

GlaxoSmithKline Consumer Healthcare

10 August 2018

Reuters: GLSM.NS; Bloomberg: SKB IN

Marginally Ahead Of Expectations

GlaxoSmithKline Consumer Healthcare's (SKB) 1QFY19 performance was marginally ahead of overall expectations. Volume growth of 12.8% during the quarter was a function of a favourable base due to GST-related issues, reduction in promotions as a part of the strategy and increased grammage in LUP products like sachets post-GST rate cut. Real underlying growth could be in the range of 7%-8%. Sharp deflation of raw material costs resulted in margin gains for SKB wherein the underlying gross margin improved 230bps YoY (430bps on a reported basis). The management indicated that more focus will be on advertising rather than promotion going forward. Operating earnings and net income grew 38% and 52% YoY, respectively, above overall expectations on a favourable base. Value market share of Horlicks and Boost stood at 44.2% and 11.2%, respectively, similar to that of the previous quarter. The management discussed that the sachet format - which forms 9% of the revenues - is growing rapidly and will aid in increasing the market penetration reach for the company. There were several other marketing campaigns carried out for Horlicks and Boost brands to increase the awareness and market penetration during the quarter. SKB believes that Rs11,000mn ready-to-drink (RTD) market in India is a very big business opportunity and expects to launch Boost RTD all over South India before the end of the current financial year. On category growth, the management expects mid-high single-digit growth led by improvement in macro environment, and increase in distribution and awareness through marketing campaigns. As regards to strategic review of key brands by the parent company, no details have been shared and a decision on the same will be taken by the end of December 2018. Although the performance in 1QFY19 was better than expectations, our core concerns regarding category growth, competition, lack of differentiated products and mainly uncertainty about the continuance of key brands still remain. Therefore, after marginally revising our estimates, we have retained Accumulate rating on SKB with a revised target price of Rs6,850 (from Rs6,700 earlier) based on FY20E EPS and P/E multiple of 32x, indicating an upside of 3% from the CMP.

Volume growth on a favourable base: Comparable sales growth during the quarter stood at 16% wherein volume growth was 12.8%. Volume growth of 12.8% during the quarter was a function of a favourable base, reduction in promotion and increased grammage in LUP products like sachets post GST rate cut. Sachet portfolio grew strongly in high double digits. RTD launch under Boost brand in Tamil Nadu has received an encouraging response. Underlying category growth remains in mid-to-high single digits. Value market share of Horlicks and Boost stood at 44.2% and 11.2%, respectively.

Favourable input prices support margin expansion: Sharp deflation of raw material costs resulted in margin gains for SKB, wherein underlying gross margin improved 230bps YoY (430bps on a reported basis). Commodity basket is likely to remain stable going forward. The management indicated that more focus will be on advertising rather than promotion going forward. Operating earnings and net income grew 38% and 52%YoY, respectively, above overall expectations on a favourable base.

Outlook and valuation: Overall, we maintain our view on the stock based on modest category growth, competition, lack of differentiated products, limited headroom for margin expansion and mainly uncertainty about the continuance of key brands. Therefore, after marginally revising our estimates, we have retained Accumulate rating on SKB with a revised target price of Rs6,850 (from Rs6,700 earlier) based on FY20E EPS and a P/E multiple of 32x, indicating an upside of 3% from the CMP.

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ACCUMULATE

Sector: FMCG

CMP: Rs6,655

Target Price: Rs 6,850

Upside: 3%

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Key Data

Current Shares O/S (mn)	42.1
Mkt Cap (Rsbn/US\$bn)	279.7/4.1
52 Wk H / L (Rs)	6,950/4,851
Daily Vol. (3M NSE Avg.)	23,411

Price Performance (%)

	1 M	6 M	1 Yr
GSK Consumer	5.0	9.4	22.9
Nifty Index	5.7	9.7	15.8

Source: Bloomberg

Y/E March (Rsmn)	1QFY18	4QFY18	1QFY19	YoY (%)	QoQ (%)	FY17	FY18	YoY (%)
Net sales	9,853	11,796	11,071	12.4	(6.1)	39,864	43,149	8.2
COGS	3,426	3,737	3,369	(1.7)	(9.9)	12,969	14,326	10.5
Gross margin %	65.2	68.3	69.6	430bps	130bps	67.5	66.8	(70bps)
Employee costs	1,338	1,376	1,680	25.6	22.1	4,672	5,346	14.4
% of sales	13.6	11.7	15.2	160bps	350bps	11.7	12.4	70bps
Advertising costs	1,278	1,693	1,439	12.6	(15.0)	5,147	5,467	6.2
% of sales	13.0	14.3	13.0	-	(140bps)	12.9	12.7	(20bps)
Other expenses	2,148	2,490	2,281	6.2	(8.4)	8,741	9,193	5.2
% of sales	21.8	21.1	20.6	(120bps)	(50bps)	21.9	21.3	(60bps)
EBITDA	1,664	2,500	2,303	38.4	(7.9)	8,335	8,818	5.8
EBITDA margin %	16.9	21.2	20.8	390bps	(40bps)	20.9	20.4	(50bps)
Depreciation	170	145	147	(13.6)	1.1	642	644	0.3
Interest expense	5	8	2	(66.7)	(76.6)	28	20	(28.1)
Other income	557	842	965	73.2	14.6	2,439	2,590	6.2
PBT	2,045	3,189	3,119	52.5	(2.2)	10,104	10,744	6.3
Tax	723	1,071	1,114	54.2	4.1	3,537	3,743	5.8
Effective tax rate %	35.3	33.6	35.7	40bps	210bps	35.0	34.8	(20bps)
PAT	1,322	2,118	2,004	51.6	(5.4)	6,566	7,001	6.6
PAT margin %	12.7	16.8	16.7	400bps	(10bps)	15.5	15.3	(20bps)
EPS	31.4	50.4	47.7	51.6	(5.4)	156.1	166.5	6.6

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 1: Financial summary

Y/E March (Rsmn)	FY16	FY17	FY18	FY19E	FY20E
Net sales	41,364	39,864	43,149	47,268	51,872
YoY growth (%)	(4.0)	(3.6)	8.2	9.5	9.7
EBITDA	8,420	8,335	8,818	10,240	11,224
EBITDA margin (%)	20.4	20.9	20.4	21.7	21.6
Reported PAT	6,873	6,566	7,001	8,322	8,997
EPS	163.4	156.1	166.5	197.9	213.9
YoY change (%)	17.7	(4.5)	6.6	18.9	8.1
RoCE (%)	31.7	25.9	24.7	26.0	25.2
RoE (%)	28.0	22.2	21.2	22.5	21.6
P/E (x)	36.9	33.0	38.5	33.9	31.3
P/B (x)	9.1	6.9	7.7	7.2	6.4
EV/EBITDA (x)	26.9	22.3	26.5	23.4	20.8

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 2: Value market share trend

Brand (%)	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19
Horlicks	44.8	44.2	43.9	44.1	44.3	44.2
Horlicks extensions	16.5	16	16.4	16.2	11.6	N.A.
Boost	11.2	11.3	11.4	11.3	11.2	11.2

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 3: Our estimates versus actual performance

Y/E March (Rsmn)	1QFY18	4QFY18	1QFY19	YoY (%)	QoQ (%)	NBIE estimate	Variation (%)
Net sales	9,853	11,796	11,071	12.4	(6.1)	10,740	3.1
EBITDA	1,664	2,500	2,303	38.4	(7.9)	2,202	4.6
EBITDA (%)	16.9	21.2	20.8	390bps	(40bps)	20.5	30bps
PAT	1,322	2,118	2,004	51.6	(5.4)	1,752	14.4

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 4: Change in our estimates

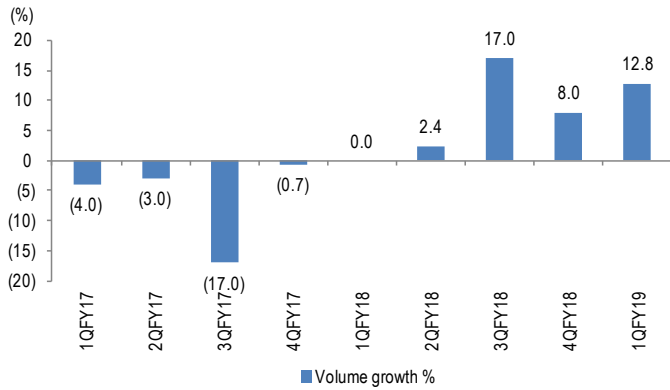
Y/E March (Rsmn)	Earlier Estimates		New Estimates		Change (%)	
	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E
Net sales	46,937	51,852	47,268	51,872	0.7	-
EBITDA	9,810	10,999	10,240	11,224	4.4	2.0
EBITDA margin (%)	20.9	21.2	21.7	21.6	80bps	40bps
Net income	7,767	8,828	8,322	8,997	7.1	1.9

Source: Company, Nirmal Bang Institutional Equities Research

Conference-call key takeaways

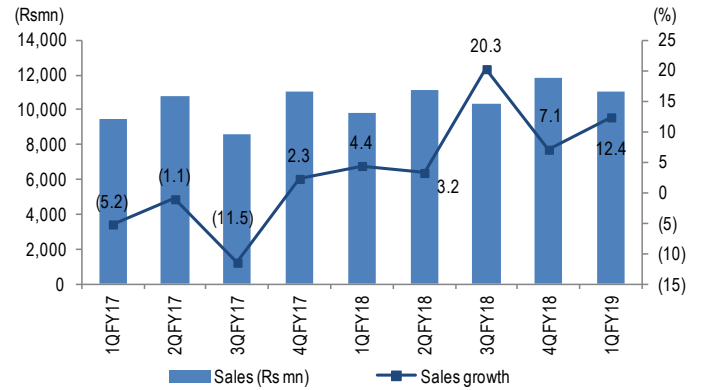
- Comparable sales growth during the quarter stood at 16% (12.6% adjusted for lost sales because of GST-related challenges) wherein volume growth was 12.8%. Volume growth of 12.8% during the quarter was a function of a favourable base, reduction in promotion and increased grammage in LUP products like sachets post GST rate cut. Sachet portfolio grew strongly in high double digits and forms 9% of the revenues. RTD launch under Boost brand in Tamil Nadu received an encouraging response. However, we believe that RTD is a crowded space and there are similar products available in the market on Pan-India basis from well-known brands like Nestle and Amul. Underlying category growth remains in mid-to-high single digits. Business auxiliary income grew 21% YoY on the back of strong growth in oral care and OTC categories. Food business witnessed a decline of 5% during the quarter as SKB decided to discontinue its Marie biscuit brand; Traditional biscuit portfolio and oats portfolio grew in mid-high single digits. SKB carried out various marketing campaigns under both the brands - Horlicks and Boost - to increase the awareness and market penetration.
- Value market share of Horlicks and Boost stood at 44.2% and 11.2%, respectively, similar to that of the previous quarter. Value market share for Horlicks and Boost stood at 50.4% and 14.2%, respectively. The share of Horlicks extensions is in the range of 11%. New launches like Protein Plus and Growth Plus under Horlicks brand reached 0.7% and 0.3% of the market, respectively.
- The company is going to expand its distribution base as market penetration is the core focus area for the management as it believes that consumption is quite stable. Apart from increasing the distribution reach through traditional channels, SKB is going to focus more on e-commerce for high-sized packs. The management indicated that overall inventory pipeline is similar or a bit lower than in the past as a result of effective inventory management practices. Although SKB is planning to expand in North and West India, its core focus and distribution lies in South and East India regions. Also, we believe that in other regions there are many competitors which are quite ahead of SKB. Hence, catering to newer geographies will remain a challenge.
- The management did not share much details about the strategic review of Horlicks and other nutrition brands announced by the parent company at the beginning of this financial year. The management stated that it is still evaluating various options. It is to be noted that revenue share is more than 90% in case of the Indian entity. Decision on this matter is expected before December 2018.

Exhibit 5: HFD volume growth trend



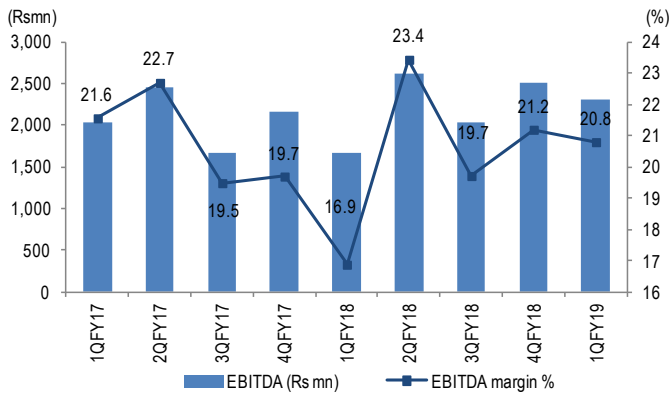
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 6: Revenue growth trend



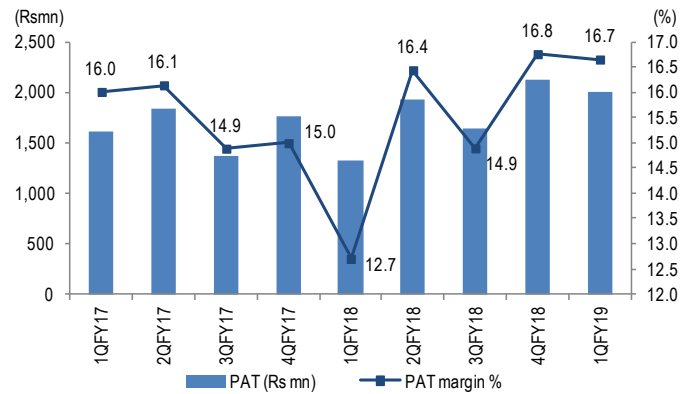
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 7: Operating margin profile



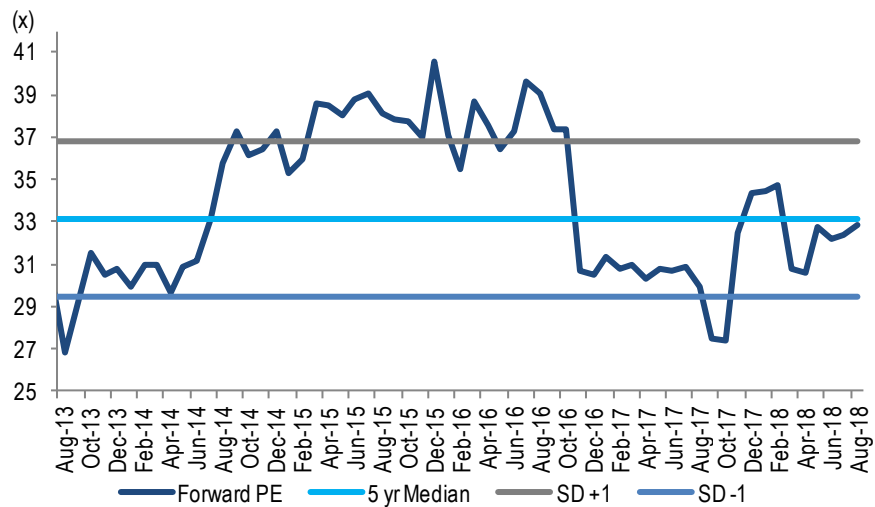
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 8: Net income trend



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 9: 1-year forward P/E



Source: Company, Nirmal Bang Institutional Equities Research

Financials

Exhibit 10: Income statement

Y/E March (Rsmn)	FY16	FY17	FY18	FY19E	FY20E
Net sales	41,364	39,864	43,149	47,268	51,872
% Growth	(4.0)	(3.6)	8.2	9.5	9.7
COGS	13,436	12,969	14,326	14,935	16,585
Staff costs	5,050	4,672	5,346	6,110	6,632
Other expenses	14,459	13,888	14,660	15,984	17,432
Total expenses	32,944	31,530	34,332	37,028	40,649
EBITDA	8,420	8,335	8,818	10,240	11,224
% growth	15.3	(1.0)	5.8	16.1	9.6
EBITDA margin (%)	20.4	20.9	20.4	21.7	21.6
Other income	2,215	2,439	2,590	3,227	3,351
Interest costs	23	28	20	13	10
Depreciation	613	642	644	616	723
Profit before tax (before exceptional items)	9,999	10,104	10,744	12,838	13,842
Exceptional items	561	-	-	-	-
Tax	3,687	3,537	3,743	4,516	4,845
PAT	6,873	6,566	7,001	8,322	8,997
Adj PAT	6,312	6,566	7,001	8,322	8,997
Adj PAT margin (%)	14.5	15.5	15.3	16.5	16.3
% Growth	17.8	4.0	6.6	18.9	8.1

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 12: Balance sheet

Y/E March (Rsmn)	FY16	FY17	FY18	FY19E	FY20E
Share capital	421	421	421	421	421
Reserves	27,566	30,806	34,431	38,758	43,652
Minority Interest	-	-	-	-	-
Net worth	27,987	31,227	34,851	39,179	44,073
Total debt	127	84	-	-	-
Deferred tax liability	(1,131)	(1,278)	(1,155)	(1,155)	(1,155)
Total liabilities	51,294	32,313	35,546	41,456	46,626
Gross block	5,694	6,316	7,016	7,816	8,616
Depreciation	882	1,442	2,085	2,701	3,424
Net block	4,813	4,874	4,931	5,115	5,192
Intangible assets	-	89	27	27	27
Capital work-in-progress	514	492	357	407	457
Investments	-	-	-	-	-
Inventories	4,616	4,612	4,094	4,498	5,043
Debtors	3,542	3,210	2,787	2,911	3,342
Cash	27,123	30,874	35,852	41,886	48,771
Loans & advances	24,489	423	311	2,033	2,749
Other current assets	703	2,579	2,739	2,836	3,112
Total current assets	37,576	41,391	45,620	52,274	60,424
Creditors	7,852	8,757	10,347	9,702	12,834
Other current liabilities & provisions	3,660	4,558	4,303	5,105	5,447
Total current liabilities	14,567	15,956	17,426	18,352	22,172
Net current assets	23,009	25,435	28,194	33,921	38,253
Total assets	51,294	32,313	35,546	41,456	46,626

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 11: Cash flow

Y/E March (Rsmn)	FY16	FY17	FY18	FY19E	FY20E
PAT	6,873	6,566	7,001	8,322	8,997
Depreciation	613	642	644	616	723
Other income	(2,215)	(2,439)	(2,590)	(3,227)	(3,351)
(Inc.)/dec. in working capital	(2,656)	1,726	2,410	399	2,843
Cash flow from operations	2,615	6,495	7,465	6,109	9,212
Capital expenditure (-)	(599)	(681)	(565)	(850)	(850)
Net cash after capex	2,017	5,814	6,900	5,259	8,362
Dividends paid (-)	(2,313)	(2,944)	(3,150)	(3,329)	(3,419)
DDT paid (-)	(471)	(599)	(630)	(666)	(684)
Inc./(dec.) in investments	-	-	-	-	-
Cash from financial activities	1,195	(25,787)	(4,255)	(2,413)	(3,826)
Opening cash balance	22,965	27,123	30,874	35,852	41,886
Closing cash balance	27,123	30,874	35,852	41,886	48,771
Change in cash balance	4,157	3,751	4,978	6,035	6,884

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 13: Key ratios

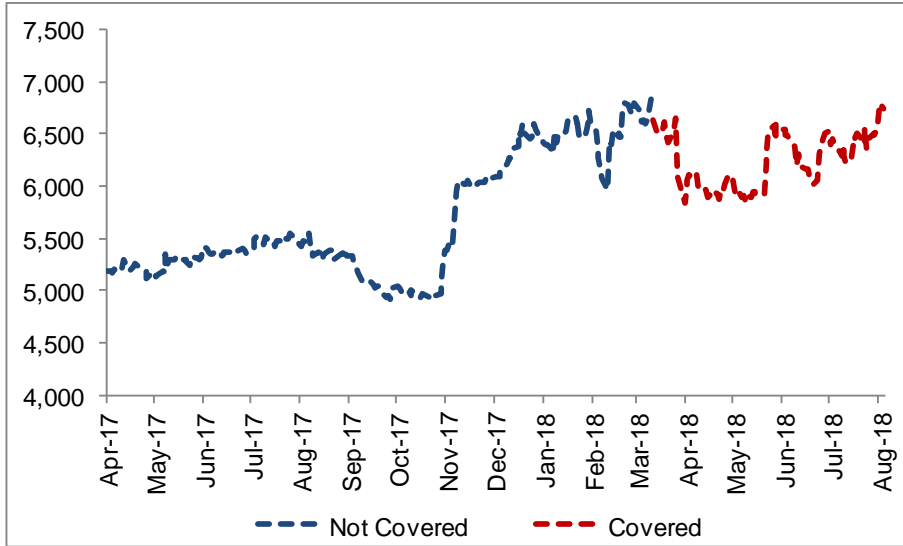
Y/E March	FY16	FY17	FY18	FY19E	FY20E
Per share (Rs)					
EPS	163.4	156.1	166.5	197.9	213.9
Book value	665.5	742.5	828.7	931.6	1,048.0
DPS	55.0	70.0	74.9	79.2	81.3
Valuation (x)					
P/Sales	6.1	5.4	6.2	6.0	5.4
EV/sales	5.5	4.7	5.4	5.1	4.5
EV/EBITDA	26.9	22.3	26.5	23.4	20.8
P/E	36.9	33.0	38.5	33.9	31.3
P/BV	9.1	6.9	7.7	7.2	6.4
Return ratios (%)					
RoCE	31.7	25.9	24.7	26.0	25.2
RoE	28.0	22.2	21.2	22.5	21.6
Profitability ratios (%)					
Gross margin	67.5	67.5	66.8	68.4	68.0
EBITDA margin	20.4	20.9	20.4	21.7	21.6
EBIT margin	18.9	19.3	18.9	20.4	20.2
PAT margin	24.2	23.9	23.5	25.4	25.1
Liquidity ratios (%)					
Current ratio	2.6	2.6	2.6	2.8	2.7
Quick ratio	2.3	2.3	2.4	2.6	2.5
Solvency ratio (%)					
Debt to Equity ratio	-	-	-	-	-
Turnover ratios					
Total asset turnover ratio (x)	0.6	0.8	0.8	0.8	0.8
Fixed asset turnover ratio (x)	7.8	7.4	8.4	8.6	9.2
Inventory days	126.0	129.8	110.9	105.0	105.0
Debtors days	29.5	30.9	25.4	22.0	22.0
Creditor days	209.9	233.7	243.4	245.0	248.0

Source: Company, Nirmal Bang Institutional Equities Research

Rating track

Date	Rating	Market price (Rs)	Target price (Rs)
13 March 2018	Accumulate	6,837	7,300
14 May 2018	Accumulate	5,919	6,700
10 August 2018	Accumulate	6,655	6,850

Rating track graph



Disclaimer

Stock Ratings Absolute Returns

BUY > 15%

ACCUMULATE -5% to 15%

SELL < -5%

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