until competitors scale up well.

No capex required till FY22E to support PAT growth:

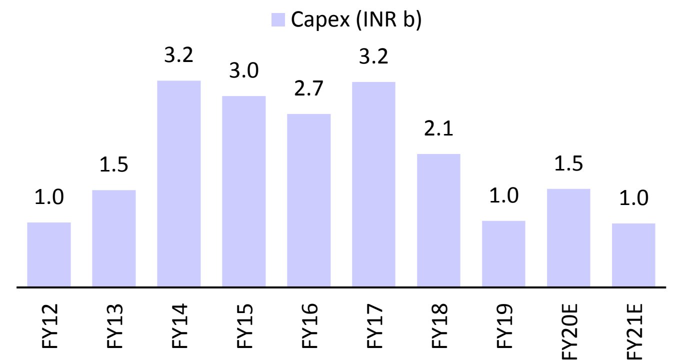
- CLGT had created significant capacity between FY14-17 before the onslaught of herbal players, which delayed capacity utilization pick-up. Therefore, it doesn't need any material capex until FY22E. Even if volumes were to recover to high single-digits (assuming some market share recovery) from low to mid-single digits, PAT growth will be much higher than EBITDA/topline growth as was witnessed in Nestle's case recently when they finally got their strategy right.

Exhibit 27: CLGT incurred significant capex between FY14-17



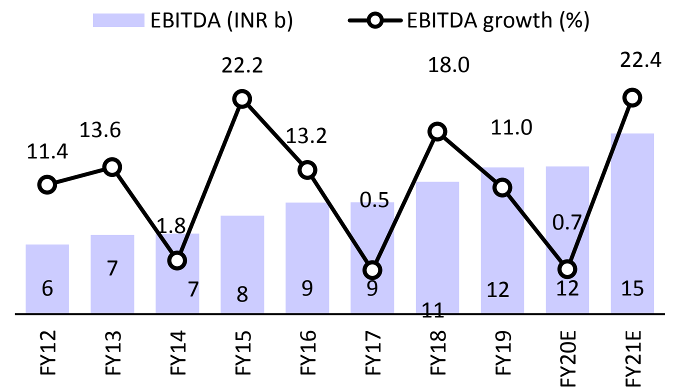
Source: Company, MOFSL

Exhibit 28: No material capex anticipated until FY22E



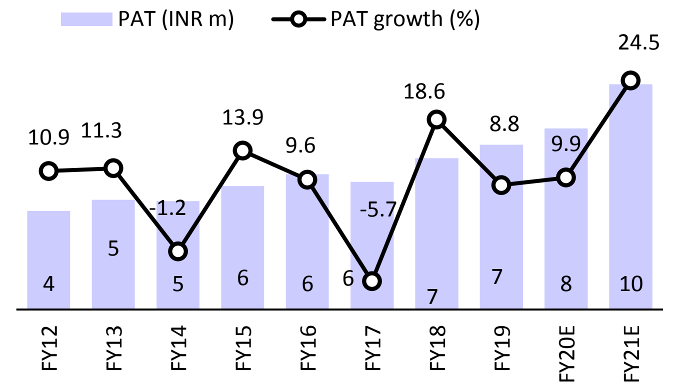
Source: Company, MOFSL

Exhibit 29: EBITDA growth to be higher than sales



Source: Company, MOFSL

Exhibit 30: PAT growth to be much higher than EBITDA



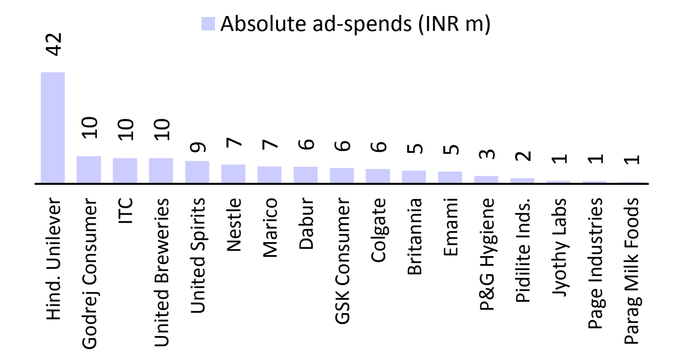
Source: Company, MOFSL

Strength of moats compared to peers

- CLGT's distribution reach (direct reach from 1 m to 2.3x m over FY12-18 exit), massive ad-spends and cash flows directed into a single category unlike peers, consistent category development efforts and brand equity have enabled it to outlast peers across emerging markets. CLGT has the advantages of the following moats:
  - **By far the best distribution reach in oral care** with over 6m outlets (and in fact the second best across all FMCG products); this strength is being consolidated with significant increase in rural coverage over the past few years;
  - **Unmatched category development efforts** in schools, cumulative reach of ~150m school children contacted across 0.3m schools in the last 40 years, enabling it to unlock category growth potential;

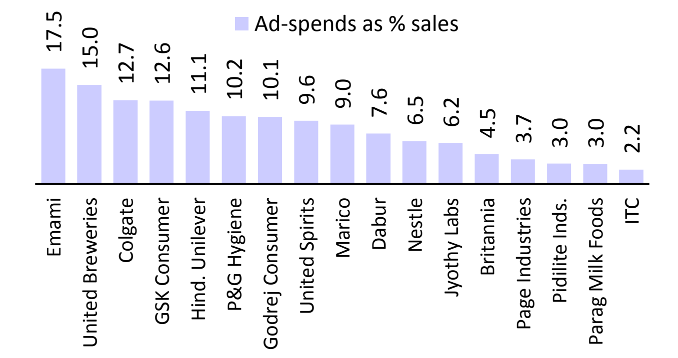
- **The most dominant brand** (more than 3x market share of any other brand in oral care) as well as the most trusted in oral hygiene brand (rated no. 1 by Brand Equity in each of the past nine years);
- **Benefits of concentrating focus in oral care**. With 98% sales for the company coming in from oral care, a category that it dominates, CLGT is able to channel its vast cash flows into advertising and capacity expansion unlike peers for whom oral care is at best 10% of sales. CLGT has by far the best A&P muscle in the category with annual spends of over INR5-6b, enhancing brand moat. CLGT was able to spend an unrivalled amount of INR12.2b during FY14-17 in state-of-the-art facilities. Thereby, it augmented capacities, attained large-scale benefits, gained an ability to roll out higher quality premium products faster and saved on logistics costs as a result of being closer to suppliers and large markets;
- **Significant contributions from its India R&D center**, one of CLGT's few global innovation centers, has enabled successful rollout of herbal/natural products.

Exhibit 31: Absolute ad-spends of CLGT v/s peers (FY19)



Source: Company, MOFSL

Exhibit 32: Ad-spends as % of sales - CLGT v/s peers (FY19)



Source: Company, MOFSL

Past track record highly encouraging

- Over the past 25 years, CLGT has emerged even stronger during periods of heightened competitive activity. The industry has witnessed various trends in the past, such as:
  - HUVR launched gel-based *Close Up* toothpaste in the 1990s, but CLGT soon introduced *CLGT Max Fresh*, which is now neck-to-neck with the former in many key states.
  - P&G launched *Oral B* toothpaste in Jul'13. Coincidentally, HUVR massively ramped up ad-spends on *Pepsodent* at the same time to catch CLGT off guard. However, CLGT also increased ad-spends, to ensure that shelf space was not available for *Oral B*. Eventually, *Oral B* had to pull out and *Pepsodent* lost even more market share to CLGT.
  - While GSK gained market leadership in the premium segment by launching *Sensodyne* and *Parodontax* in the earlier part of this decade, CLGT with a much wider variety of premium products (*Colgate Sensitive*) is now close behind.
  - With two consecutive years of weak monsoons (leading to massive down trading), many lower-end/herbal players like Ajanta, Amar etc. made their

debut in the last decade. But unlike HUVR, CLGT was able to outflank them by launching herbal toothpastes, such as *Cibaca Vedshakti*. These low cost players are nowhere in the picture now.

- CLGT suffered over the past 3.5 years as it was blindsided by the herbal competition (lost 600bp market share to Patanjali between FY15-18) and at the same time, responded late in terms of herbal launches (*Swarna Vedshakti*). However, over the past three quarters, their market share has stabilized at ~51% (from ~57%) after hemorrhaging for around three years. At the same time, herbal category growth is also slowing to ~15% compared to over 30% in the past; this has helped CLGT as it has much lower market share in the herbal category.

Financial performance

Exhibit 33: Expect revenue CAGR of 9.8% over FY19-21E

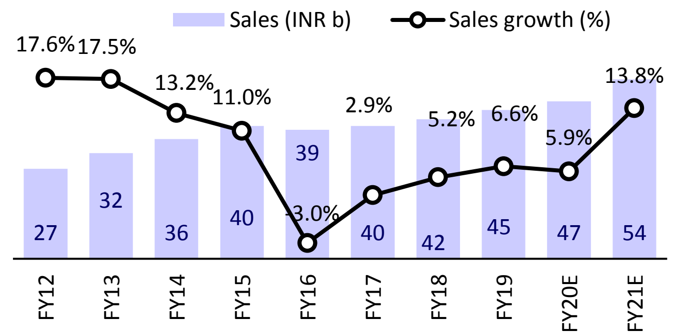


Exhibit 34: Gross margin expansion of 40bp over FY19-21E

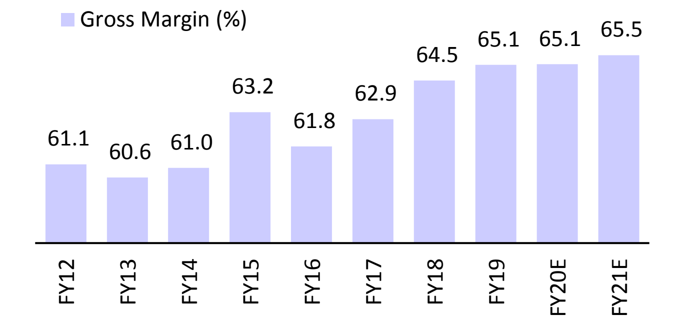


Exhibit 35: Expect EBITDA CAGR of 11.0% over FY19-21E

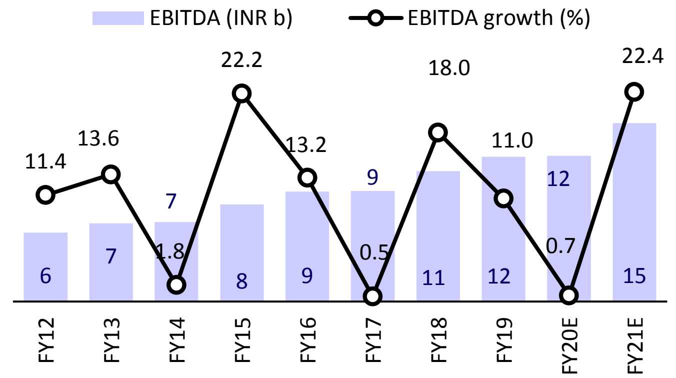


Exhibit 36: EBITDA margin expansion of 60bp over FY19-21E but likely to contract in FY20

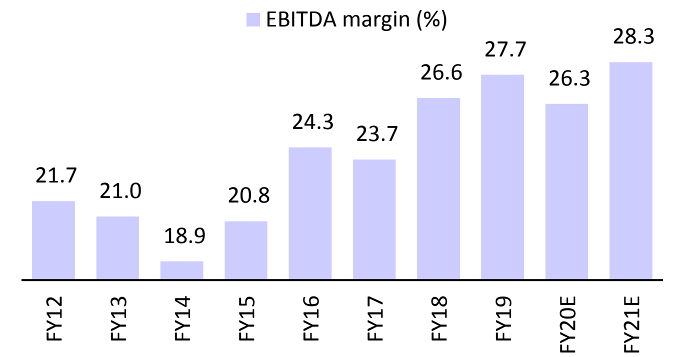


Exhibit 37: Expect PAT CAGR of 17.0% over FY19-21E

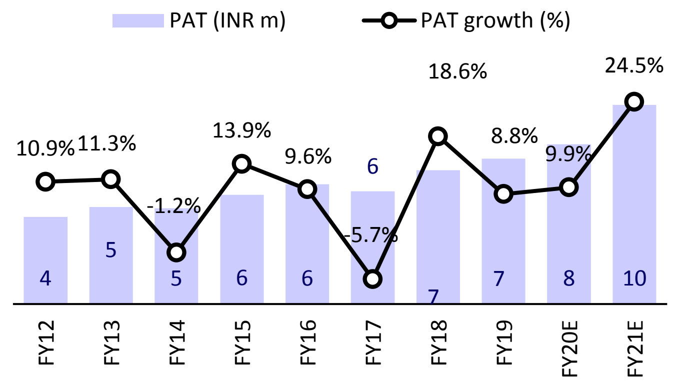


Exhibit 38: Expect return ratios to improve further

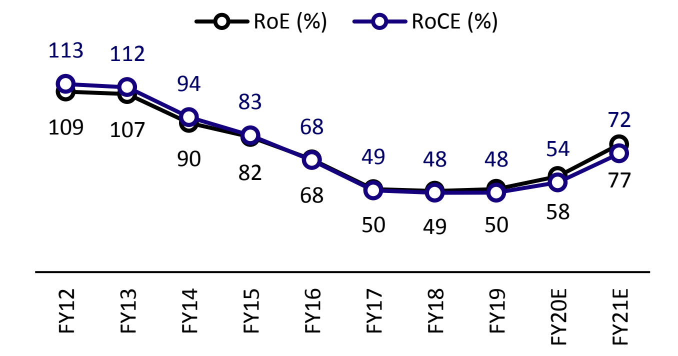


Exhibit 39: CLGT P/E (x)

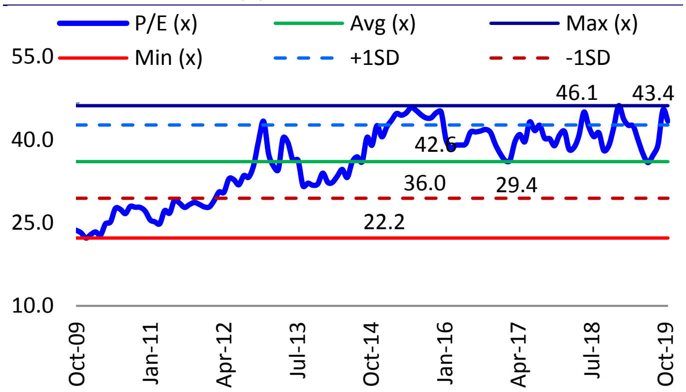
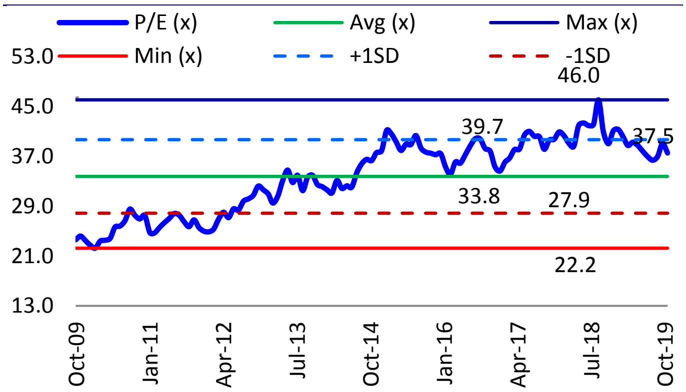


Exhibit 40: Consumer P/E



Source: Company, MOFSL

Source: Company, MOFSL

Financials and Valuations

Income Statement (INR Million)

Y/E March	2015	2016	2017	2018	2019	2020E	2021E
Net Sales	**39,887**	**38,682**	**39,818**	**41,880**	**44,624**	**47,265**	**53,804**
Change (%)	11.0	-3.0	2.9	5.2	6.6	5.9	13.8
COGS	14,677	14,763	14,763	14,887	15,586	16,495	18,584
Gross Profit	**25,210**	**23,919**	**25,055**	**26,992**	**29,039**	**30,770**	**35,220**
Gross Margin (%)	63.2	61.8	62.9	64.5	65.1	65.1	65.5
Operating expenses	16,920	14,534	15,619	15,855	16,678	18,328	19,997
EBITDA	**8,290**	**9,385**	**9,435**	**11,137**	**12,361**	**12,442**	**15,223**
Change (%)	22.2	13.2	0.5	18.0	11.0	0.7	22.4
Margin (%)	20.8	24.3	23.7	26.6	27.7	26.3	28.3
Depreciation	750	1,114	1,332	1,565	1,592	1,748	1,849
Int. and Fin. Charges	0	0	0	0	25	80	80
Financial Other Income	264	395	411	375	377	328	332
Profit before Taxes	**7,804**	**8,666**	**8,514**	**9,947**	**11,120**	**10,942**	**13,626**
Change (%)	17.6	11.1	-1.8	16.8	11.8	-1.6	24.5
Margin (%)	19.6	22.4	21.4	23.8	24.9	23.2	25.3
Tax	2,009	2,541	2,740	3,022	3,717	2,754	3,429
Tax Rate (%)	28.4	29.3	32.2	31.1	33.0	25.2	25.2
Adjusted PAT	**5,590**	**6,125**	**5,774**	**6,850**	**7,451**	**8,188**	**10,196**
Change (%)	13.9	9.6	-5.7	18.6	8.8	9.9	24.5
Margin (%)	14.0	15.8	14.5	16.4	16.7	17.3	19.0
Non-rec. (Exp)/Income	0	-313	0	-117	305	0	0
Reported PAT	**5,590**	**5,812**	**5,774**	**6,734**	**7,756**	**8,188**	**10,196**

Balance Sheet (INR Million)

Y/E March	2015	2016	2017	2018	2019	2020E	2021E
Share Capital	272	272	272	272	272	272	272
Reserves	7,431	10,038	12,466	14,974	14,196	13,550	12,368
Net Worth	**7,703**	**10,310**	**12,738**	**15,246**	**14,468**	**13,822**	**12,640**
Loans	0	0	0	0	777	777	777
Deferred Liability	26	97	275	355	309	309	309
Capital Employed	**7,729**	**10,407**	**13,013**	**15,601**	**15,553**	**14,908**	**13,725**
Gross Block	12,829	14,866	17,188	19,077	21,077	22,618	23,618
Less: Accum. Depn.	-5,013	-4,785	-6,107	-7,617	-9,169	-10,916	-12,766
Net Fixed Assets	**7,816**	**10,081**	**11,081**	**11,459**	**11,909**	**11,702**	**10,852**
Capital WIP	1,412	784	1,666	1,586	1,987	1,987	1,987
Investments	371	312	312	312	312	312	312
Current	371	0	0	0	0	0	0
Non-current	0	312	312	312	312	312	312
Curr. Assets, L&A	**7,420**	**8,852**	**10,048**	**12,282**	**12,058**	**13,078**	**13,020**
Inventory	2,522	2,915	2,926	2,267	2,486	2,636	2,971
Account Receivables	696	1,015	1,299	2,010	2,098	2,315	2,343
Cash & Bank	2,545	2,887	2,943	4,562	3,994	4,534	3,994
Others	1,657	2,035	2,880	3,443	3,481	3,593	3,713
Curr. Liab. and Prov.	**9,290**	**9,622**	**10,094**	**10,037**	**10,712**	**12,170**	**12,446**
Account Payables	5,144	5,519	5,975	6,203	6,132	7,534	7,703
Other Liabilities	2,874	3,438	3,356	3,040	3,757	3,772	3,836
Provisions	1,272	664	763	794	823	864	907
Net Current Assets	**-1,870**	**-770**	**-46**	**2,245**	**1,346**	**908**	**575**
Application of Funds	**7,729**	**10,407**	**13,013**	**15,601**	**15,553**	**14,908**	**13,725**

E: MOFSL Estimates

Financials and Valuations

Ratios							
Y/E March	**2015**	**2016**	**2017**	**2018**	**2019**	**2020E**	**2021E**
Basic (INR)							
EPS	**20.6**	**22.5**	**21.2**	**25.2**	**27.4**	**30.1**	**37.5**
Cash EPS	23.3	26.6	26.1	30.9	33.2	36.5	44.3
BV/Share	28.3	37.9	46.8	56.1	53.2	50.8	46.5
DPS	12.5	11.0	11.0	24.0	23.0	26.2	33.7
Payout %	60.6	48.8	51.7	95.3	84.0	87.0	90.0
Valuation (x)							
P/E	75.0	68.4	72.6	61.2	56.0	51.0	40.9
Cash P/E	66.1	57.9	59.0	49.8	46.1	42.0	34.6
EV/Sales	10.4	10.8	10.4	9.9	9.3	8.7	7.7
EV/EBITDA	50.2	44.3	44.1	37.2	33.5	33.2	27.2
P/BV	54.4	40.7	32.9	27.5	28.8	30.2	33.0
Dividend Yield (%)	0.8	0.7	0.7	1.6	1.5	1.7	2.1
Return Ratios (%)							
RoE	81.6	68.0	50.1	49.0	50.1	57.9	77.1
RoCE	82.5	67.5	49.3	47.9	47.9	54.2	71.6
RoIC	236.5	119.0	75.7	76.5	78.4	92.3	129.1
Working Capital Ratios							
Debtor (Days)	6	9	11	17	17	18	16
Asset Turnover (x)	6.7	4.2	3.6	3.1	3.4	3.7	4.7
Leverage Ratio							
Debt/Equity (x)	0.0	0.0	0.0	0.0	0.1	0.1	0.1

Cash Flow Statement							(INR Million)
Y/E March	**2015**	**2016**	**2017**	**2018**	**2019**	**2020E**	**2021E**
OP/(loss) before Tax	7,804	8,666	8,514	9,947	11,121	10,942	13,626
Depreciation	750	1,114	1,332	1,565	1,592	1,748	1,849
Int./Div. Received	97	-264	34	81	85	-328	-332
Interest Paid	-264	-261	-297	-290	-317	80	80
Direct Taxes Paid	-2,055	-2,524	-3,014	-3,474	-4,144	-2,754	-3,429
(Incr)/Decr in WC	49	156	311	-889	1,494	979	-207
CF from Operations	**6,382**	**6,887**	**6,880**	**6,940**	**9,830**	**10,667**	**11,587**
(Incr)/Decr in FA	-2,994	-2,713	-3,212	-2,087	-1,042	-1,541	-1,000
Free Cash Flow	**3,388**	**4,175**	**3,668**	**4,853**	**8,788**	**9,126**	**10,587**
(Pur)/Sale of Investments	0	70	0	0	0	0	0
Others	135	12	-205	564	-1,209	1,732	1,735
CF from Invest.	**-2,859**	**-2,631**	**-3,418**	**-1,523**	**-2,251**	**191**	**735**
Change in Equity	0	0	0	0	0	0	0
(Incr)/Decr in Debt	0	0	0	0	-121	0	0
Dividend Paid	-3,388	-2,987	-2,717	-2,986	-6,462	-8,833	-11,379
Others	-460	-928	-689	-812	-1,564	-1,484	-1,484
CF from Fin. Activity	**-3,848**	**-3,915**	**-3,406**	**-3,798**	**-8,147**	**-10,317**	**-12,863**
Incr/Decr of Cash	**-325**	**342**	**56**	**1,619**	**-568**	**541**	**-541**
Add: Opening Balance	2,870	2,545	2,887	2,943	4,562	3,994	4,534
Closing Balance	**2,545**	**2,887**	**2,943**	**4,562**	**3,994**	**4,534**	**3,993**

E: MOFSL Estimates

Explanation of Investment Rating	
Investment Rating	**Expected return (over 12-month)**
BUY	>=15%
SELL	< - 10%
NEUTRAL	< - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

*In case the recommendation given by the Research Analyst is inconsistent with the investment rating legend for a continuous period of 30 days, the Research Analyst shall within following 30 days take appropriate measures to make the recommendation consistent with the investment rating legend.

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