

Gillette India

14 May 2018

Reuters: GILE.NS; Bloomberg: GILL IN

Transition Blues

Gillette India's (GILL) 3QFY18 performance was significantly below our expectations mainly on account of the exceptional base quarter, transition from 28% to 18% GST regime and focus on higher media spends. Although there was a decline in revenues and profitability during the quarter, our channel checks indicate that the underlying trends in grooming are fairly strong and we believe the long-term story led by premiumisation and margin expansion is intact. Gross margin has shown a robust 460bps YoY margin expansion in 9MFY18. Oral care segment's performance has been satisfactory, both on the top-line and profitability fronts. In our view, higher media spending is positive wherein the market leader is exploiting the business opportunity to gain further share in the fastest-growing category. It is to be noted that GILL's quarterly performance has always been volatile and it is incorrect to judge its performance based on a quarter of decline. Therefore, we have retained Buy rating on GILL with a revised target price of Rs7,600 (from Rs8,000 earlier) based on FY20E EPS, indicating an upside of 16% from the CMP.

GST-related transition hurts the grooming sales: On the back of strong base quarter and GST-related transition wherein GILL had to pare high-priced stocks in the channel, the top-line of the company declined 14% YoY during the quarter. Comparable sales growth YTD (nine months) was above 5%. Sales from the grooming category on a reported basis were down 22% (on the base of positive 23%) whereas the oral care category grew 17% YoY. Our channel checks indicate that the underlying trend in grooming is fairly strong. Also, we believe that higher media spending is a positive sign wherein the market leader clearly sees the opportunity to grow and gain further share.

Margin contraction on account of higher media spends: Low growth in grooming (high-margin business) business resulted in a change in the product mix compared to the base quarter. However, gross margin continued to show improvement which reflects the premiumisation trend shaping out in the category. In 9MFY18, gross margin has shown a robust improvement of 460bps YoY. EBIT margin of grooming and oral care businesses stood at 22.8% and 25.2%, respectively, during the quarter. GILL ramped up its media spending mainly in the grooming category. Hence, EBITDA for the quarter declined 26% YoY. It is to be noted that the base quarter was an exceptional quarter wherein the company massively cut down its media spending (much lower than in the past) and hence the margin in grooming business therein is not comparable. Strong oral care segment's performance during the past few quarters has been supported by healthy margin improvement compared to previous years which will contribute towards blended margin expansion.

Outlook and valuation: We believe that one quarter of subdued performance on account of GST-related transition and an unfavourable base effect will not hurt the long-term growth story of men's grooming business in India and GILL being the market leader will remain the biggest beneficiary. Low per capita spending and premiumisation will continue to remain the key tailwinds for the industry. Also, in our opinion, the new young leadership will work in GILL's favour. Therefore, we have retained our Buy rating on GILL with a revised target price of Rs7,600 (from Rs 8,000 earlier), indicating an upside of 16% from the CMP, based on FY20E EPS and earnings multiple of 60x after revising our earnings estimates.

BUY

Sector: FMCG

CMP: Rs6,532

Target Price: Rs7,600

Upside: 16%

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Key Data

Current Shares O/S (mn)	32.6
Mkt Cap (Rsbn/US\$bn)	212.6/3.2
52 Wk H / L (Rs)	7,197/4,550
Daily Vol. (3M NSE Avg.)	4,561

Price Performance (%)

	1 M	6 M	1 Yr
Gillette India	(0.3)	9.1	36.7
Nifty Index	3.7	4.7	14.7

Source: Bloomberg

Y/E June (Rsmn)	3QFY17	2QFY18	3QFY18	YoY (%)	QoQ (%)	9MFY17	9MFY18	YoY (%)
Net sales	5,249	4,075	4,515	(14.0)	10.8	13,260	12,671	(4.4)
COGS	2,267	1,681	1,870	(17.5)	11.2	6,060	5,212	(14.0)
% of sales	43.2	41.3	41.4	(180bps)	10bps	45.7	41.1	(460bps)
Gross margin %	56.8	58.7	58.6	180bps	(10bps)	54.3	58.9	460bps
Employee costs	360	246	299	(17.1)	21.7	906	824	(9.1)
% of sales	6.9	6.0	6.6	(20bps)	60bps	6.8	6.5	(30bps)
Advertising costs	512	569	612	19.5	7.6	1,578	1,640	3.9
% of sales	9.8	14.0	13.6	380bps	(40bps)	11.9	12.9	100bps
Other expenses	514	600	554	7.7	(7.8)	1,572	1,778	13.0
% of sales	9.8	14.7	12.3	250bps	(250bps)	11.9	14.0	220bps
EBITDA	1,595	979	1,181	(26.0)	20.6	3,144	3,219	2.4
EBITDA margin %	30.4	24.0	26.1	(420bps)	210bps	23.7	25.4	170bps
Depreciation	84	99	115	36.6	15.3	248	306	23.0
EBIT	1,511	880	1,066	(29.5)	21.2	2,895	2,913	0.6
EBIT margin %	28.8	21.6	23.6	(520bps)	200bps	21.8	23.0	120bps
Other income	84	20	11	(87.4)	(47.0)	329	42	(87.3)
PBT	1,575	886	1,068	(32.2)	20.6	3,184	2,921	(8.2)
Tax	517	298	355	(31.3)	19.2	1,030	977	(5.1)
Effective tax rate %	33	34	33	40bps	(40bps)	32	33	110bps
PAT	1,058	588	713	(32.6)	21.3	2,154	1,944	(9.7)
PAT margin %	19.8	14.4	15.8	(410bps)	140bps	15.9	15.3	(60bps)
EPS	32.3	18.0	21.9	(32.3)	21.3	65.7	59.6	(9.2)

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 1: Financial summary

Y/E June (Rsmn)	FY16	FY17	FY18E	FY19E	FY20E
Net sales	17,552	17,336	17,552	19,728	22,660
YoY growth (%)	(11.1)	(1.2)	1.2	12.4	14.9
EBITDA	3,051	3,816	4,634	5,382	6,419
EBITDA margin (%)	17.4	22.0	26.4	27.3	28.3
Reported PAT	2,123	2,531	2,796	3,377	4,145
EPS	65.1	77.7	85.8	103.6	127.2
YoY change (%)	34.3	19.2	10.5	20.8	22.7
RoCE (%)	32.7	47.8	75.2	72.1	71.0
RoE (%)	25.3	35.2	50.2	49.7	49.9
P/E (x)	68.1	65.8	76.1	63.0	51.4
P/B (x)	15.4	33.3	34.8	28.5	23.3
EV/EBITDA (x)	45.7	43.3	45.5	38.6	32.4

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 2: Our estimates versus actual performance

Y/E June (Rsmn)	3QFY17	2QFY18	3QFY18	YoY (%)	QoQ (%)	NBIE estimate	Variation (%)
Net sales	5,249	4,075	4,515	(14.0)	10.8	5,424	(16.8)
EBITDA	1,595	979	1,181	(26.0)	20.6	1,709	(30.9)
EBITDA (%)	30.4	24.0	26.1	(420bps)	(210bps)	31.5	(540bps)
PAT	1,058	588	713	(32.6)	21.3	1,061	(32.8)

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 3: Change in our estimates

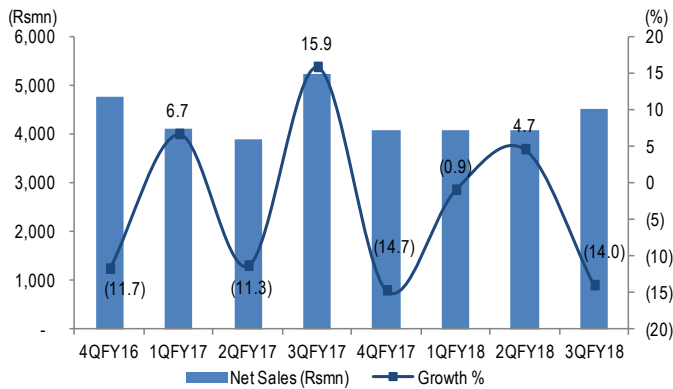
Y/E June (Rsmn)	Old estimates			New estimates			Change (%)		
	FY18E	FY19E	FY20E	FY18E	FY19E	FY20E	FY18E	FY19E	FY20E
Net sales	18,169	20,713	23,699	17,552	19,728	22,660	(3.4)	(4.8)	(4.4)
EBITDA	4,794	5,604	6,657	4,634	5,382	6,419	(3.3)	(4.0)	(3.6)
EBITDA (%)	26.4	27.1	28.1	26.4	27.3	28.3	-	20bps	20bps
PAT	3,006	3,630	4,361	2,796	3,377	4,145	(7.0)	(7.0)	(5.0)

Source: Company, Nirmal Bang Institutional Equities Research

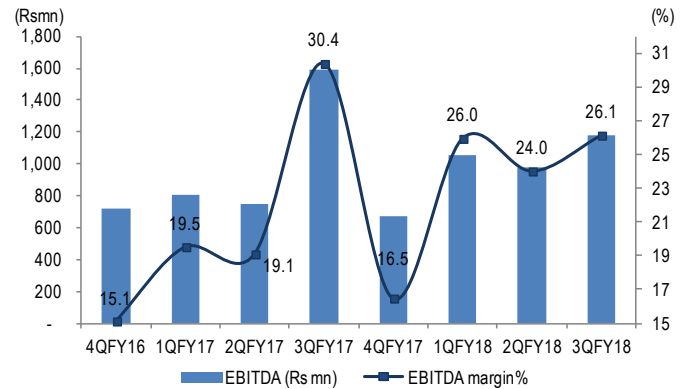
Exhibit 4: Segment-wise performance

Description	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18
Net sales (Rsmn)							
Grooming	3,363	3,133	4,501	3,410	3,089	3,322	3,530
Oral care	830	835	844	966	992	754	985
Total	4,193	3,968	5,345	4,376	4,080	4,075	4,515
Sales proportion (%)							
Grooming	80.2	79.0	84.2	77.9	75.7	81.5	78.2
Oral care	19.8	21.0	15.8	22.1	24.3	18.5	21.8
Growth (%)							
Grooming	11.7	(9.1)	23.0	(16.7)	(8.1)	6.0	(21.6)
Oral care	(6.4)	(15.2)	(8.5)	28.7	19.4	(9.8)	16.7
EBIT (Rsmn)							
Grooming	665	686	1,347	318	801	744	805
Oral care	74	(25)	194	213	170	143	249
Total	740	661	1,541	531	971	887	1,053
EBIT margin (%)							
Grooming	19.8	21.9	29.9	9.3	25.9	22.4	22.8
Oral Care	8.9	(3.0)	22.9	22.0	17.2	19.0	25.2
Capital employed (Rsmn)							
Grooming	3,365	3,302	2,514	2,850	3,451	3,766	3,960
Oral care	162	(30)	(67)	37	(82)	(23)	5
Unallocated	6,375	6,406	8,284	2,119	2,264	2,067	2,606
Total	9,901	9,677	10,732	5,006	5,632	5,810	6,571

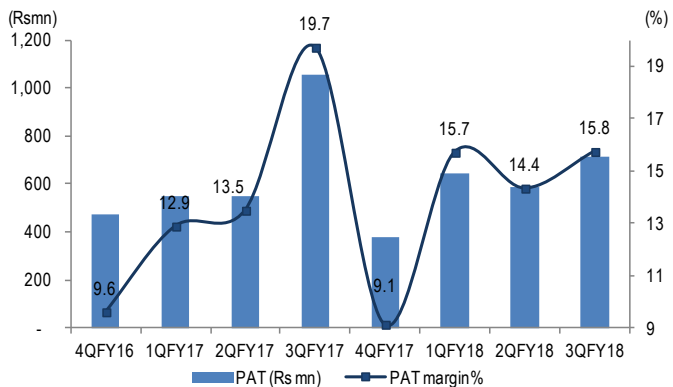
Note: As the previous quarters are not reclassified as per the new accounting treatment under the GST regime, the reported numbers as mentioned above are not comparable. Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 5: Top-line growth trend


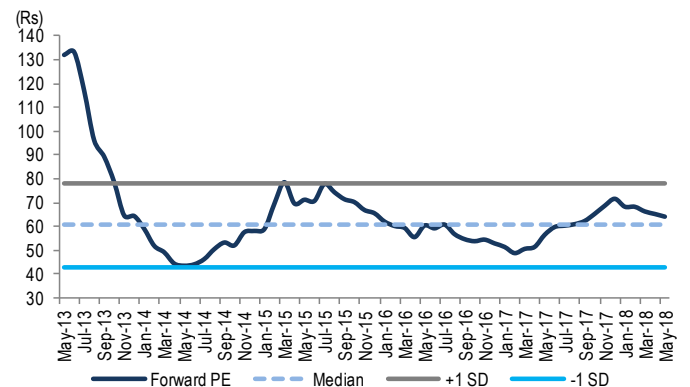
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 6: Operating margin profile


Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 7: Net income vis-à-vis margins


Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 8: One-year forward P/E


Source: Company, Nirmal Bang Institutional Equities Research

Financials

Exhibit 9: Income statement

Y/E June (Rsmn)	FY16	FY17	FY18E	FY19E	FY20E
Net sales	17,552	17,336	17,552	19,728	22,660
% Growth	(11.1)	(1.2)	1.2	12.4	14.9
COGS	8,542	7,860	7,228	8,097	9,249
Staff costs	1,068	1,097	1,043	1,133	1,269
Advertising costs	2,387	2,304	2,260	2,537	2,879
Other expenses	2,504	2,259	2,388	2,580	2,843
Total expenses	14,501	13,520	12,918	14,347	16,241
EBITDA	3,051	3,816	4,634	5,382	6,419
% growth	64.7	25.1	21.4	16.1	19.3
EBITDA margin (%)	17.4	22.0	26.4	27.3	28.3
Other income	358	378	53	220	370
Interest costs	53	67	43	50	50
Depreciation	303	384	447	482	520
Profit before tax (before exceptional items)	3,052	3,743	4,197	5,070	6,219
Tax	1,062	1,212	1,401	1,693	2,075
PAT (before exceptional items)	2,123	2,531	2,796	3,377	4,145
PAT	2,123	2,531	2,796	3,377	4,145
<i>PAT margin (%)</i>	<i>11.9</i>	<i>14.3</i>	<i>15.9</i>	<i>16.9</i>	<i>18.0</i>
% Growth	34.3	19.2	10.5	20.8	22.7

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 11: Balance sheet

Y/E June (Rsmn)	FY16	FY17	FY18E	FY19E	FY20E
Share capital	326	326	326	326	326
Reserves	9,040	4,680	5,798	7,149	8,807
Net worth	9,366	5,006	6,124	7,475	9,133
Total debt	-	-	-	-	-
Deferred tax liability	(150)	(190)	(190)	(190)	(190)
Total liabilities	9,252	4,863	5,970	7,321	8,979
Gross block	4,909	5,659	6,409	7,159	7,909
Depreciation	3,051	3,435	3,881	4,363	4,883
Net block	1,858	2,224	2,527	2,796	3,026
Capital work-in-progress	882	633	750	750	750
Investments	-	-	-	-	-
Inventories	2,446	2,224	1,737	2,434	2,128
Debtors	1,098	1,303	909	1,036	1,074
Cash	5,372	1,157	2,088	5,294	5,050
Loans & advances	703	299	2,188	597	2,590
Other current assets	396	260	260	260	260
Total current assets	9,733	4,985	5,035	9,065	8,553
Creditors	3,211	3,227	2,713	3,808	3,490
Other current liabilities & provisions	1,632	1,704	1,776	2,037	2,409
Total current liabilities	4,843	4,932	4,489	5,845	5,899
Net current assets	4,890	53	546	3,220	2,655
Total assets	9,252	4,863	5,970	7,321	8,979

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 10: Cash flow

Y/E June (Rsmn)	FY16	FY17	FY18E	FY19E	FY20E
PAT	2,123	2,531	2,796	3,377	4,145
Depreciation	303	384	447	482	520
Other income	(358)	(378)	(53)	(220)	(370)
(Inc./dec.) in working capital	2398	622	438	532	322
Cash flow from operations	4,519	3,225	3,671	4,221	4,666
Capital expenditure (-)	(849)	(501)	(867)	(750)	(750)
Net cash after capex	3,669	2,724	2,805	3,471	3,916
Dividends paid (-)	-	-	-	-	-
	976	6,890	1,678	2,026	2,487
Inc./(dec.) in total borrowings	-	-	-	-	-
Inc./(dec.) in investments	-	-	-	-	-
Cash from financial activities	(1,094)	(6,987)	(1,732)	(2,076)	(2,537)
Opening cash balance	1,813	5,372	1,157	2,088	5,294
Closing cash balance	5,372	1,157	2,088	5,294	5,050
Change in cash balance	3,559	(4,215)	931	3,206	-244

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 12: Key ratios

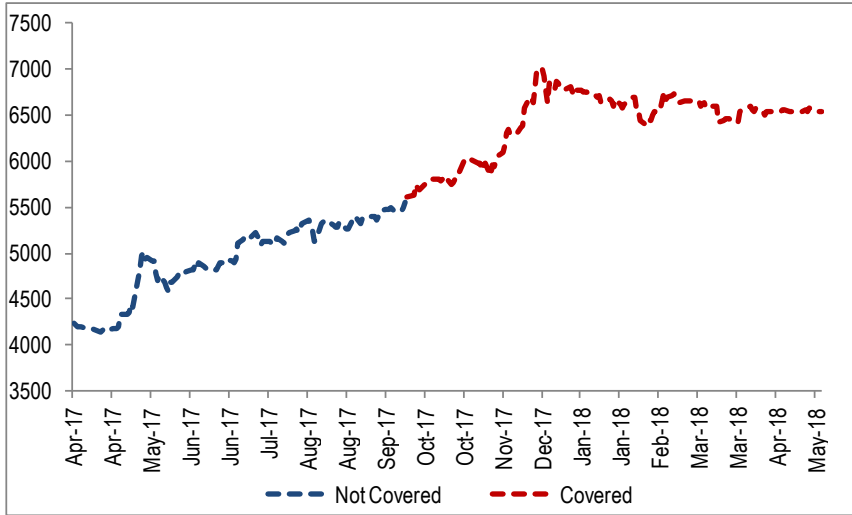
Y/E June	FY16	FY17	FY18E	FY19E	FY20E
Per share (Rs)					
EPS	65.1	77.7	85.8	103.6	127.2
Book value	287.4	153.6	187.9	229.4	280.2
DPS	24.9	176.2	42.9	51.8	63.6
Valuation (x)					
P/Sales	8.2	9.6	12.1	10.8	9.4
EV/sales	7.9	9.5	12.0	10.5	9.2
EV/EBITDA	45.7	43.3	45.5	38.6	32.4
P/E	68.1	65.8	76.1	63.0	51.4
P/BV	15.4	33.3	34.8	28.5	23.3
Return ratios (%)					
RoCE	32.7	47.8	75.2	72.1	71.0
RoE	25.3	35.2	50.2	49.7	49.9
Profitability ratios (%)					
Gross margin	51.3	54.7	58.8	59.0	59.2
EBITDA margin	17.4	22.0	26.4	27.3	28.3
EBIT margin	15.7	19.8	23.9	24.8	26.0
PAT margin	17.0	21.1	23.8	25.4	27.0
Liquidity ratios (%)					
Current ratio	2.0	1.0	1.1	1.6	1.5
Quick ratio	1.5	0.6	0.7	1.1	1.1
Solvency ratio (%)					
Debt-to-equity ratio	-	-	-	-	-
Turnover ratios					
Total asset turnover ratio (x)	1.2	1.8	1.7	1.5	1.5
Fixed asset turnover ratio (x)	9.9	8.1	6.9	7.1	7.5
Debtor days	24	25	23	18	17
Inventory days	95	108	100	94	90
Creditor days	126	149	150	147	144

Source: Company, Nirmal Bang Institutional Equities Research

Rating track

Date	Rating	Market price (Rs)	Target price (Rs)
29 September 2017	Buy	5,640	7,000
14 November 2017	Buy	5,861	7,000
12 February 2018	Buy	6,546	8,000
14 May 2018	Buy	6,532	6,700

Rating track graph



Disclaimer

Stock Ratings Absolute Returns

BUY > 15%

ACCUMULATE -5 to 15%

SELL < -5%

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