



India Equities
Food and Dairy Products

Quarterly Update

GlaxoSmithkline Consumer Healthcare Ltd

BUY

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CMP **Rs 1,800**
Target Price **Rs 2,129**

Investment horizon 12 months
Sensex 18,115
Nifty 5,440

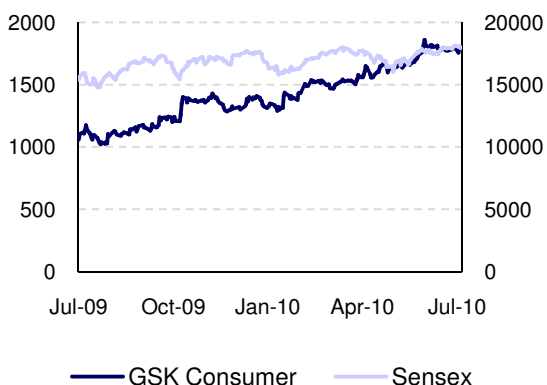
Stock Details

BSE Code 500676
NSE Code GSKCONS
Reuters Code GLSM.BO
Bloomberg Code SKB IN
Market Cap (Rs cr) 7,570.0
Beta 0.33
52 W High / Low (Rs) 1,895.0 / 1,005.0
Avg Daily Volume 7,395
Face Value (Rs) 10.00

Shareholding Pattern (%)

Promoters 43.16
MF/Banks/Indian FIs 20.51
FII / NRIs / OCBs 19.13
Indian Public 17.20

Price Chart



Performance Highlights

Revenues up 14.5% yoy on volume growth and price increase:

GlaxoSmithKline Consumer Healthcare Limited (GSK Consumer) showed a 14.5% yoy growth in net sales to Rs 537.4cr on account of 10% volume growth and 5% growth via price hikes. The Horlicks and Boost brands showed 10% and 17% volume growth, respectively. The net sales growth was impacted due to rise in raw material costs, hike in excise duty and decline in exports. The distribution network has also been expanding and the company targets to have a direct coverage of 6 lakh outlets by CY2010 end.

Operating margin maintained while PAT margin goes up:

The EBIDTA margin remained almost flat at 18.9% during Q2CY2010. The rise in raw material costs was offset by a decline in employee expenditure and A&P expenses during the quarter. The PAT margin was, however, up at 13.0% due to decline in depreciation cost and effective tax rate. The net profit for the quarter was up 30.0% to Rs 71.8cr in Q2CY2010.

Valuation: We have used Relative Valuation based on average of EV/EBIDTA and Price/Earnings (P/E) ratios. The stock is currently trading at EV/EBIDTA of 17.0xCY2010E and P/E of 25.0xCY2010E earnings. The sales growth is expected to improve in H2CY2010 on account of softening of raw material prices with a decline in food inflation. **We maintain Buy on the stock with a Target Price of Rs 2,129.**

Exhibit 1: Quarterly Financials

| Particulars | Rs cr | | | | |
|--------------------------|----------|----------|--------|----------|--------|
| | Q2CY2010 | Q2CY2009 | YoY(%) | Q1CY2010 | QoQ(%) |
| Revenue | 552.5 | 486.2 | 13.6 | 664.0 | (16.8) |
| Other Income | 12.9 | 5.8 | 122.6 | 8.0 | 62.0 |
| Total Income | 565.4 | 492.0 | 14.9 | 672.0 | (15.9) |
| Total Expenditure | 448.0 | 394.6 | 13.5 | 515.4 | (13.1) |
| EBIDTA | 104.5 | 91.6 | 14.1 | 148.7 | (29.7) |
| <i>EBIDTA Margin (%)</i> | 18.9 | 18.8 | - | 22.4 | - |
| Depreciation | 9.3 | 10.5 | (11.9) | 9.6 | (3.0) |
| EBIT | 108.2 | 86.9 | 24.5 | 147.1 | (26.4) |
| Interest | 0.6 | 1.1 | (41.0) | 0.6 | 8.8 |
| Profit before Tax | 107.6 | 85.8 | 25.3 | 146.5 | (26.6) |
| Tax | 35.8 | 30.7 | 16.8 | 50.3 | (28.9) |
| Net Profit | 71.8 | 55.2 | 30.0 | 96.2 | (25.4) |
| <i>PAT Margin (%)</i> | 13.0 | 11.4 | - | 14.5 | - |
| EPS | 17.1 | 13.1 | 30.0 | 22.9 | (25.4) |

Source: Company data, Parsoli Research; *CY - Financial year ending December



GSK Consumer's sales grew 14.5% yoy to Rs 537.4cr during Q2CY2010 on account growth in volumes by 10.0% and price hike by 5%

The rise in raw material prices was offset by decline in employee and A&P expenses resulting in flat EBIDTA margin

Key Updates

Revenues driven by volume growth and price hike

During Q2CY2010, the company's sales were up 14.5% yoy to Rs 537.4cr as compared to Rs 469.4cr in Q2CY2009. The quarter saw 10% growth by volumes and 5% growth by way of price hikes. During the quarter, Horlicks (company's flagship brand) grew 10% in terms of volume and Boost saw a 17% volume growth. In addition, to offset the increase in prices of raw materials (including milk, sugar, barley, etc.), the company took a price hike of 5%. The quarterly revenues were also impacted by the 2% hike in excise duty from 8% to 10% announced in the Union Budget. However, Boost has benefitted from the company's efforts to expand its distribution pan-india. GSK Consumer had a direct coverage of around 5 lakh retail outlets in CY2009 and the company targets to expand it to 6 lakh outlets by CY2010 end. Its indirect coverage spans over 9.5lac outlets pan-India. Going forward, the growth looks to be primarily volume driven as the company would not desire to take further price hikes in order to sustain demand. For 6mCY2010, the net sales have grown by 17.0% yoy to Rs 1,216.5cr from Rs 1,039.9cr for 6mCY2010.

Exports, which contribute 8% of net sales, grew by only about 3% yoy during the quarter as compared to 27% yoy growth last quarter. The management indicated that the steep fall in growth was on account of increased competitive pressure in Sri Lanka, which is a key export market for the company.

EBIDTA margin remained flat; PAT margin up 163bps yoy

Due to the continued impact of high food inflation in key raw materials including liquid milk (prices up 25% yoy and 10% qoq), milk powder (prices up 15% yoy and 9% qoq), sugar (prices up 50% yoy); the company's operating profit margin remained almost flat at 18.9% during the quarter. The raw material expenses (as percentage of net sales) went up by 202bps yoy to 26.9%. However, the hike in raw material expenditure was offset by 11bps yoy decline in employee expenses and 182bps yoy decline in A&P (advertisement and promotion) expenditure. The A&P expenses were high in CY2009 on account of the number of launches made by the company across the health food category including Glaxo Nutrition's ActiGrow, Horlicks NutriBar, Junior Horlicks Biscuits, Horlicks Asha, Horlicks Cornflake Crunchies Biscuits, Horlicks Foodles and Horlicks ProHeight.

| | Exhibit 2: Cost Analysis | | | % of sales |
|-------------------|--------------------------|----------|----------------|------------|
| | Q2CY2010 | Q2CY2009 | bps change yoy | |
| Material Expenses | 26.9 | 24.9 | 202 | |
| Employee Expenses | 10.7 | 10.8 | (11) | |
| A&P Expenses | 13.5 | 15.4 | (182) | |
| Total Expenditure | 81.1 | 81.2 | (7) | |

Source: Company data, Parsoli Research

Going forward, the management expects milk prices to strengthen further during Q3CY2010 and come down only in Q4CY2010. The sugar prices are expected to soften during H2CY2010.



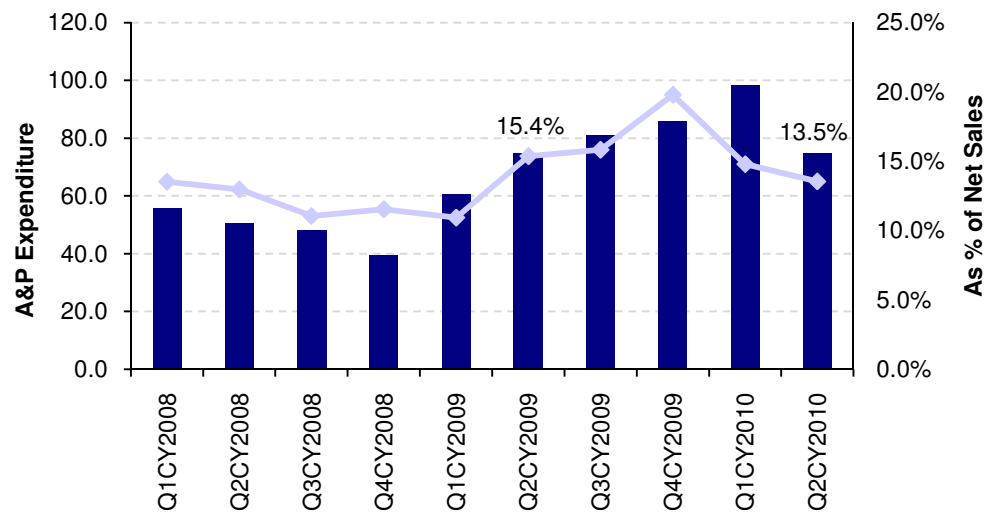
The A&P expenses declined by 182bps yoy to 13.5% in Q2CY2010 and, going forward, the management expects them to stay at around 14-15%

During Q2CY2010, while the operating profit margin remained flat, the PAT margin increased by 163bps yoy to 13.0% as against 11.4% in Q2CY2009. The increase was mainly on account of a decline in depreciation expenses during CY2010 and a reduction in tax rate. The abolishment of fringe benefit tax (FBT) and a reduction in the surcharge rate decreased the effective tax rate. Overall, the net profit increased by 30.0% yoy to Rs 71.8cr in Q2CY2010 as compared to Rs 55.2cr in Q2CY2009.

A&P expenses stabilize

While in Q2CY2009, the A&P expenditure (as % of net sales) was high on account of expenses incurred in promoting new launches. The A&P expenses on a yoy basis have come down by 182bps in Q2CY2010. The company now looks to strengthen the market position of the new product launches. Going forward, the management expects the A&P expenses to stay at around 14-15% of net sales.

Exhibit 3: A&P expenditure



Source: Company data, Parsoli Research

The newly launched Foodles has been able to capture market share of 5% and 4% in South and East India, respectively

Performance across product categories

GSK Consumer adopted an aggressive product launch drive during CY2009 in order to diversify its operations and stay in focus of the target of doubling CY2007 revenues of Rs 1,278.5cr by CY2011. The company had launched Foodles, an instant multi-grain noodles brand, in South and East India and has now captured 5% and 4% market share, respectively. The product is available across two price points, Rs 15 pack which is the multi-grain (wheat) variant and the Rs 10 pack which is the maida variant. The company plans to launch the brand in North and West India during the next quarter.

According to the management, the Horlicks Nutribar has just established its pan India presence and the company may introduce new variants, depending on the success of the brand in future. Horlicks Asha which was test marketed in Andhra Pradesh has not been launched across India as the company still awaits the results of test marketing. The Chill Doodh brand has been planned to be kept only under modern retail for now.



We expect GSK Consumer's revenues to grow at a CAGR of 20.9% during CY2009-11 to reach a turnover of Rs 2,809.4cr by CY2011

We maintain Buy on the stock with a target price of Rs 2,129

Outlook & Valuation

GSK Consumer's performance in CY2010 has been affected by the food inflation pressures. The company did undertake price rise to offset the rise in raw material costs. Going forward, the raw material prices are expected to remain strong in Q3CY2010 and likely to come down in Q4CY2010. The management has indicated that company's focus would be on expanding distribution network, expanding into new categories and driving growth via product innovation. Horlicks continues to be the key brand and the Malted food drinks (MFD) category a key revenue generator contributing 90-95% of total sales. The remaining sales are contributed by the biscuits category. However, to diversify its revenues across categories and present itself as a leading player in the healthy food segment, the company has forayed into new categories with products like Nutribar, Foodles, etc. While the company's performance across new categories would become more clear by CY2010 end, we expect the company's revenues to increase at a CAGR of 20.9% (CY2009-11E) to Rs 2,809.4cr by CY2011. GSK Consumer is moving well in-line with its goal to double CY2007 revenues by CY2011. The company plans to continue to promote its new brands and leverage Horlicks' brand equity to establish itself in new categories. In addition, the company is expanding its distribution network to directly cover 6 lakh retail outlets and has an indirect coverage of 9.5 lakh outlets. The expanded distribution would be key to increasing GSK Consumer's revenues in the rural market, which currently contribute about 33% of total sales.

Relative Valuation

GSK Consumer currently trades at an EV/EBIDTA multiple of 17.0xCY2010E and 12.9xCY2011E. When considering the industry average of 29.2x, the stock trades at a discount of 32.6%. Going forward, we believe that GSK Consumer will be able to expand its EBIDTA margin from 16.0% in CY2009 to 16.8% in CY2010. We have assigned a multiple of 21.0 to value the stock, which is at a 39.1% discount to the industry average. Using this target multiple on our CY2010 EBIDTA estimates of Rs 390.7cr, we arrive at a target price of Rs 2,169 per share.

When considering the P/E multiple, the stock currently trades at 25.0xCY2010E and 20.0xCY2011E earnings. The industry average multiple for the peer group stands at 37.7x. We expect the company's EPS to grow at a CAGR of 27.4% during CY2009-11 to touch Rs 89.9 by CY2011. We are assigning a multiple of 29.0 to value the stock. Employing this target multiple on our CY2010 EPS estimates of Rs 72.0, we arrive at a target price of Rs 2,088.

We give a price target of Rs 2,129 for the stock representing an upside of 18.3%.

Exhibit 4: Valuation Summary

| Pricing Methodologies | Weight Assigned | Target Price |
|---------------------------------------|------------------------|---------------------|
| Target price using EV/EBIDTA approach | 50.0% | 2,169.2 |
| Target price using P/E approach | 50.0% | 2,088.1 |
| Weighted average target price (Rs) | | 2,128.6 |
| Current Market Price (CMP) | | 1,800.0 |
| Upside from current levels (%) | | 18.3 |

Source: Company data, Parsoli Research



Financial Statements

| Exhibit 5: Profit & Loss Statement | | | | | Rs cr |
|------------------------------------|---------|---------|---------|---------|---------|
| | CY2007 | CY2008 | CY2009 | CY2010E | CY2011E |
| Net Sales | 1,278.5 | 1,541.8 | 1,921.5 | 2,321.8 | 2,809.4 |
| <i>% chg</i> | 15.4 | 20.6 | 24.6 | 20.8 | 21.0 |
| Total Expenditure | 1,053.7 | 1,309.6 | 1,614.9 | 1,931.1 | 2,309.3 |
| <i>% chg</i> | 14.1 | 24.3 | 23.3 | 19.6 | 19.6 |
| EBIDTA | 224.7 | 232.2 | 306.6 | 390.7 | 500.1 |
| <i>Margin (%)</i> | 17.6 | 15.1 | 16.0 | 16.8 | 17.8 |
| Other Income | 68.5 | 95.5 | 89.3 | 104.5 | 140.5 |
| Depreciation & Amortisation | 43.5 | 41.9 | 42.0 | 37.0 | 69.2 |
| Interest | 4.6 | 0.0 | 0.0 | 2.2 | 2.0 |
| PBT | 245.1 | 285.7 | 353.9 | 456.0 | 569.3 |
| <i>Margin (%)</i> | 19.2 | 18.5 | 18.4 | 19.6 | 20.3 |
| Total Tax | 82.4 | 97.4 | 121.1 | 153.2 | 191.3 |
| <i>(% of PBT)</i> | 33.6 | 34.1 | 34.2 | 33.6 | 33.6 |
| PAT | 162.7 | 188.3 | 232.8 | 302.8 | 378.0 |
| <i>% chg</i> | 28.2 | 15.8 | 23.6 | 30.1 | 24.8 |
| <i>Margin (%)</i> | 12.7 | 12.2 | 12.1 | 13.0 | 13.5 |

Source: Company data, Parsoli Research; *CY - Financial year ending December

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