



India Equities  
FMCG

Initiating Coverage

## Godrej Consumer Products Limited

**BUY**

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**CMP** **Rs 256**  
**Target Price** **Rs 316**

Investment horizon 12 months  
Sensex 16,994  
Nifty 5,089

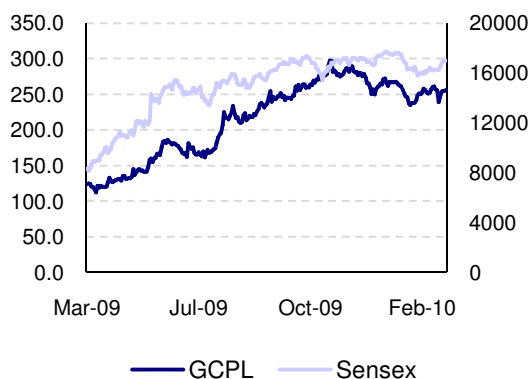
### Stock Details

BSE Code 532424  
NSE Code GODREJCP  
Reuters Code GOCP.BO  
Bloomberg Code GCPL IN  
Market Cap (Rs cr) 7,893.4  
Beta 0.15  
52 W High / Low (Rs) 304.0 / 110.5  
Avg Daily Volume 61,293  
Face Value (Rs) 1.00

### Shareholding Pattern (%)

Promoters 73.51  
MF/Banks/Indian FIs 1.11  
FII / NRIs / OCBs 18.49  
Indian Public 6.89

### Price Chart



### Investment Rationale

**New product launches with presence at multiple price points:** Godrej Consumer Products Limited (GCPL) has been aggressively launching new variants of existing products as well as entering into new product categories. Alongside the launch of new variants in soaps and hair colour categories, the company recently forayed into the hand hygiene category. Also, in order to tap the rural demand, GCPL has been introducing low-price packs and aims to expand its distribution network to 8,000 small towns and 50,000 villages across India. Through these efforts, the company aims to increase its revenues from the rural markets which are an emerging growth engine, from the current 42.0% to 50.0% of revenues.

**Growth via acquisitions to be value accretive:** GCPL is aggressively targeting acquisitions in the personal care, hair colour and household insecticide categories. The company is looking to acquire businesses across these categories in India and other developing nations where it already holds a presence. In view of this strategy, the company is aiming to acquire the 51.0% Sara Lee's stake in the joint venture (JV) company Godrej Sara Lee. The acquisition, if completed, will not only help the company in increasing the revenues, but will also be EPS accretive.

**Valuation:** We have used Relative Valuation based on EV/EBIDTA and Price/Earnings (P/E) multiple methods. For valuing the stock, we have taken the average price arrived from the above two methodologies. GCPL currently trades at an EV/EBIDTA multiple of 20.7x FY2010E and 16.8x FY2011E and P/E multiple of 24.2x FY10E earnings and 20.7x FY2011E earnings. Considering the company's focus on rural markets and growth via acquisitions, **we recommend a Buy on the stock considering a 12 month investment horizon with a Target Price of Rs 316.**

### Exhibit 1: Financial Summary

Particulars	FY2008	FY2009	FY2010E	FY2011E	FY2012E
Net Sales (Rs cr)	1102.57	1392.96	2014.47	2433.97	2932.19
Total Income (Rs cr)	1108.57	1436.58	2061.26	2482.65	2990.84
PAT (Rs cr)	159.24	172.62	326.04	381.94	457.77
PAT Margin (%)	14.4	12.4	16.2	15.7	15.6
EBIDTA Margin (%)	19.5	14.6	19.5	19.7	19.7
EPS (Rs)	7.1	6.8	10.6	12.4	14.9
P/E (x)	17.6	19.5	24.2	20.7	17.2
P/BV (x)	7.7	4.0	8.3	7.5	6.4
RoE (%)	92.8	30.5	47.8	47.1	46.7
RoCE (%)	55.5	26.9	44.0	46.4	47.7
EV/EBIDTA (x)	13.7	14.2	17.2	16.8	13.7
EV/Sales (x)	2.7	2.1	3.3	3.3	2.7

Source: Company data, Parsoli Research



***GCPL offers products at low-price points in the soap and hair colour categories***

***The company is maintaining a strong focus on the rural markets and aims to expand its coverage to 8,000 towns and 50,000 villages***

## **Investment drivers**

### **Presence across categories at multiple price points**

GCPL offers products in the soap and hair colour categories at multiple price points (at Rs 5 and Rs 10) that are, both, attractive and affordable for customers. With the onset of slowdown, the consumers have been increasingly downtrading (opting for smaller packs or cheaper value products) across all the Fast Moving Consumer Goods (FMCG) categories like soaps, laundry, tea, hair care, etc. This has been on account of the continuous rise in food inflation which has led to higher portion of consumer income being taken up by food items. This downtrading has worked in favor of GCPL whose market share in the soaps category has gone up from 9.1% in Q1FY2009 to 10.3% in Q3FY2010. This is because, during FY2009, when most of the other companies in the soap segment suddenly increased their prices on account of a steep increase in commodity prices, GCPL raised prices for Cinthol and Godrej No. 1 at a lower rate and much later than its competitors. This helped the company increase its market share with consumers taking notice and appreciating brands like Godrej No. 1 and FairGlow. Hence, with the increase in market share, the company established a stronger presence in the market, with Cinthol targeting the premium segment and Godrej No.1 and Godrej FairGlow targeting the middle and lower segments.

In the hair colour category also, GCPL offers a range of products including powders, oil-based liquids, creams and lotions in a range of colours like black, burgundy, brown, etc. All the hair colour products are affordably priced and each one targets a separate consumer class with Renew targeting the top end of the market; Expert in the mid-market segment and Nupur and Kali Mehndi targeting the lower segment.

GCPL has been able to offer value to consumers by making its products available at various price points. Alongside, the company has competitively priced its products by charging lower prices compared to peers. This has helped the company in targeting consumers who have becoming price conscious in the current economic environment.

### **Strong focus on rural market**

GCPL is increasingly targeting the demand from the rural markets through a number of initiatives. In May 2009, the company covered around 17,000-18,000 villages and had a network coverage of about 3,300 small towns. The company, in order to increase the rural reach of its products, targets to cover 50,000 villages and cover 8,000 small towns in three years. GCPL has also targeted 50,000 salons and barber shops in semi-urban and rural areas in order to promote its hair care brands like Nupur (mehndi) and Expert (hair colour), soaps and other toiletries. The salons and barber shops showcase the entire range of GCPL's products and serve as a promotional point for these products. The company has placed combipacks which have shaving creams, talcum powder, soaps and hair colours. The effort, according to the management, is a brand building exercise which the company is undertaking in order to have greater and deeper presence across small towns and villages in India. Another effort towards fortifying its rural presence has been through the introduction of low-unit price packs between Rs 5 and Rs 10. The Rs 5 price point is an attractive proposition for rural markets and the company is pushing it aggressively in order to enhance its distribution reach. The rural segment contributes around 42.0% of the total revenues and GCPL is targeting to increase this to 50.0% by capitalizing on the rise in rural disposable income and the swell in rural demand for FMCG products. The company is also advertising heavily on Doordarshan and All India Radio to have a better rural reach. The company's popular soap brand, Godrej No. 1, has focused its advertisement spends only on



***GCPL is looking to acquire the remaining 51.0% stake in GSLL which is expected to be EPS accretive***

***GSLL is a growing business with revenues of Rs 755cr in FY2009 showing a yoy growth of 27.0%***

***GCPL is looking to expand its presence in the personal wash, hair care and household insecticide categories via acquisitions***

Doordarshan rather than the cable and satellite television.

#### **Godrej Sara Lee's acquisition to add value**

GCPL currently holds 49.0% stake in Godrej Sara Lee (GSLL) business, a JV with the U.S. based Sara Lee Corp. Going forward, GCPL is aggressively pursuing to acquire the remaining 51.0% stake in the business. GSLL primarily functions across three business segments, namely, household insecticides, personal care and air care. The product portfolio comprises of GSLL-owned brands like Good Knight, Jet and Hit. GSLL, in addition, manufactures, markets and distributes Sara Lee's international brands like Ambipur car perfume, Kiwi shoe polish and Brylcreem in India. Sara Lee, in order to exit its non-core businesses, has already sold its home care division (comprising Brylcreem) to Unilever and the air care unit (consisting of Ambipur) to Procter & Gamble (P&G). However, the sale of these divisions is not likely to impact the operations of the JV as the licensed brands (which include Ambipur, Kiwi and Brylcreem) will continue to operate under GSLL in India. In case P&G or Unilever want to sell these licensed brands in India, they will first have to buy out the rights. According to the management, the owned brands account for around 85.0% of total JV sales and the licensed brands account for the remaining 15.0%.

According to the JV terms, GCPL enjoys the right of first refusal in GSLL which gives it considerable advantage towards buying out the 51.0% stake in the business. The acquisition is expected to add value to GCPL's operations and also boost the company's profitability. The fact that GSLL has a substantial market presence in India only adds on to the attractiveness of this business. In the household insecticide segment, it enjoys a market share that has grown from 32.4% in September 2008 to 33.2% in September 2009.

The acquisition of the remaining 51.0% stake in GSLL, we believe, will be EPS accretive for GCPL. GSLL is a growing business whose total revenues for FY2009 stood at Rs 755cr, having grown at around 27.0% yoy. For FY2010, we expect the business to continue to perform well and revenues to grow by 23.1% yoy to Rs 929.4cr.

#### **Inorganic growth via domestic and/or international acquisitions**

The company is looking to increase its presence in the personal wash, hair care and household insecticides by targeting acquisitions in the domestic and international market. Towards this, GCPL has also taken the approval from its board to raise upto Rs 3,000cr for mergers and acquisitions. A part of the amount raised (approx. Rs 800cr) is expected to go towards acquiring the remaining 51.0% stake in GSLL. According to the management, the company's top priority for acquisitions (apart from GSLL) would be India followed by acquiring business in countries where GCPL already has its operations (Africa, Middle East, etc.).

*GCPL is a leading FMCG company in India with major presence in the toilet soap and hair colour categories.*

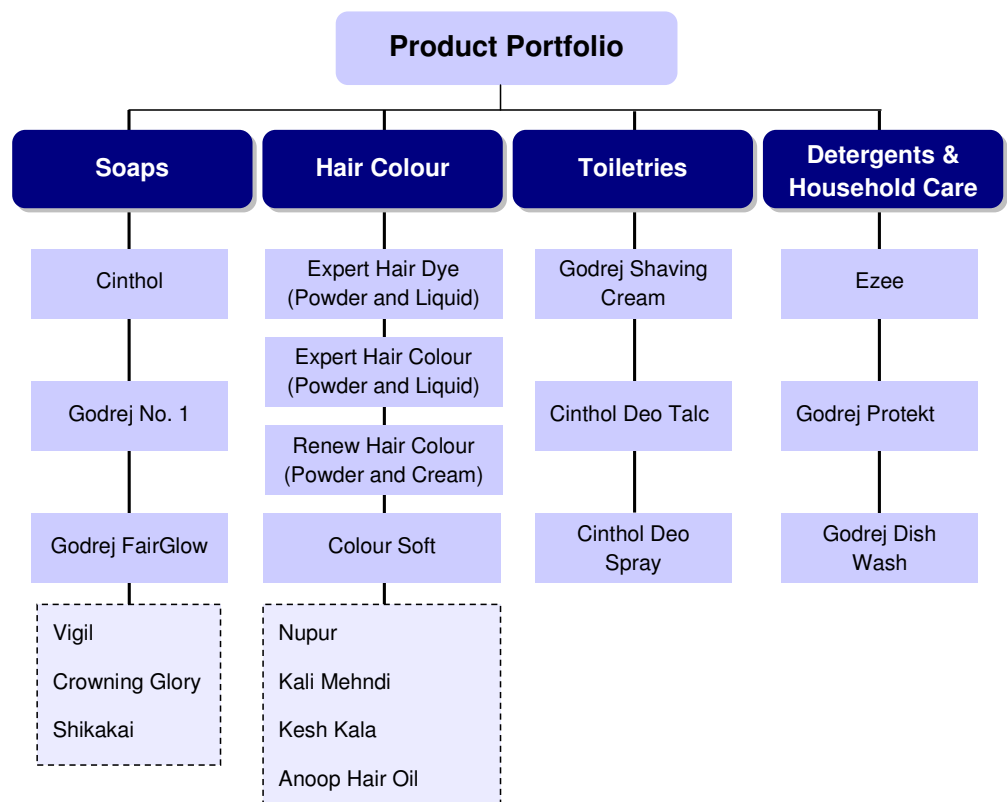
*The company's product portfolio spans across four key categories*

## Company Overview

GCPL, part of the Godrej group, is a leading FMCG company offering personal and household care products in India. The company has a pan-India presence through its branch offices in all the metros and manufacturing facilities at Malanpur (Madhya Pradesh), Baddi-Thana (Himachal Pradesh), Baddi-Katha (Himachal Pradesh), Sikkim and Guwahati (Assam). GCPL is a leading player in the toilet soap category with popular brands like Cinthol, Godrej Fairglow and Godrej No.1. Along with its presence in India, the company owns international brands and trademarks in developed markets including Europe, Australia and Canada.

## Business Structure

**Exhibit 2: Business Structure**



*Source: Company data, Parsoli Research*

## Toilet Soaps

*GCPL's leading brands in the toilet soaps category include Cinthol, Godrej No.1 and FairGlow*

In the soaps category, the company offers a number of products including leading brands like Cinthol, Godrej No.1 and FairGlow. Cinthol is the popular soap brand of GCPL which is available in Cinthol Regular, Fresh (aqua fresh) and Deo (with cologne, classic, sport and musk variants). Godrej No. 1, a leading soap brand of the company, is the largest selling Grade 1 soap in India and has market leadership position in Uttaranchal, Punjab, Haryana, Himachal Pradesh, etc. The product is offered in nine variants which are available at multiple price points. Godrej FairGlow, another Grade 1 soap of GCPL, is available across three variants in 75gm and 125gm sizes.



*In the hair colour segment, the company offers a range of dyes and hair colorants which include Expert, Renew and Colour Soft*

*Godrej Ezee is a market leader in the liquid detergent category with 82.0% market share*

*GCPL holds international presence across Europe, Australia, Canada, Africa and the Middle East region*

### **Hair Colours**

The hair colour segment offers hair dye and hair colour (in powder and liquid forms) under the Expert range. The Expert powder hair dye comes in a convenient size of 3gm sachet and is available across 25lac outlets in India. The Expert liquid hair dye is available in natural black colour in 40ml and 20ml packs. The Expert powder hair colour comes in 3gm sachet in four colours (gentle black, dark brown, natural brown, burgundy) and the Expert liquid hair colour is available in 40ml packs in three colours (gentle black, natural brown, dark brown). The Renew range offers powder and cream hair colour variants. The Renew powder hair colour is available in four colours attractively priced at Rs 20 per sachet in a pack of three sachets. The Renew cream hair colour is offered in six colours and is available in packs of 20ml and 50ml. Colour Soft offers a complete hair colouring kit and is available in five colours.

### **Toiletries**

GCPL offers shaving cream, talcum powder and deodorant spray under this category. The shaving cream comes under the brand of Godrej and the talcum powder and deodorant sprays come under the Cinthol brand. The talcum powder is available as Cinthol Deo Talc in five variants and the Cinthol deo spray is available in four variants.

### **Detergents & Household Care**

Godrej Ezee is used for special clothes and delicate garments like woolens, silks, baby clothes, wool blends, premium cottons etc. to protect the colours of clothes. It is available in three sizes of 18gm sachet, 200gm pack and 500gm pack. According to the management, the company is a market leader and enjoys a market share of 82.0% in this category. GCPL recently forayed into the hand hygiene category with the launch of Godrej Protekt which offers an entire range of hand sanitizers, hand wash and wipes and is available in three variants. It also offers utensil cleaner like Godrej Dish Wash under the household care category.

In December 2008, GCPL acquired the 50.0% stake of its JV partner SCA Hygiene Products in Godrej SCA Hygiene Limited. Post the transaction, the JV which owns the Snuggy brand of baby diapers, became a 100% subsidiary of GCPL.

### **International Operations**

GCPL has expanded its presence not only within India, but also across Europe, Australia, Canada, Africa and the Middle East region. The company owns international brands and trademarks in these regions through a number of subsidiaries. GCPL exports to 33 countries and in FY2009, the company recorded an export turnover of Rs 19.4cr.

#### **Exhibit 3: GCPL Subsidiaries**

<b>Subsidiary</b>	<b>Country</b>	<b>Revenues (Rs cr)</b>	<b>PAT (Rs cr)</b>
Keyline Brands Limited	U.K.	182.4	14.5
Rapidol (Pty.) Ltd.	South Africa	49.0	6.5
Kinky Group	South Africa	51.3	5.7
Godrej Global Mideast FZE	UAE	13.4	0.4

*Source: Company data, Parsoli Research*



***Rapidol and Kinky are GCPL's South African subsidiaries engaged in the hair care business***

***Godrej Global Mideast FZE distributes GCPL's products across GCC countries***

***The company's 49:51 JV with U.S. based Sara Lee operates across home care, personal care and air care segments***

**Keyline Brands Ltd.**

The company was acquired by GCPL in 2005 and operates in the toiletries and personal care segment. Its portfolio includes a number of brands including Cuticura, Adorn, Erasmic, Nulon, Aapri and Inecto.

**Rapidol (Pty.) Ltd.**

Rapidol, acquired in 2006, is one of the South African subsidiaries of GCPL and has strong presence across many countries in Africa, especially Southern Africa. Over the years, the company has developed a range of premier hair colourants and hair care products designed to colour and care for colour treated hair in the harsh climatic conditions of Africa. Rapidol owns, manufactures and distributes the ethnic hair colour brand, Inecto and hair care brand Soflene in the African continent.

**Kinky Group**

Kinky was acquired in April 2008 and offers a variety of products including hair, hair braids, hair pieces, wigs and wefted pieces in South Africa. It also offers hair accessories like styling gels, hair sprays and oil free shampoo. The company operates through 24 retail stores which include own stores as well as cash & carry outlets.

**Godrej Global Mideast FZE**

GCPL acquired Godrej Global Mideast FZE in 2007 which is a UAE based business. It distributes GCPL's products like soaps, hair colors and toiletries in UAE and other GCC (Gulf Co-operation Council) countries.

**Joint Ventures**

**Godrej Sara Lee Limited**

GSLL is a JV with U.S. based Sara Lee Corp having its operations in India. In 2009, GCPL acquired 49.0% stake from Godrej Consumer Biz and Godrej Hygiene Care, the two subsidiaries of Godrej & Boyce, which had a stake in the JV company. GCPL is now looking to acquire the remaining 51.0% stake of Sara Lee in the JV company as Sara Lee is exiting its non-core businesses worldwide.

GSLL operates across three categories, namely, home care, personal care and air care. Under the home care segment, the company offers household insecticide brands GoodKnight, HIT and Jet. Under the personal care segment, the company has Brylcreem, a men hair grooming product and in the air care portfolio, GSLL has Ambipur which offers an entire range of air fresheners. GSLL also manufactures, markets and distributes Kiwi, the shoe care brand of Sara Lee, in India. While GoodKnight, HIT and Jet are GSLL-owned brands, Brylcreem, Ambipur and Kiwi are licensed brands which belong to Sara Lee's international portfolio.

## Industry Overview

Fast Moving Consumer Goods (FMCG) are high consumption, low price products which find usage in the everyday needs of consumers. These include food products like dairy products, packaged foods, biscuits, snacks; beverages like tea, coffee, juices, carbonated drinks; personal care products like soap, shampoo, hair colour, deodorants, cosmetics and a variety of household and sanitation items. Despite slowdown, the sector continues to be one of the major drivers of the Indian growth story. The sector not only showed resilience during the slowdown that grappled the world markets, but also managed to grow during the period. The sector's basic nature of offering low ticket size products targeting the most basic needs of consumers makes it less prone to economic swings.

## FMCG Sector - Market Size

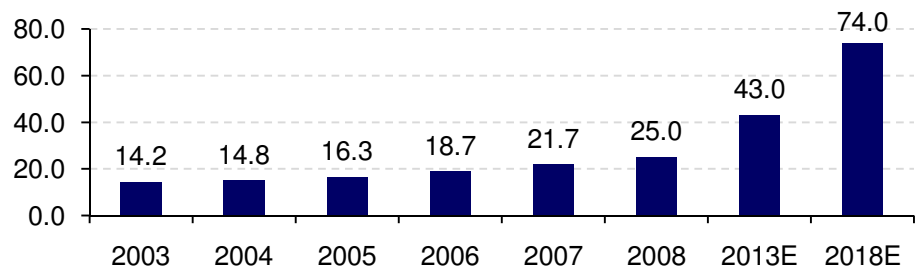
The Indian FMCG sector is the fourth largest sector in the economy and during the last couple of years; the sector has shown promising growth. The consumer base across products like soaps, detergents, personal care products, etc., has expanded cushioning the sector's demand during slowdown. According to the Federation of Indian Chambers of Commerce and Industry (FICCI)-Technopak sector report, the sector grew at a CAGR of 12.0% during 2003-08, reaching a market size of US\$ 25bn in 2008. Going forward, it is expected to touch a market size of US\$ 43bn in 2013 and US\$ 74bn in 2018, at a CAGR of 11.5% during 2008-2018. However, in case the Goods & Service Tax (GST) gets implemented, the sector is expected to grow at a more optimistic pace reaching a market size of US\$ 50bn by 2013 and US\$ 100bn by 2018, showing a CAGR growth of 14.9% during 2008-2018.

**The FMCG sector is expected to touch a market size of US\$ 74bn by 2018, growing at a CAGR of 11.5% during FY2008-18.**

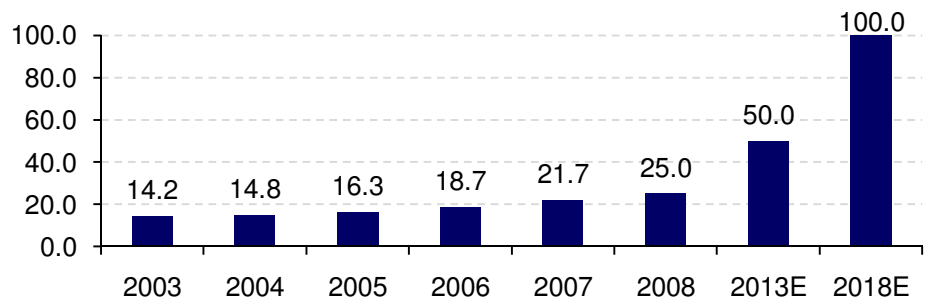
**The implementation of GST is expected to give further push to the market growth**

**Exhibit 4: FMCG Sector, Market Size** US\$ bn

Expected growth with no change in Industry status



Expected growth with GST implementation and FDI being opened in Multi-brand retail



Source: FICCI-Technopak report, Parsoli Research  
 \*Conversion rate, US\$ 1.0 = Rs 48.0

***GST reform, post-implementation, is expected to offer cost savings of around 10-12%***

The proposed GST is a tax reform aimed at making the tax system more efficient and uniform across all sectors and industries. It is expected to remove the indirect taxation regime wherein multiple taxes get levied at the central and state level. The current taxation (including the indirect taxes) comes to around 30.0% and GST proposes to reduce this tax rate to around 16.0% leading to cost savings of approximately 10-12%. The tax, proposed to come into force from April 1<sup>st</sup>, 2011, will allow single point taxation and would enable the prices of all FMCG products to fall allowing consumers to buy more and making the products more cost competitive.

***The toilet soap category is highly saturated with an all India penetration of 91.5%***

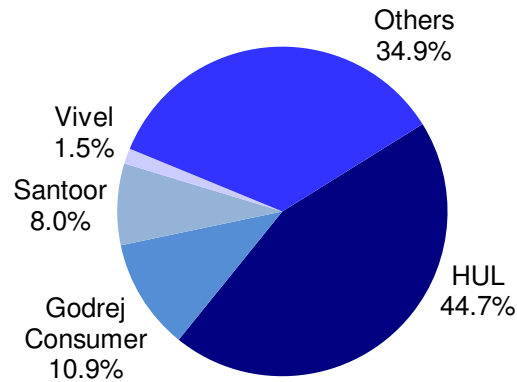
**Product Categories**

**Toilet Soaps**

The toilet soap category in India is an intensely competitive one with major players like HUL (Lifebuoy, Liril, Hamam, Rexona, Breeze, Lux, etc.), GCPL (Cinthol, Godrej No.1), Wipro Consumer (Santoor), ITC (Vivel) and Reckitt Benckiser (Dettol). According to FICCI-Technopak sector report, the overall market penetration in this category stands at 91.5% with the urban market penetration at 97.4% and that of rural market at 88.9%. The high level of penetration across this category makes it one of the most difficult categories to enter into, establish and then maintain market leadership. According to the October 2009 data from AC Nielsen, a marketing research firm, HUL continues to dominate the soap market with a 44.7% market share, though it has seen a decline in its market share which stood at 49.6% in December 2008. The company has lost its share in the soaps category to products like Godrej No.1 and Santoor as HUL mainly offers high-value products and due to the slowdown, consumers have started shifting to cheaper brands. GCPL with its Godrej No.1 soap stands second with a market share of 10.9%. Santoor (8.0%) is the top soap brand in South India and third largest in the overall rankings.

***GCPL has the second largest market share of 10.9% in the toilet soap category***

**Exhibit 5: Toilet Soap Category - Market Share**



*Source: AC Nielsen, Parsoli Research*

**Hair Care**

The hair care market includes products like shampoos, hair oils, conditioners, hair dyes, etc. According to The Associated Chambers of Commerce and Industry (ASSOCHAM), this market stands at around Rs 8,000cr having grown by 14.7% during Q1FY2010.



**The market for hair colours is largely dominated by liquids and powder hair dyes/colours that make up for 40-45% of the market**

The hair colour market is broadly divided at three levels with the top end comprising of creams which constitute 20-25% of the market; the base of the market is henna (mehndi) at 15% and the bulk comes from liquids and powders which make up for around 40-45%. In the hair colour market, GCPL competes with brands L'Oreal (Garnier) and Revlon in the top end segment. GCPL is the market leader with 33.1% market share in the segment.

### Liquid Detergents

This is a small category in the overall FMCG market. GCPL dominates the delicate fabric-wash category with a market share of 82.0%. In this category, GCPL competes with Wipro Consumer Care's newly launched Wipro Safewash.

### Growth Drivers

#### Growth across soaps and hair colour categories

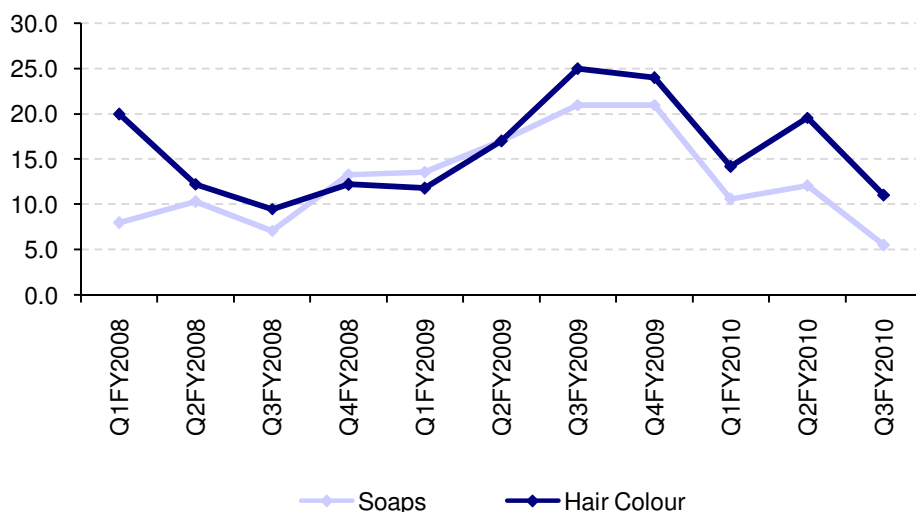
**The toilet soap category, despite high penetration, continues to grow on account of increasing per capita consumption**

The market for toilet soaps and hair colours is growing as the per capita consumption on these categories is going up, especially in rural India. According to a Federation of Indian Chambers of Commerce and Industry (FICCI)-Technopak report, the market penetration for toilet soap category stands at 91.5% (all India), with urban penetration at 97.4% and rural penetration at 88.9%. Though the market stands high on penetration, a greater amount of disposable income in the hands of consumers in rural areas is pushing the demand under this category.

In the hair colour category, the urban market is growing as consumers are increasingly switching from liquid dyes and powders to hair colorants. As the urban consumers are increasingly experimenting with new hair colours, the demand in this category has seen a paradigm shift from the powder dyes to the premium hair colours. So, it is the premium segment which is seeing higher growth in urban areas. The market in semi-urban and rural areas is still under-penetrated. However, as the aspiration value for such products has increased in tier I, II and III cities, the demand for hair colours has also gone up. The rural consumers prefer powder dyes (available in SKUs of Rs 5 and Rs 10) as they are cheaper compared to other high end products.

**The hair colour category is seeing high growth in, both, the urban as well as the rural market**

**Exhibit 6: Industry Growth** %



Source: Company data, Parsoli Research



*The rural demand is getting a push from the government's increasing expenditure under NREGS and Bharat Nirman Programme*

*A rise in the prices of palm oil may hurt the margins as it makes up for a major part of the raw material costs*

*In the premium segment of the hair colour category, GCPL is facing intense competition from Garnier, Revlon and Schwarzkopf*

Despite its high penetration, the soap category continues to grow every quarter at a minimum rate of around 6-10%. The growth in the hair colour category, on the other hand, is higher as the market size and the penetration remains low.

#### **Buoyant rural demand**

The demand for FMCG products has remained largely unaffected by the economic slowdown. The market, however, did see a shift in demand in the form of consumer downtrading. During the period of sluggish economic activity when the urban consumers were more cautious over household expenditures, the rural demand continued to thrive. On the back of this demand, the FMCG sector has performed well and it continues to see demand growth. The rural consumption has got a further push in the Union Budget 2010-11 with the hike in government allocation for the National Rural Employment Guarantee Scheme (NREGS) to Rs 40,100cr. Another effort in favor of the rural demand has been the increased outlay of Rs 48,000cr for the Bharat Nirman Programme for improving the rural infrastructure. These government expenditures have insulated the rural markets which have not seen a decline in demand as a result of slowdown. In fact, according to AC Nielsen, the demand for personal care products in rural areas outperformed the urban areas during April-September 2009.

#### **Key Concerns**

##### **Rise in palm oil prices**

Oils & fats make up for around 50.0% of GCPL's costs as a key raw material in the company's soap segment are palm oil derivatives. This makes the company's profitability highly sensitive to change in palm oil prices. The company saw erosion in its operating margins during FY2009 due to a steep rise in palm oil prices. This also led to a decline of around 100bps in GCPL's market share in the soap segment as GCPL had to raise its prices in order to combat the rise in raw material prices. Though the commodity prices have come down from 2008 highs and the company has regained its market share this year, another surge in the palm oil prices could again have an adverse impact on the company's profitability.

##### **Intense competition in the premium hair colour category**

GCPL is present across all the levels in the hair colour category, from the base level with Nupur (mehndi) to Renew hair colour targeted towards the top end of the market. However, the company faces stiff competition from international brands like Garnier, Revlon and Schwarzkopf in the cream hair colour category. Since GCPL plans to focus mainly on the value-based brands in the hair colour category, the competition for the company is expected to intensify with new launches coming from international brands which may lead to a loss of market share for GCPL.

**HUL is the market leader in the FMCG space with the highest revenues**

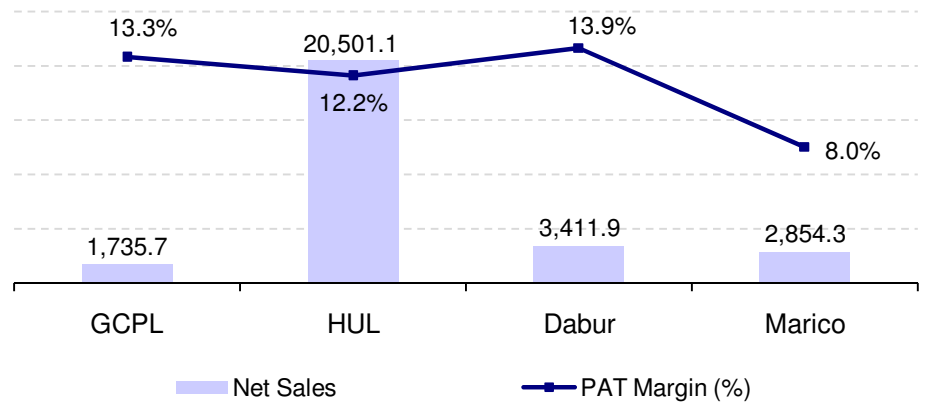
**GCPL, Dabur and Marico have improved their PAT margin for the 9 months ended December 2009 on account of higher sales, lower commodity prices and deeper rural penetration**

**GCPL grew its revenues at a CAGR of 23.3% during FY2004-09**

## Peer Comparison

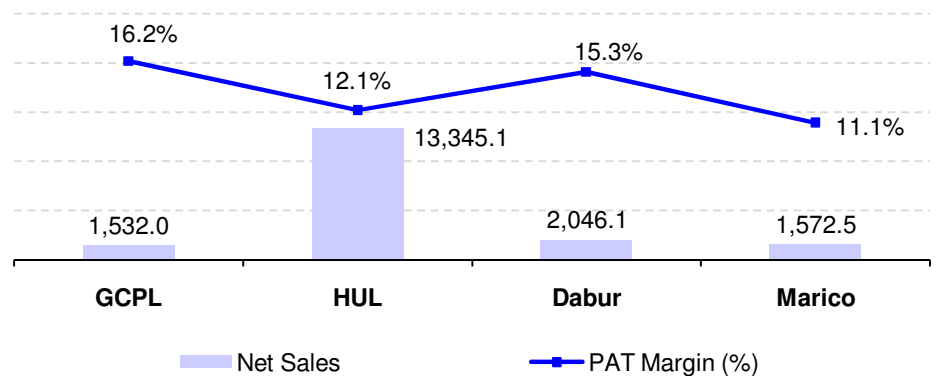
The FMCG sector in India is highly competitive across all its major categories, namely, food processing, personal care, home care, etc. GCPL is among the leading players in the personal care category where it competes with HUL, ITC, Wipro Consumer, etc.

**Exhibit 7: Net Sales (15 months ended March 2009) Rs cr**



Source: Company data, Parsoli Research  
\*Consolidated Results

**Exhibit 8: Net Sales (9 months ended December 2009) Rs cr**



Source: Company data, Parsoli Research  
\*Standalone Results

GCPL is a growing player in the FMCG space and its revenues have grown at a CAGR of 23.3% during FY2004-2009 as compared to Dabur's growth of 16.1% and Marico's 21.9%. HUL is still the market leader contributing the highest revenues to the sector. In terms of margin, GCPL's PAT margin (for 15 months ended March 2009) stood at 13.3% as compared to Dabur's highest margin of 13.9%. GCPL's margins declined during FY2009 due to a steep rise in palm oil derivative prices (which make up for around 50.0% of the company's raw material cost). This led to a steep erosion in the company's profit margins. However, during FY2010, with the oil prices coming down from their highs, the company has again expanded its margins to 16.2% (for 9 months ended December 2009).



*The operational expenditure of GCPL stands at 78.1% of sales on account of low employee costs and A&P expenses*

*GCPL's return ratios were majorly impacted during FY2009 due to a steep rise in palm oil prices, a key raw material for the soap segment*

GCPL has already contracted its palm oil derivative requirements till April-May 2010 and continues to proactively forward cover, as and when the opportunity arises. Also, the company's costs are expected to remain under control as the palm oil refiners in India are now allowed to import the palm oil duty free as a result of which the derivatives are available at considerably lower prices.

<b>Exhibit 9: Cost Analysis</b>					<b>% of sales</b>
	<b>GCPL</b>	<b>HUL</b>	<b>Dabur</b>	<b>Marico</b>	
Raw Material Cost	44.8	33.6	31.1	46.5	
Employee Cost	6.4	5.8	8.4	7.0	
Advertising Cost	6.5	10.5	12.2	11.2	
Operating Expenditure	78.1	81.0	74.9	80.7	

*Source: Company data, Parsoli Research  
\*Data for 15 months ended March 2009*

Among the key industry players, HUL has the highest operational expenditure at 81.0% of sales due to high manufacturing and other expenses. Though GCPL has the highest Cost of Goods Sold (COGS) among peers at 54.4% of sales, the company has low manufacturing and other expenses on account of lower advertisement and publicity (A&P) expense. GCPL primarily focuses on advertising for Godrej No. 1, a value-based brand with turnover exceeding Rs 500cr, through Doordarshan in order to have a larger reach in the rural market. This low-cost focused A&P approach has kept a cap on company's operational costs.

<b>Exhibit 10: Ratio Comparison, FY2009</b>				
	<b>GCPL</b>	<b>HUL*</b>	<b>Dabur</b>	<b>Marico</b>
ROCE (%)	26.9	118.7	43.6	33.8
ROE (%)	30.5	117.4	47.7	41.6
Fixed Assets Turnover	6.1	12.4	5.0	9.4
Working Capital Turnover	3.5	(211.0)	19.6	6.7
<b>Days</b>				
Inventory Turnover	79	86	100	94
Debtors Turnover	16	10	23	17
Creditors Turnover	30	60	56	38

*Source: Company data, Parsoli Research  
\*For 15 months ended March 2009*

HUL has the highest ROCE and ROE at 118.7% and 117.4%, respectively, among the industry peers. During FY2009, the ROCE and ROE for GCPL declined to 26.9% and 30.5%, respectively, as the steep rise in palm oil prices (a key raw material in the soap category) impacted the profits.



*The company is aggressively targeting the rural market and looking to acquire new businesses in order to increase revenues*

*We expect the company's revenues to grow at a CAGR of 29.4% during FY2009-12E and the EBIDTA margin to expand by around 500bps to 19.7% by FY2012*

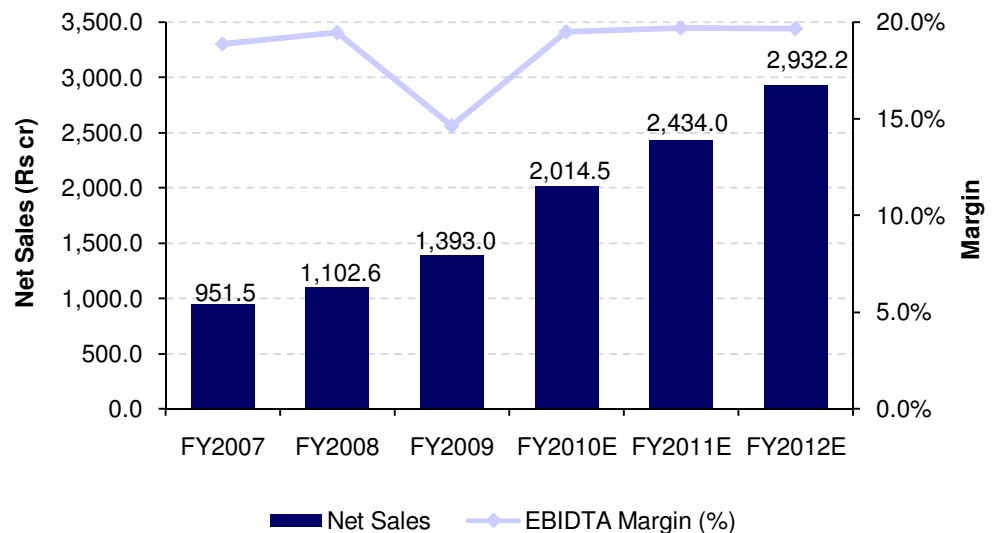
*We expect the net profit to grow at a CAGR of 38.4% during FY2009-12E to Rs 457.8cr in FY2012*

## Financial Performance

### High growth in revenues with profit margin expansion

GCPL is following a three-pronged strategy of expanding distribution reach with focus on rural areas, product presence at multiple price points and growth via acquisitions; in order to accelerate its growth. We believe that by following this strategy, the company will be able to expand its revenues at a CAGR of 28.2% during FY2009-12E to Rs 2,932.2cr by FY2012. In addition, in terms of margin, the company has been able to improve its operating margin during 9mFY2010 owing to a decline in palm oil prices. The company has already contracted its palm oil derivative requirements till April-May 2010 and continues to proactively forward cover, as and when the opportunity arises. Also, the COGS for the company are expected to remain under control as the palm oil refiners in India are now allowed to import the palm oil duty free as a result of which the derivatives are available at considerably lower prices. Going forward, we expect the EBIDTA margin to increase by around 500bps from 14.6% in FY2009 to 19.7% in FY2012E.

**Exhibit 11: Net Sales and Margin Expectations, FY2007-2012E**



Source: Company data, Parsoli Research

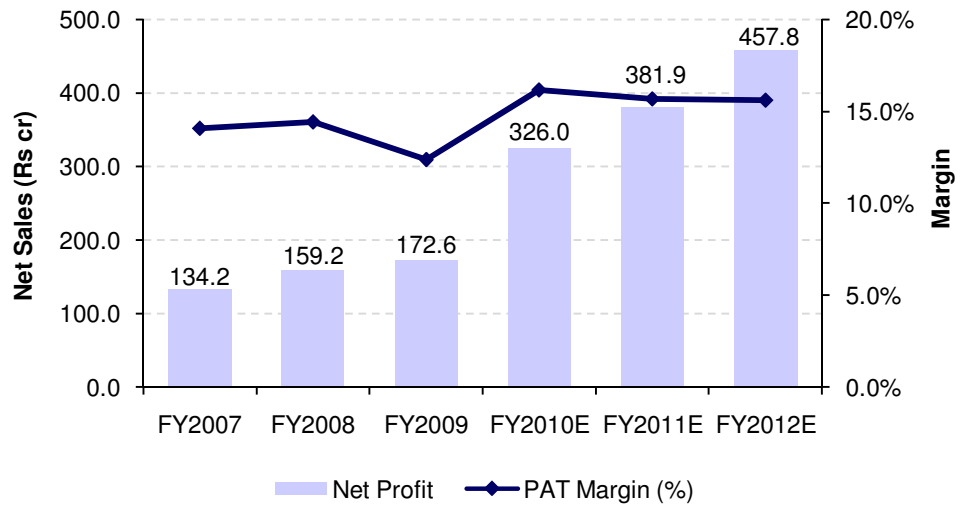
### Net profit to increase to Rs 456.1cr

We expect the company's net profit to grow at a healthy CAGR of 38.4% (FY2009-12E) to reach Rs 457.8cr by FY2012. Alongside, supported by the strong growth in EBIDTA margin and low debt on the company's books, the PAT margin is expected to expand by 322bps to touch 15.6% by FY2012 as compared to 12.4% in FY2009. However, with the increase in MAT (Minimum Alternate Tax) from 10.0% to 15.0% during FY2010, the company's overall tax rate has also increased.



*The PAT margin is expected to increase to 15.6% by FY2012*

**Exhibit 12: Net Profit and PAT Margin, FY2007-2012E**



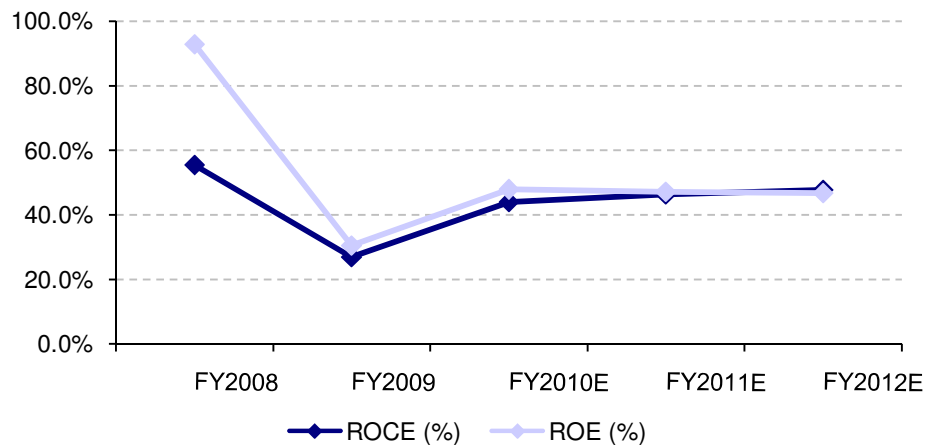
Source: Company data, Parsoli Research

**Growth in ROCE and ROE**

*With the decline in palm oil prices, the ROCE and ROE are expected to expand*

We expect GCPL's ROCE to improve from 26.9% in FY2009 to 47.7% in FY2012 on account of a 503bps improvement in EBIDTA margin during the period. Consequently, the PAT margin is also expected to improve by 322bps during FY2009-12 which would result in ROE expansion from 30.5% in FY2009 to 46.7% in FY2012.

**Exhibit 13: Return Ratios, FY2008-2012E**



Source: Company data, Parsoli Research

*GCPL is looking to acquire 51.0% stake in GSLL for an approximate value of Rs 800cr*

Going forward, the company is aggressively targeting to acquire domestic and/or international businesses in the personal care, hair care and household insecticide category. For this purpose, the company's board has approved raising of funds upto Rs 3,000cr. The company's top priority would be an acquisition within India. Also, GCPL plans to acquire the remaining 51.0% stake in GSLL which is expected to be for an approximate value of Rs 800cr. Even after acquiring the 100.0% stake in GSLL, the company will have enough funds to acquire businesses in the personal care and hair care categories.



*During Q3FY2010, the topline showed a robust growth of 53.1% to touch Rs 517.6cr turnover*

*During the quarter, the growth in the soap and hair colour categories was largely volume driven with both the categories outperforming the industry growth*

*For 9mFY2010, the company's revenues have gone up by 46.0% yoy with the EBIDTA margin at 19.6%*

**Recent Quarter Update**

<b>Exhibit 14: Quarterly Analysis</b>						<b>Rs cr</b>
<b>Particulars</b>	<b>Q3FY2010</b>	<b>Q3FY2009</b>	<b>YoY (%)</b>	<b>Q2FY2010</b>	<b>QoQ (%)</b>	
Revenue	517.6	338.1	53.1	575.6	(10.1)	
Other Income	11.1	15.9	(30.2)	13.9	(20.2)	
Total Income	528.6	353.9	49.4	589.5	(10.3)	
Total Expenditure	416.2	293.8	41.6	463.7	(10.2)	
<b>EBIDTA</b>	<b>101.4</b>	<b>44.2</b>	<b>129.4</b>	<b>111.9</b>	<b>(9.4)</b>	
<i>EBIDTA Margin (%)</i>	<i>19.6</i>	<i>13.1</i>	<i>-</i>	<i>19.4</i>	<i>-</i>	
Depreciation	5.6	5.1	10.5	6.8	(17.3)	
<b>EBIT</b>	<b>106.9</b>	<b>55.0</b>	<b>94.3</b>	<b>119.1</b>	<b>(10.2)</b>	
Interest	2.0	6.1	(67.0)	2.6	(22.6)	
Profit before Tax	104.9	48.9	114.5	116.4	(9.9)	
Tax	19.8	8.8	123.8	23.4	(15.7)	
<b>Net Profit</b>	<b>85.1</b>	<b>40.1</b>	<b>112.5</b>	<b>93.0</b>	<b>(8.5)</b>	
<i>PAT Margin (%)</i>	<i>16.4</i>	<i>11.9</i>	<i>-</i>	<i>16.2</i>	<i>-</i>	
EPS	2.8	1.6	77.8	3.0	(8.5)	

*Source: Company data, Parsoli Research  
\*Consolidated results*

**Robust growth in topline with PAT growth of 112.5%**

During Q3FY2010, GCPL's revenues grew by 53.1% yoy to Rs 517.6cr being largely driven by volume growth in the soap and hair colour categories. The soaps category saw a value growth of 13.0% against an industry growth of 5.5%. Of the total growth in this category, 10.0% growth was volume driven. In the hair colour category also, the company outperformed the market by showing a value growth of 17.0% against the industry growth of 11.0%. The entire growth in this category was volume driven. The volume growth was supported by enhanced rural distribution resulting in increased penetration of the company's products.

The EBIDTA for the quarter stood at Rs 101.4cr, showing a healthy growth of 129.4% yoy. The EBIDTA margin grew strongly by 652bps yoy to 19.6% in Q3FY2010 as compared to 13.1% in Q3FY2009. The growth was primarily on account of low prices of palm oil derivatives which led to an 1,160bps yoy decline in COGS to 47.5% of sales in Q3FY2010. The decline, however, was partially offset by a 625bps yoy increase in employee expenses to 11.6% of sales on account of higher incentives to employees and a 68.5% yoy jump in A&P expenses. Even with an increase in the tax rate due to higher MAT which was raised from 10.0% to 15.0% during FY2010, the company's net profit grew by 112.5% yoy to Rs 85.1cr. The PAT margin also expanded by 460bps yoy.

For 9mFY2010, the total revenues have grown by 46.0% yoy to Rs 1,532cr. Overall, the total expenditure has come down by 657bps yoy to 80.4% of sales on account of steep decline in COGS (due to softening of palm oil prices) by 977bps yoy. The employee expenses have, however, increased by 408bps yoy 10.1% of sales. For 9mFY2010, the EBIDTA has more than doubled to Rs 299.8cr (against Rs 136.4cr for 9mFY2009), with the EBIDTA margin going up to 19.6%. The PAT for 9mFY2010 was up by 117.6% yoy to Rs 247.8cr with the PAT margin having improved by 532bps yoy to 16.2%.



*The company's market share in the toilet soap category declined by 40bps during the quarter*

*During Q3FY2010, GCPL launched new variants of existing products, introduced smaller SKUs and forayed into the hand hygiene category*

*The South African subsidiaries have performed well on the back of extended market reach*

**Decline in toilet soap category market share**

GCPL's market share in the toilet soap category declined by 40bps qoq during the quarter. The market share, however, was up by 100bps yoy from 9.5% in Q3FY2009 to 10.3% in Q3FY2010. The category growth was primarily volume driven as price hikes have been difficult with consumers (who are now more price sensitive) on account of rising food inflation taking up higher share of customer wallet. During the quarter, the company launched Godrej No.1 Moisturizing Soap with milk cream and almond. The product is available at multiple price points of Rs 30, Rs 40 and Rs 50. According to the management, GCPL's soap category market share has usually been lower in the winter months as the company did not have a glycerine soap (used in winters) in its portfolio. With the launch of Godrej No.1 Moisturizing Soap (for winters), the market share is expected to improve in Q4FY2010.

**New launches across categories and price points**

During the quarter, GCPL launched Godrej No.1 Moisturizing Soap for winters. The company also launched a 140gm SKU (stock keeping unit) of Godrej No.1 in Natural & Sandal variants in Northern markets. Under the Cinthol brand, the company launched Cinthol skin protection talc in South and extended the Cinthol Deodrant & Complexion soap at more accessible price points of Rs 6 and Rs15. The company, in the hair colour category, launched additional shades of Plum Crazy and Wine Red under the Renew Hair Colour range and changed the packaging configuration to smaller SKU for Godrej Expert PHD. During the quarter, the company forayed into the hand hygiene category with the launch of Godrej Protekt which offers a range of hand sanitizers, hand wash and wet wipes and is available in three variants.

**Growth in international business**

The company's international subsidiaries performed extremely well during the quarter, specially the South African businesses. Net sales from Kinky group and Rapidol were up by 39.4% yoy and 49.2%, respectively. The revenue from Kinky group stood at Rs 23.7cr for Q3FY2010 and the PAT was at Rs 3.1cr. The growth has come as GCPL increased the footprint for Kinky which earlier used to sell through 20-22 of its own stores has gone in to retail trade also. The revenue from Rapidol was Rs 21.3cr with the net profit at Rs 4.2cr. The overall growth in the South African businesses has come as GCPL, following its 'One Africa' strategy, has moved both the brands into more number of countries.



***On the basis of EV/EBIDTA methodology, we arrive at a fair price of Rs 321 per share***

***The P/E methodology gives us a fair price of Rs 310 per share***

***GCPL, when valued by taking the average from EV/EBITDA and P/E methodologies gives a target price of Rs 316 per share***

***We expect the company to reach a turnover of Rs 2,932.2cr by FY2012, growing at a CAGR of 28.2% during FY2009-12E***

## Valuation

For valuing the company, we have used Relative Valuation based on EV/EBIDTA and Price/Earnings (P/E) multiple methodologies considering FY2011 estimates. A comparative valuation using EV/EBIDTA methodology helps us in comparing the company's performance with its peers irrespective of their depreciation and finance expenditures. The P/E multiple methodology helps in comparing peer group performance with the company with respect to earnings potential. We have considered an investment horizon of 12 months.

## Comparative Valuation

GCPL currently trades at an EV/EBIDTA multiple of 20.7x FY2010E and 16.8x FY2011E. When considering the current EV/EBIDTA multiple, the stock trades above the industry average of 23.3. Going forward, the company is expected to improve its EBIDTA margin by 503bps yoy from 14.6% in FY2009 to 19.7% in FY2012. The growth will be supported by the expanding rural distribution network, new launches across categories and price points and value accretion on account of acquisitions in the domestic and/or international market. Therefore, we are assigning a multiple of 21.0 to value the stock. Using this target multiple on our FY2011 EBIDTA estimates of Rs 479.5cr, we arrive at a target price of Rs 321.3 per share.

When considering the P/E multiple, the stock trades at 24.2x FY10E earnings and 20.7x FY2011E earnings. The current industry average multiple for peer group stands at 26.9. With the high growth expectation in the FMCG industry on the back of buoyant rural demand and increasing per capita consumption, going forward, we expect the company's EPS to grow at a CAGR of 29.6% (FY2009-12E) to Rs 14.9 by FY2012. We are assigning a multiple of 25.0 to value the stock. Employing this target multiple on our FY2011 EPS estimates of Rs 12.4, we arrive at a target price of Rs 309.9.

By taking an average of the price estimated through EV/EBIDTA and P/E methodologies, which is Rs 321.3 and Rs 309.9, respectively, we arrive at a target price of Rs 316 representing an upside of 23.2%.

### Exhibit 15: Valuation

	Rs
CMP	256.2
Target price using EV/EBIDTA methodology	321.3
Target price using P/E methodology	309.9
Fair value	315.6
Upside from current levels (%)	23.2

*Source: Company data, Parsoli Research*

## Future Outlook and Conclusion

We believe that the company will be able to grow its revenues at a CAGR of 28.2% (FY2009-12E) to Rs 2,932.2cr. This growth is expected on the back of company's strategy of aggressively targeting rural market through expanded distribution network, smaller SKUs at Rs 5 and Rs 10 price points and new product launches. The company, in order to increase the rural reach of its products, targets to cover 50,000 villages and cover 8,000 small towns in three years. We expect the profit margins to expand during FY2010 with EBIDTA margin at 19.5% on account of lower commodity prices. The improvement in EBIDTA margin will support PAT margin which is expected to be around 16.2% for FY2010E.



***The stock is expected to perform well over 12 months horizon and we recommend a buy on the stock with a target price of Rs 316***

The FMCG sector, which grew at a CAGR of 12.0% during 2003-08 to a market size of US\$ 25bn in 2008, is expected to reach US\$ 43.0bn in 2013 and US\$ 74.0bn in 2018, showing a CAGR of 11.5% during 2008-2018. The sector, till now, has seen growth coming from volumes as well as price-hikes. However, with the rising food inflation taking up a major share of the household expenditure, future growth is likely to come primarily from volumes. We expect that the demand from rural India will continue to grow the revenues for FMCG companies. In addition, categories like toilet soaps are expected to grow with higher per capita consumption and that of hair colour would grow on account of shifting urban demand for hair colorants and the aspirational value attached with such products in the semi-urban and rural areas. We believe that the company's strategy to target the rural market would help GCPL in expanding its revenue share from the rural market. In addition, GCPL's intention to grow via acquisitions in the personal care, hair colour and household insecticide category is expected to be value accretive. We expect the stock to perform well for 12 months horizon. **We recommend a BUY on the stock with a Target Price of Rs 316.**



## Financial Statements

<b>Exhibit 16: Profit &amp; Loss Statement</b>					<b>Rs cr</b>
	<b>FY2008</b>	<b>FY2009</b>	<b>FY2010E</b>	<b>FY2011E</b>	<b>FY2012E</b>
<b>Net Sales</b>	1,102.6	1,393.0	2,014.5	2,434.0	2,932.2
<i>% chg</i>	15.9	26.3	44.6	20.8	20.5
Total Expenditure	888.1	1,189.3	1,621.6	1,954.5	2,356.0
<i>% chg</i>	15.1	33.9	36.4	20.5	20.5
<b>EBIDTA</b>	214.5	203.7	392.8	479.5	576.2
<i>Margin (%)</i>	19.5	14.6	19.5	19.7	19.7
Other Income	6.0	43.6	46.8	48.7	58.6
Depreciation & Amortisation	18.2	19.2	23.4	39.0	51.1
Interest	14.8	18.9	11.2	14.7	15.1
<b>PBT</b>	187.5	209.2	405.0	474.5	568.7
<i>Margin (%)</i>	17.0	15.0	20.1	19.5	19.4
Total Tax	28.3	36.6	79.0	92.5	110.9
<i>(% of PBT)</i>	15.1	17.5	19.5	19.5	19.5
<b>PAT</b>	159.2	172.6	326.0	381.9	457.8
<i>% chg</i>	18.7	8.4	88.9	17.1	19.9
<i>Margin (%)</i>	14.4	12.4	16.2	15.7	15.6

Source: Company data, Parsoli Research

<b>Exhibit 17: Balance Sheet</b>					<b>Rs cr</b>
	<b>FY2008</b>	<b>FY2009</b>	<b>FY2010E</b>	<b>FY2011E</b>	<b>FY2012E</b>
<b>SOURCES OF FUNDS</b>					
Equity Share Capital	22.6	25.7	30.8	30.8	30.8
Reserves & Surplus	149.0	541.2	650.9	780.4	949.8
Net Worth	171.6	566.8	681.7	811.2	980.6
Total Loans	187.1	277.6	260.0	240.0	240.0
Deferred Tax Liability	8.9	4.2	4.2	4.2	4.2
Capital Employed	367.6	848.6	945.9	1055.5	1224.8
<b>APPLICATION OF FUNDS</b>					
Gross Block	293.7	337.0	419.5	599.5	729.5
Less: Acc. Depreciation	125.3	109.8	133.1	172.1	223.2
<b>Net Block</b>	168.3	227.2	286.3	427.3	506.3
Capital Work-in-Progress	71.6	2.5	120.0	90.0	60.0
Goodwill	95.6	208.6	208.6	208.6	208.6
Investments	0.0	7.5	374.8	374.8	374.8
Current Assets	351.9	732.7	367.9	434.2	648.7
Current Liabilities	322.7	329.9	411.7	479.5	573.6
Net Current Assets	29.2	402.9	(43.8)	(45.3)	75.1
Miscellaneous Expenditure	2.9	0.0	0.0	0.0	0.0
Capital Deployed	367.6	848.6	945.9	1055.5	1224.8

Source: Company data, Parsoli Research

**Exhibit 18: Key Ratios**

Per Share Data (Rs)	FY2008	FY2009	FY2010E	FY2011E	FY2012E
EPS	7.1	6.8	10.6	12.4	14.9
DPS	4.0	4.0	6.0	7.0	8.0
Book Value	364.7	848.6	945.9	1,055.5	1,224.8
<b>Returns (%)</b>					
ROE	92.8	30.5	47.8	47.1	46.7
ROCE	55.5	26.9	44.0	46.4	47.7
Dividend Payout	56.7	58.6	56.7	56.5	53.9
<b>Valuation Ratios (x)</b>					
P/E	17.6	19.5	24.2	20.7	17.2
P/Cash EPS	15.8	17.6	22.6	18.8	15.5
P/BV	7.7	4.0	8.3	7.5	6.4
EV/EBIDTA (x)	13.7	14.2	17.2	16.8	13.7
EV/Sales (x)	2.7	2.1	3.3	3.3	2.7

Source: Company data, Parsoli Research

**Exhibit 19: Cash Flow Statement**

Particulars	FY2008	FY2009	FY2010E	FY2011E	FY2012E
PBT	187.5	209.2	405.0	474.5	568.7
Depreciation & Amortisation	18.2	19.2	23.4	39.0	51.1
Interest	14.8	18.9	11.2	14.7	15.1
Change in Working Capital	(18.3)	(37.9)	90.9	49.3	27.6
Change in Goodwill	(7.0)	(113.0)	0.0	0.0	0.0
Direct taxes paid	(27.3)	(41.3)	(79.0)	(92.5)	(110.9)
<b>Cash Flow from Operations</b>	167.8	55.1	451.5	484.9	551.5
(Inc.)/Dec. in Fixed Assets	(23.8)	(43.3)	(82.5)	(180.0)	(130.0)
(Inc.)/Dec. in Cap WIP	(31.8)	69.1	(117.5)	30.0	30.0
<b>Free Cash Flow</b>	112.3	80.9	251.5	334.9	451.5
Inc./(Dec.) in Investments	0.0	(7.5)	(367.3)	0.0	0.0
Inc./(Dec.) in Capital	0.0	360.1	5.1	0.0	0.0
Inc./(Dec.) in Loans	13.5	90.5	(17.6)	(20.0)	0.0
Dividend paid (incl. tax)	(108.5)	(120.5)	(216.3)	(252.4)	(288.4)
Interest paid (Net)	(14.8)	(18.9)	(11.2)	(14.7)	(15.1)
Miscellaneous	(7.4)	(49.0)	0.0	0.0	0.0
<b>Cash Flow from Financing</b>	(117.2)	254.8	(607.3)	(287.1)	(303.5)
Inc./(Dec.) in Cash	(4.9)	335.7	(355.8)	47.8	148.0
Opening Cash balances	47.5	42.6	378.3	22.5	70.3
Closing Cash balances	42.6	378.3	22.5	70.3	218.3

Source: Company data, Parsoli Research



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