GlaxoSmithKline Consumer Healthcare

Ready to gain demand recovery and benign inputs

Q3FY15 Result Update

February 03, 2015

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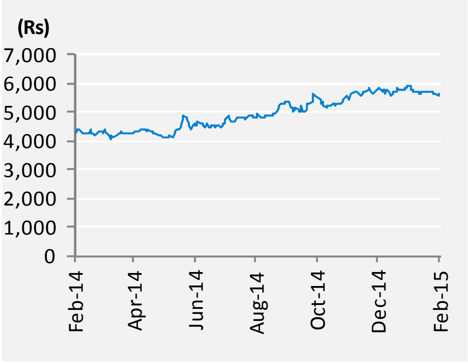
Rating	**Accumulate**
Price	Rs5,648
Target Price	Rs5,727
Implied Upside	1.4%
Sensex	29,000
Nifty	8,757

(Prices as on February 03, 2015)

Trading data			
Market Cap. (Rs bn)			237.5
Shares o/s (m)			42.1
3M Avg. Daily value (Rs m)			161.4
Major shareholders			
Promoters			72.46%
Foreign			11.45%
Domestic Inst.			1.59%
Public & Other			14.50%
Stock Performance			
(%)	**1M**	**6M**	**12M**
Absolute	(4.3)	16.3	32.8
Relative	(8.3)	2.5	(10.7)
How we differ from Consensus			
EPS (Rs)	**PL**	**Cons.**	***% Diff.***
2016	168.1	166.1	*1.2*
2017	202.1	198.2	*2.0*

Price Performance (RIC: GLSM.BO, BB: SKB IN)



Source: Bloomberg

GSK has posted impressive performance in 3Q with initial signs of volume recovery and 19.8% EBIDTA growth despite 32% higher adspend on relaunch of BSLX (base Horlicks) and WHLX (Women Horlicks). Input costs scenario looks favourable with a further decline of 25% in SMP prices in the past 4 months despite firm barley prices. We believe GSK is one of the best plays on recovery in discretionary spend by the consumers. We expect 260bps margin expansion over FY15-17 led by higher gross margins and lower ad-spends. We estimate 19.6% PAT CAGR over FY15-17 with 22% CAGR in the past five years. We upgrade the stock to Accumulate.

- **Volumes up 5%, market share gains in Horlicks;** Volumes increased 5% (2% in 2Q) led by strong growth across segments. MFD market share increased by 120bps as base Horlicks (BSLX) share increased 50bps and women Horlicks (WHLX) share increased 0.3%. Strong market activation and re-launch of base and junior Horlicks enabled volume recovery. Oats sales grew by 25%, YoY market share is up 6.1% with HLX emerging as No2 player. OTC marketing income increased by 25% led by reintroduction of Crocin advanced.

- **Revenues up 16.5%, Gross margins up 180bps: R**evenues increased 16.5%, gross margins increased 180bps to 66.5% due to benign SMP prices and benefits of 17% hike in Rs5 pack of Horlicks and 1.5% in large packs. 260bps higher adspend curtailed gains from 110bps lower staff costs and 180bps lower input costs. EBIDTA increased 20%. 23% higher financial income enabled 21% PAT growth. Higher other income accounted for 67.8% of incremental PBT.

- **Expect volume recovery and margin expansion:** We believe re-launch of BSLX and WHLX is well timed as pick- up in economic recovery is expected to boost demand. We estimate 160bps margin expansion in FY16 as benefits of lower SMP (23% of RM, 25% decline since 2Q), higher volumes and 18% price increase in small unit packs are realised.

Key financials (Y/e March)	**2014***	**2015E**	**2016E**	**2017E**
Revenues (Rs m)	49,018	44,206	51,464	59,877
Growth (%)	*53.1*	*(9.8)*	*16.4*	*16.3*
EBITDA (Rs m)	9,060	7,587	9,681	11,850
PAT (Rs m)	6,747	5,944	7,069	8,501
EPS (Rs)	160.4	141.3	168.1	202.1
Growth (%)	*54.5*	*(11.9)*	*18.9*	*20.3*
Net DPS (Rs)	69.8	60.8	74.0	88.9

Profitability & Valuation	**2014***	**2015E**	**2016E**	**2017E**
EBITDA margin (%)	*18.5*	*17.2*	*18.8*	*19.8*
RoE (%)	*42.5*	*30.4*	*31.2*	*32.3*
RoCE (%)	*42.3*	*30.3*	*31.1*	*32.2*
EV / sales (x)	4.8	5.4	4.6	4.0
EV / EBITDA (x)	26.2	31.2	24.5	20.0
PE (x)	35.2	40.0	33.6	27.9
P / BV (x)	13.1	11.3	9.8	8.4
Net dividend yield (%)	*1.2*	*1.1*	*1.3*	*1.6*

Source: Company Data; PL Research **FY14 =15 Months*

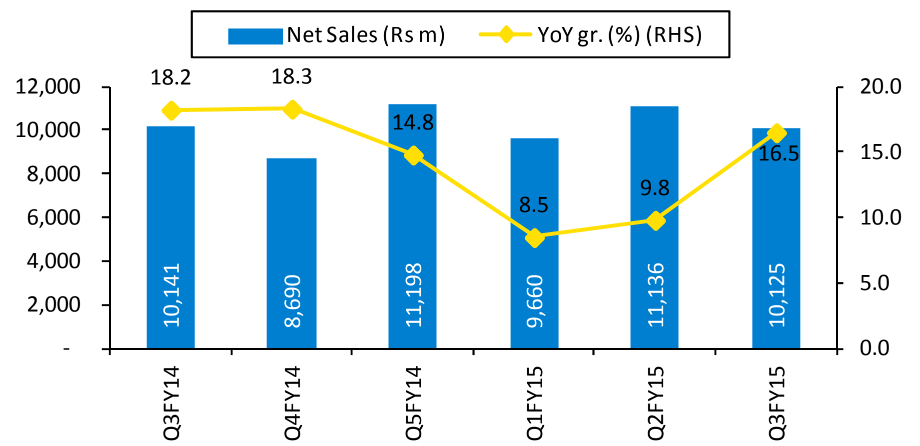
Exhibit 1: 20.9% PAT growth: Sales growth up 16.5% on Higher realisations and 5% volume growth

	Q3FY15	Q3FY14	*YoY gr. (%)*	Q2FY15	9MFY15	9MFY14	*YoY gr. (%)*
Net Revenue	**10,125**	**8,690**	***16.5***	**11,136**	**30,921**	**27,734**	***11.5***
Gross Profit	6,730	5,623	*19.7*	7,005	19,875	18,075	*10.0*
% of NS	*66.5*	*64.7*	*1.8*	*62.9*	*64.3*	*65.2*	
Advertising & Promotion	2180	1648	*32.3*	1753	5347	4656	*14.8*
% of NS	*21.5*	*19.0*		*15.7*	*17.3*	*16.8*	
Total Expenses	9,066	7,806	*16.1*	9,179	26,258	23,369	*12.4*
% of NS	*89.5*	*89.8*		*82.4*	*84.9*	*84.3*	
EBITDA	**1,059**	**884**	***19.8***	**1,957**	**4,663**	**4,365**	***6.8***
Margins %	*10.5*	*10.2*	*0.3*	*17.6*	*15.1*	*15.7*	
Depreciation	131	112	*17.2*	121	372	350	*6.3*
Interest	2	4	*(56.8)*	2	6	7	*(23.0)*
Financial other Income	548	446	*23.0*	619	1,624	1,265	*28.4*
PBT	**1,474**	**1,213**	***21.5***	**2,453**	**5,909**	**5,272**	***12.1***
Tax	510	416	*22.6*	850	2,041	1,806	*13.0*
Adjusted PAT	**964**	**797**	***20.9***	**1,603**	**3,868**	**3,466**	***11.6***

Source: Company Data, PL Research

Q3FY14 sales grew 16.5%, HFD gained 1.2% market share

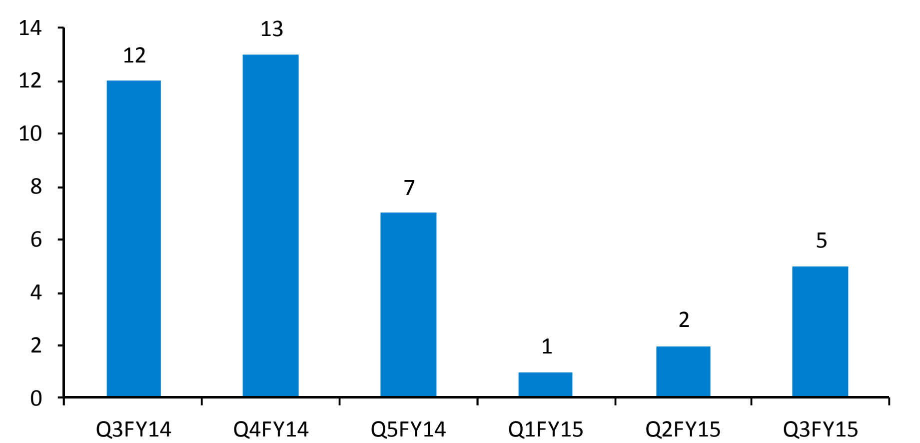
Exhibit 2: Growth across regions and strong activation programme boost sales growth



Source: Company Data, PL Research

Q3FY15 Domestic MFD volumes grew ~5 in a challenging environment

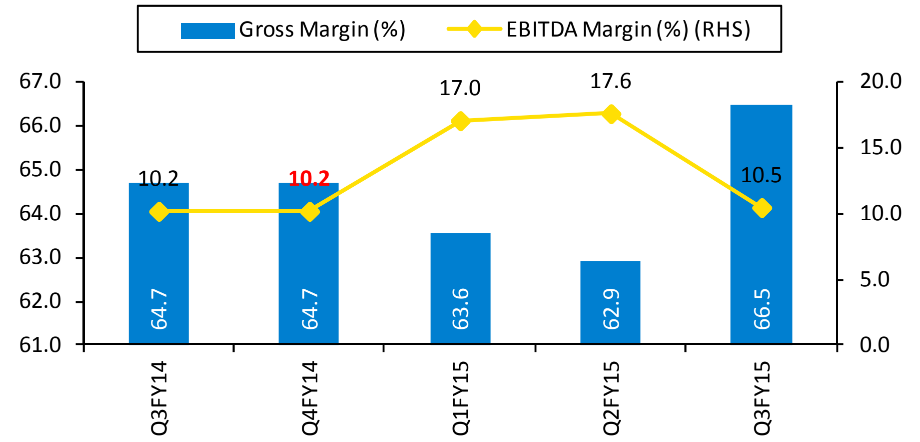
Exhibit 3: Volumes up 5% on market share gains in Horlicks



Source: Company Data, PL Research

Benign SMP and Milk prices help to boost gross margins

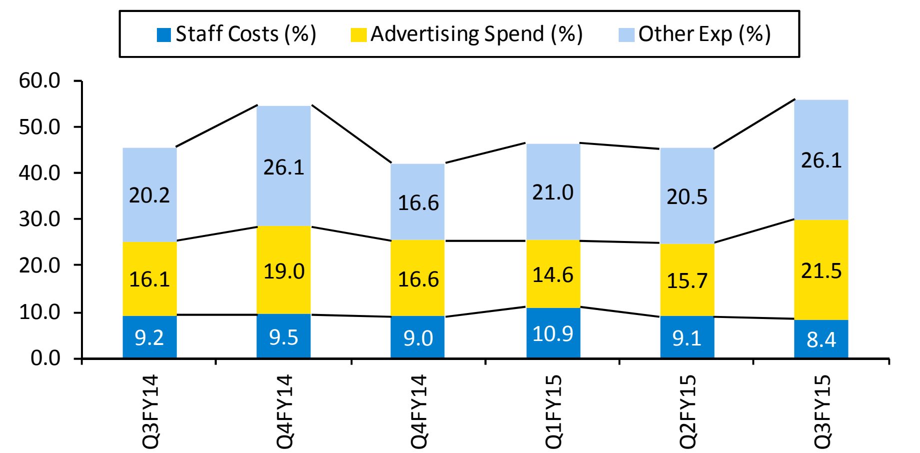
Exhibit 4: Gross margins up 180bps due to benign input cost and higher realisations



Source: Company Data, PL Research

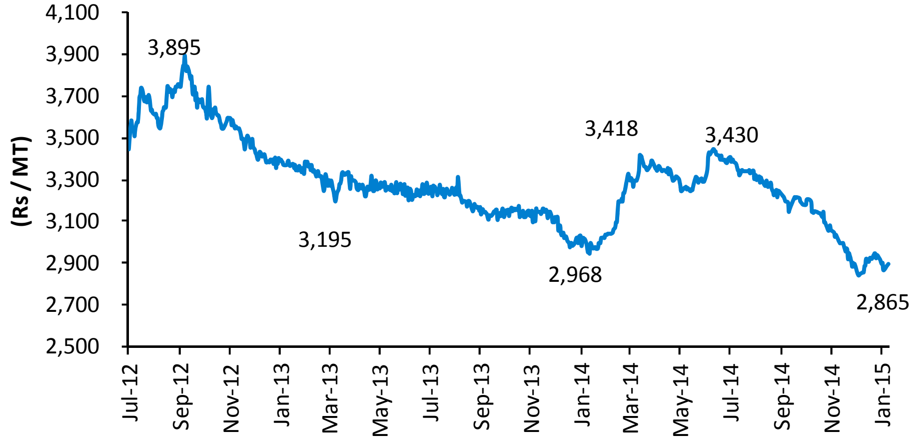
Ad spend higher by 260bps while other expenses are up by 10bps

Exhibit 5: Overheads: Ad spends up 32%; Other expenses increase 17%



Source: Company Data, PL Research

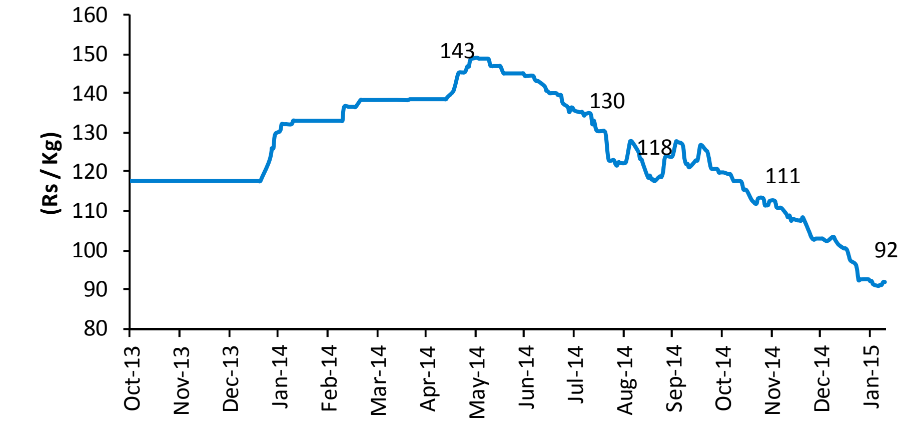
Exhibit 6: Sugar Prices: down 8% QoQ and 2.4% YoY



Source: Bloomberg, PL Research

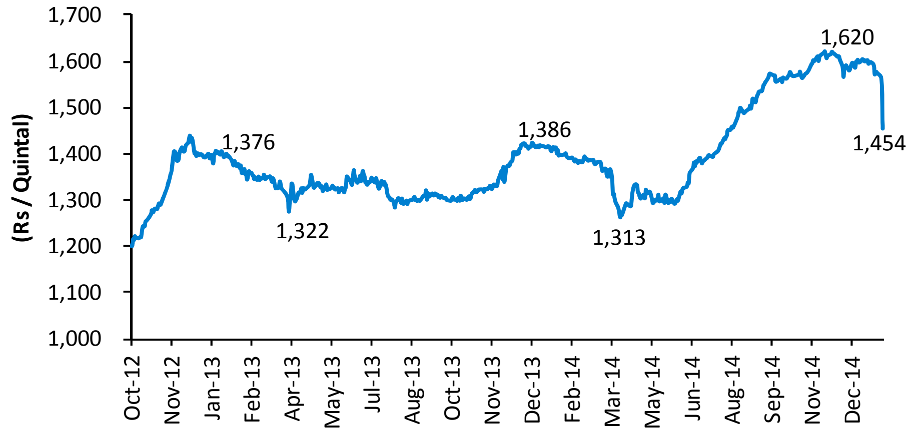
SMP prices are down 62% from its peak of Rs 149/Kg

Exhibit 7: Skimmed Milk Powder are down 11.2% YoY and 12.5% QoQ



Source: Bloomberg, PL Research

Exhibit 8: Barley Prices up 8.6% QoQ and 18.1% YoY, down 11.4% from peak



Source: Bloomberg, PL Research

Income Statement (Rs m)

Y/e March	2014*	2015E	2016E	2017E
Net Revenue	**49,018**	**44,206**	**51,464**	**59,877**
Raw Material Expenses	13,777	12,802	14,688	16,991
Gross Profit	35,241	31,404	36,775	42,887
Employee Cost	4,701	4,200	4,786	5,509
Other Expenses	21,481	19,618	22,308	25,528
EBITDA	**9,060**	**7,587**	**9,681**	**11,850**
Depr. & Amortization	625	525	767	991
Net Interest	(1,726)	(1,955)	(1,810)	(2,038)
Other Income	1,737	1,965	1,820	2,048
Profit before Tax	**10,161**	**9,017**	**10,723**	**12,896**
Total Tax	3,413	3,073	3,655	4,395
Profit after Tax	**6,747**	**5,944**	**7,069**	**8,501**
Ex-Od items / Min. Int.	—	—	—	—
Adj. PAT	**6,747**	**5,944**	**7,069**	**8,501**
Avg. Shares O/S (m)	**42.1**	**42.1**	**42.1**	**42.1**
EPS (Rs.)	**160.4**	**141.3**	**168.1**	**202.1**

Balance Sheet Abstract (Rs m)

Y/e March	2014*	2015E	2016E	2017E
Shareholder's Funds	18,128	20,993	24,314	28,308
Total Debt	—	—	—	—
Other Liabilities	(809)	(923)	(1,059)	(1,224)
Total Liabilities	**17,319**	**20,070**	**23,254**	**27,084**
Net Fixed Assets	3,784	8,233	11,465	11,974
Goodwill	—	—	—	—
Investments	18,237	17,498	18,904	24,216
Net Current Assets	(4,701)	(5,661)	(7,114)	(9,106)
Cash & Equivalents	*151*	*430*	*421*	*452*
Other Current Assets	*11,040*	*9,767*	*11,021*	*12,119*
Current Liabilities	*15,892*	*15,858*	*18,556*	*21,677*
Other Assets	—	—	—	—
Total Assets	**17,319**	**20,070**	**23,255**	**27,084**

Cash Flow Abstract (Rs m)

Y/e March	2014*	2015E	2016E	2017E
C/F from Operations	6,483	7,569	9,117	11,322
C/F from Investing	(4,022)	(4,235)	(5,406)	(6,813)
C/F from Financing	(2,341)	(3,066)	(3,693)	(4,440)
Inc. / Dec. in Cash	119	268	19	69
Opening Cash	32	151	430	421
Closing Cash	151	430	421	452
FCFF	4,796	4,350	7,780	6,016
FCFE	4,796	4,350	7,780	6,016

Quarterly Financials (Rs m)

Y/e March	Q1CY14	Q1FY15	Q2FY15	Q3FY15
Net Revenue	**11,198**	**9,660**	**11,136**	**10,125**
EBITDA	**2,300**	**1,646**	**1,957**	**1,059**
% of revenue	*20.5*	*17.0*	*17.6*	*10.5*
Depr. & Amortization	169	119	121	131
Net Interest	2	2	2	2
Other Income	480	458	619	548
Profit before Tax	**2,610**	**1,983**	**2,453**	**1,474**
Total Tax	893	682	850	510
Profit after Tax	**1,717**	**1,301**	**1,603**	**964**
Adj. PAT	**1,717**	**1,301**	**1,603**	**964**

Source: Company Data, PL Research. . **FY14 = 15 Months*

Key Financial Metrics

Y/e March	2014*	2015E	2016E	2017E
Growth				
Revenue (%)	53.1	(9.8)	16.4	16.3
EBITDA (%)	54.0	(16.3)	27.6	22.4
PAT (%)	54.5	(11.9)	18.9	20.3
EPS (%)	54.5	(11.9)	18.9	20.3
Profitability				
EBITDA Margin (%)	18.5	17.2	18.8	19.8
PAT Margin (%)	13.8	13.4	13.7	14.2
RoCE (%)	42.3	30.3	31.1	32.2
RoE (%)	42.5	30.4	31.2	32.3
Balance Sheet				
Net Debt : Equity	—	—	—	—
Net Wrkng Cap. (days)	(48)	(46)	(44)	(43)
Valuation				
PER (x)	35.2	40.0	33.6	27.9
P / B (x)	13.1	11.3	9.8	8.4
EV / EBITDA (x)	26.2	31.2	24.5	20.0
EV / Sales (x)	4.8	5.4	4.6	4.0
Earnings Quality				
Eff. Tax Rate	33.6	34.1	34.1	34.1
Other Inc / PBT	17.1	21.8	17.0	15.9
Eff. Depr. Rate (%)	7.3	4.4	5.7	5.2
FCFE / PAT	71.1	73.2	110.1	70.8

Source: Company Data, PL Research. **FY14 = 15 Months*

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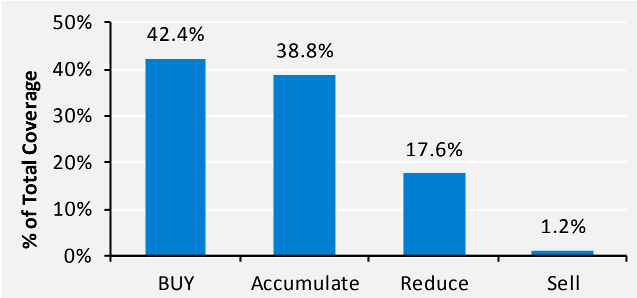

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BUY	:	Over 15% Outperformance to Sensex over 12-months
Accumulate	:	Outperformance to Sensex over 12-months
Reduce	:	Underperformance to Sensex over 12-months
Sell	:	Over 15% underperformance to Sensex over 12-months
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Not Rated (NR)	:	No specific call on the stock
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