



Colgate-Palmolive Company

Leading the industry in material reporting

Business Overview

Iconic American brand with a long history. In 1928 Palmolive-Peet Company acquired Colgate, creating the Colgate-Palmolive Company we know today, selling toothpaste and cleaning products. In 2005 the company restructured, selling off numerous major brands to focus on the higher margin oral care business along with personal and pet products. The company is listed in the top 200 largest U.S. corporations by revenues¹.

Diversified revenue stream. Colgate-Palmolive products are sold in over 200 countries. Operations are evenly split internationally between North America, Latin America, Europe, and Asia with each region contributing ~20% of revenues (see Figure 1). The business can be divided in two segments: oral, personal, and home care and the second being pet nutrition. Colgate is an industry leader in oral care maintaining a 39.9% market share of global toothpaste sales². It's main competitor in the oral care space is Procter and Gamble which owns brands such as Crest and Oral-B.

Investment Thesis

Short Term: Stable topline growth will continue in a post-COVID market. Colgate saw net sales rise 7.5% in the fourth quarter of 2020, one of the fastest growth rates the company has seen in ten years (See Figure 2). This growth was due to increased consumption caused by the COVID-19 pandemic which led to increased sales of hand and dish soap. Management expects top line growth will level off to 3%-5% in the coming years however consumption of cleaning products will be higher compared to 2019 levels³. The increase in consumption will be driven by better hygiene practices as consumers are unlikely to change their habits post pandemic.

Long Term: Company will utilize its trusted brand to drive change, offering more environmentally friendly products. Due to its dominant share of the market, Colgate will be able to drive change in the industry and command a first mover advantage in environmentally friendly products. They are currently introducing the industry's first toothpaste with recyclable packaging. They also launched a toothbrush made of bamboo with zero plastic packaging. Colgate is aware of changing consumer tastes and is adapting fast. A recent study found 74% of consumer are willing to pay more for products with sustainable packaging⁴. This preference will grow as millennials and Gen Z make up a larger portion of consumers. The consumer products industry is known for its slow steady growth; therefore, Colgate's explicit growth strategy is to branch into trendy niches with high growth (ex. acquisition of Hello Products). By being the first to offer sustainable products, Colgate is tapping into this faster growth segment and establishing itself in the minds of consumers as a sustainable brand. This enthusiasm for sustainable packaging presents a unique opportunity for Colgate to create innovative products to meet this growing demand.

Catalysts

Margin expansion through premium products. One example of this is the rollout of the Optic White toothpaste line over the past three years. In 2020 they released the latest version, marketing it as their best whitening toothpaste with 3% hydrogen peroxide. At \$7, this toothpaste is priced 133% higher compared to the peroxide free alternative⁵. Through innovation, the company is investing in its brands and continues to offer products that consumers are willing to pay a premium for which has contributed to the 19.6% growth in margins over the past four years (See Figure 3). This also can be seen in Colgate's industry leading ROIC, which shows these investments are paying off (See Figure 5).

Investing in high growth categories and incorporating a subscription-based sales model. In January 2020 Colgate acquired the oral care brand Hello Products for \$351M. The brand targets a younger audience with its charcoal and CBD based products. Its sales are based on a subscription model which is currently a fast-growing trend in the personal care sector as it ensures brand loyalty and recurring revenues⁶. Early in 2020 the company introduced the hum Electric Toothbrush sold exclusively online⁷. By purchasing online, the consumer can simultaneously sign up for a recurring subscription of refills. The toothbrush comes with a Bluetooth connection to an app which functions as a diagnostic tool to improve brushing habits. In both cases Colgate is investing in high growth trends such as charcoal/hemp products with Hello or in self diagnostic devices such as hum toothbrushes. Both examples also illustrate the company's strategy of incorporating a subscription-based offering to consumers which improves recurring revenues. The investments in high growth trends and subscription services will help the firm achieve its goal of 3%-5% annual revenue growth in the medium-long term.

Short term boost in sales will result in increased buybacks and more flexibility for future acquisitions. The increased consumption in 2020 due to the COVID-19 pandemic has given the company a short-term boost in sales which will continue for the remainder of the pandemic. Overall, the company has seen an 18% growth in free cashflow, and management has used the excess to pay down debts incurred in the acquisitions of Hello Products and Filorga along with share buybacks and dividends.

Recommendation

Target Price
Upside
Risk

BUY

\$90.19
15%
MEDIUM

Market Data

Current Price	\$78.43
52W range	\$58.49 – 86.41
Mkt Cap (mm)	\$67,228
EV (mm)	\$75,596
Current Dividend	\$1.76
Dividend Yield	2.2%
Shares Outstanding (mm)	857.2

Figure 1: Diversified Revenue Mix

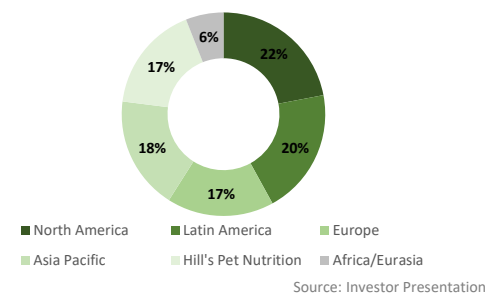


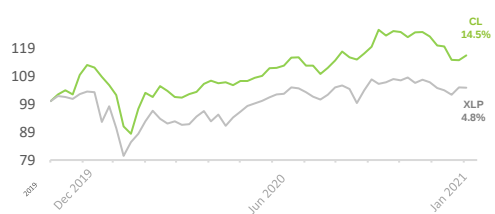
Figure 2: Revenue Growth



Figure 3: Rising FCF Margins



Figure 4: Stock Performance vs. Benchmark



The boost in sales resulted in Colgate's outperformance of the industry benchmark (XLP) by nearly 10% in 2020 (See Figure 4). By paying down its debt, Colgate is using this short-term event to strengthen its balance sheet which will provide more flexibility for future acquisitions. The recent acquisitions of Hello Products and Filorga expose Colgate to higher growth segments. Hello's products are made of charcoal and CBD making it a part of the *natural & organic personal care* market which is expected to grow at 11.1% CAGR over the next five years⁸. Filorga offers premium anti-aging creams, and the global *anti-aging* market is expected to grow at 6.8% CAGR⁹. Both segments are growing much faster than the personal care industry which only has an expected CAGR of 3.1% over the same time¹⁰. Colgate is emerging from the pandemic with a strong balance sheet which will give it more flexibility in its future acquisitions as it will have a higher debt capacity. These acquisitions will maintain Colgate's industry leading returns over the long run.

Risks
Transition risks. Despite its progress in environmental issues, Colgate remains one of the largest plastic polluters in the world¹¹. This reliance on disposable plastic products creates a great risk for the company as regulators adopt stricter regulations to limit plastic waste. The personal care industry has already experienced such regulations when the U.S and other nations banned the use of microbeads (used in exfoliating and toothpaste products) in 2017¹². As regulations on plastics becomes more stringent Colgate may face increased costs in sourcing raw materials.

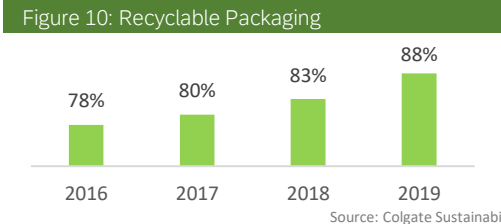
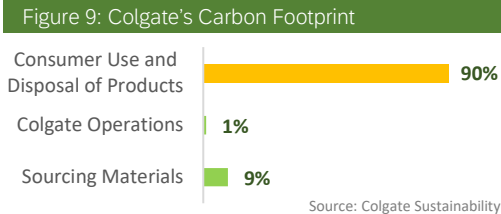
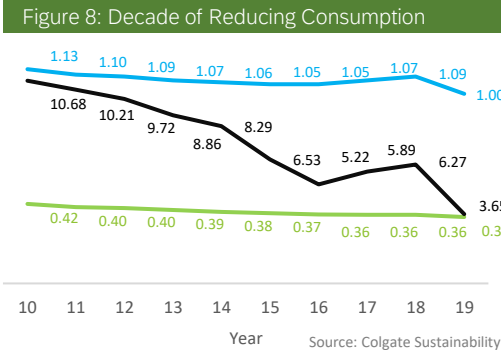
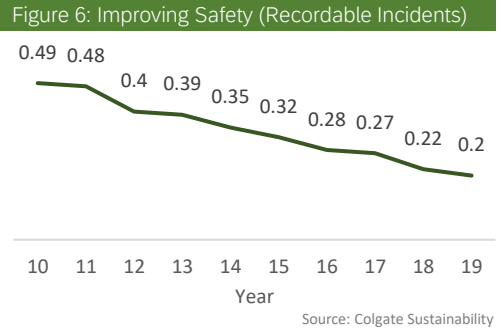
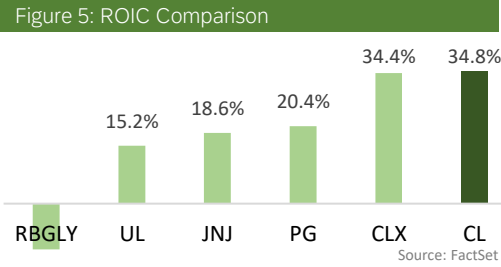
Physical risks. Colgate is a global enterprise with 78% of its sales generated outside North America. This puts its manufacturing and supply chain at risk to major global disruptions. Significant environmental changes or extreme weather could have an impact on their logistics. One example of this is the COVID-19 pandemic. Despite befitting from the pandemic, the company was negatively affected in the early months as China and other Asian nations experienced disruptions and lock downs and had an impact on sales in Asia which fell 9% in Q1 of 2020.

Environment
Strengths. Colgate's sustainability achievements have been recognized across multiple organizations. The MSCI assigns an AA rating to Colgate indicating it is an industry leader in household products industry (See Figure 7). Colgate was also listed on the Dow Jones Sustainability Index meaning it is in the top 20% of the largest U.S. companies which meet long term environmental criteria¹³. This recognition is due to the company's transparent initiatives which have materially improved sustainability. Colgate has spent the past two decades significantly reducing its water, waste, and energy consumption (See Figure 8). These achievements were due to partnerships it formed, such as *TRUE Zero* waste which helps organizations reduce waste along their supply chain, mainly in packaging. Colgate also works with the *Science Based Targets* organization which helps companies develop targets to align themselves with the Paris Agreement Goals and forces them report on their progress.

Weakness. As a consumer products corporation, Colgate is responsible for packaging waste and a large consumer of virgin plastics. *BreakFreeFromPlastic* named Colgate as one of the top ten plastic polluters in the world. Colgate's largest environmental impact is in its Scope 2 emissions which are the indirect emissions of its products along the supply chain such as; logistics, consumer use, and product end-of-life (See Figure 9). The firm is taking steps to reduce these emissions in its products offerings. Having introduced the recyclable toothpaste bottle, bamboo and aluminium toothbrushes are a few examples which are contributing a material improvement in the sustainability of their products and packaging (See Figure 10). The company will continue improving in this matter as they have pledged to cut their virgin plastic use by 1/3 in the next five years.

Social
Improving safety & transparency. As part of its commitment to transparency, Colgate has listed all U.S. products on SmartLabel, a platform where consumers can scan a barcode and learn about all the ingredients and their functions in Colgate products. This service helps consumers make informed decisions about the products they purchase¹⁴. Colgate has also made great progress in its safety record. The *total recordable rate* (recordable incidents) has declined 60% in the past decade and the *lost workday case rate* is also at an all time low (See Figure 6). Safety data is verified by third parties who visited Colgate sites to ensure impartiality¹⁵.

Governance
Diverse and independent board. 90% of board members are independent and 40% of the seats are held by women. The office of Chairman and CEO are not separated and held by Noel Wallace; who is the only non-independent board member. Compensation for board members is 74% performance based which is awarded based on EPS, payout, and organic sales growth targets. Stock options and PBRU's are used to ensure long term shareholder value creation as their value is derived from the appreciation of the stock price. The company also maintains a clawback policy where equity can be recouped if financial results are restated or for misconduct, and this is another method of ensuring long term goals are met¹⁶. Colgate ties senior management compensation, in part, to sustainability objectives which is a necessary incentive to ensure the company meets its objectives¹⁷.



Works Cited

1. (2021). Colgate Palmolive. Wikipedia. Retrieved from: <https://en.wikipedia.org/wiki/Colgate-Palmolive>
2. (2021). Form 10-Q. Colgate Palmolive. Retrieved from: <https://investor.colgatepalmolive.com/static-files/48985cba-a716-4aa6-b42d-94ef38b8dd37>
3. (2020). Colgate Palmolive Q4 Earnings Call. Motley Fool. Retrieved from: <https://www.fool.com/earnings/call-transcripts/2021/01/29/colgate-palmolive-co-cl-q4-2020-earnings-call-tran/>
4. Holbrook, Emily. (April 2020). New Report Finds Overwhelming Majority of Consumers Are Willing to Pay More for Sustainable Packaging. Environment Energy Leader. Retrieved from: <https://www.environmentalleader.com/2020/04/new-report-finds-overwhelming-majority-of-consumers-are-willing-to-pay-more-for-sustainable-packaging/>
5. (2020). Investor Presentation. Colgate Palmolive. Retrieved from: <https://investor.colgatepalmolive.com/static-files/a65490ac-2442-41e3-8751-e18a1471bd92>
6. (2021). Hello Products. Retrieved from: <https://www.hello-products.com/shop/charcoal/>
7. (2021). Colgate Palmolive. Retrieved from: <https://hum.colgate.com/products/hum-battery-powered-toothbrush>
8. (May 2018). Natural & Organic Personal Care Market. Credence Research. Retrieved from: <https://www.credenceresearch.com/report/natural-and-organic-personal-care-market>
9. Wood, Laura. (July 2020). Anti-Aging Products Industry Projected to be Worth \$83.2 Billion by 2027. Research and Markets. Retrieved from: <https://www.globenewswire.com/news-release/2020/07/24/2067180/0/en/Anti-Aging-Products-Industry-Projected-to-be-Worth-83-2-Billion-by-2027-Key-Trends-Opportunities-and-Players.html>
10. (2021). Statista. Retrieved from: <https://www.statista.com/outlook/70000000/108/beauty-personal-care/canada>
11. Segran, Elizabeth. (November 2019). Coca-cola, Nestle and PepsiCo are the world's biggest plastic polluters-again. Fast Company. Retrieved from: <https://www.fastcompany.com/90425011/coca-cola-nestle-and-pepsico-are-the-worlds-biggest-plastic-polluters-again>
12. (2021). Microbeads. Wikipedia. Retrieved from: <https://en.wikipedia.org/wiki/Microbead#Use>
13. (2021). Dow Jones Sustainability North America Composite Index. S&P Dow Jones Indices. Retrieved from: <https://www.spglobal.com/spdji/en/indices/esg/dow-jones-sustainability-north-america-composite-index/#overview>
14. (May 2020). Colgate Proxy Statement. Colgate Palmolive. Retrieved from: <https://investor.colgatepalmolive.com/static-files/97f15c8b-41ca-4e7a-a722-8e513e5d4f45>
15. (2021). Governance Commitment in Action. Colgate Palmolive. Retrieved From: <https://www.colgatepalmolive.com/en-us/about/governance/governance-commitment-in-action>
16. (2021). Our 2019 Progress – Performance. Colgate Palmolive. Retrieved From: <https://www.colgatepalmolive.com/en-us/core-values/sustainability/performance>
17. (2021). Our 2019 Progress – People. Colgate Palmolive. Retrieved From: <https://www.colgatepalmolive.com/en-us/core-values/sustainability/people>

Miscellaneous

- (2021). Concordia Sustainable Investing Practicum. Retrieved from: <https://www.linkedin.com/company/concordia-university-sustainable-investing-practicum/?originalSubdomain=ca>
- (2021). ESG Rating – Colgate. MSCI. Retrieved from: <https://www.msci.com/our-solutions/esg-investing/esg-ratings/esg-ratings-corporate-search-tool/>