

Assessing Earnings Quality of Colgate-Palmolive Using Beneish M-Score, Piotroski Score and Modified C-Score

Yafet Mulaw

Financial Analysis Report (FY2023–FY2024)

1. Company Overview

Colgate-Palmolive is a global consumer goods company operating in the fast-moving consumer goods (FMCG) sector, primarily focused on oral care, personal care, home care and pet nutrition products. The company has a strong global presence with well-established brands and a stable demand base driven by essential consumer products.

The FMCG industry is characterized by stable cash flows, strong brand competition, pricing power and operational efficiency. Colgate-Palmolive holds a strong market position within the oral care segment and benefits from brand strength, global distribution and consistent consumer demand.

The company's business model focuses on high-volume consumer sales, brand-driven pricing and operational efficiency to generate consistent margins and cash flows.

2. Objective of Analysis

The objective of this analysis is to assess the earnings quality and financial reliability of Colgate-Palmolive for FY2023 and FY2024 using structured forensic and fundamental analysis tools.

This analysis aims to:

- Evaluate the likelihood of earnings manipulation
- Assess financial strength and sustainability
- Analyze consistency between profits and cash flows
- Identify any accounting red flags
- Provide a structured view of earnings quality for investment or credit evaluation

The analysis is conducted from the perspective of a junior financial analyst evaluating the company's financial integrity and operational strength.

3. Methodology Used

The analysis was conducted using financial data from FY2023 and FY2024 in Excel. The following models were applied:

Beneish M-Score

The Beneish M-score is a forensic accounting model used to detect potential earnings manipulation.

It analyzes variables such as receivables, margins, asset quality, depreciation and accruals.

- Score less than -1.78 → Low probability of earnings manipulation
- Score greater than -1.78 → Possible manipulation risk

This model helps evaluate the reliability of reported earnings.

Piotroski F-Score

The Piotroski score measures a company's financial strength using nine accounting-based criteria across:

- Profitability
- Leverage and liquidity
- Operating efficiency

Scores range from 0 to 9:

- 7–9 → Strong financial position
- 4–6 → Average
- 0–3 → Weak fundamentals

It indicates overall financial health and operational improvement.

Modified C-Score (Earnings Quality Checks)

The Modified C-score evaluates earnings quality by examining divergences between income and cash flow and changes in working capital or asset structure.

Key checks include:

- Net income vs operating cash flow divergence
- Receivable and inventory trends
- Other current assets vs revenue growth
- Depreciation trends
- Total asset growth patterns

This model helps identify aggressive accounting or deterioration in earnings quality.

4. Financial Analysis & Findings

Beneish M-Score Analysis

The calculated Beneish M-score for Colgate-Palmolive is **-2.616**.

This score is below the threshold of -2.22, indicating a **low probability of earnings manipulation**.

Key observations:

- Receivables growth remained aligned with revenue growth.
- Gross margins and asset quality remained stable.
- Accrual levels were low and consistent with operations.
- Leverage and depreciation indicators did not show abnormal changes.

Overall, the Beneish model suggests that reported earnings are reliable and not artificially inflated.

Piotroski F-Score Analysis

Colgate-Palmolive recorded a **Piotroski F-score of 7**, indicating strong financial fundamentals.

Positive indicators:

- Positive net income and return on assets
- Positive operating cash flows
- Strong gross margin improvement
- Improved asset turnover
- No new equity dilution
- Reduction in long-term debt

Areas of moderation:

- Operating cash flow did not exceed net income in the current year
- Current ratio did not show improvement

Despite these minor factors, a score of 7 reflects **strong financial health, improving efficiency and stable profitability**.

Modified C-Score (Earnings Quality Assessment)

The modified C-score checks indicate that Colgate-Palmolive qualifies as a **non-modifier company**, suggesting no earnings quality concerns.

Key findings:

Cash Flow vs Net Income

- No widening divergence between net income and operating cash flow
- Both increased proportionally from FY2023 to FY2024
- Indicates strong cash-backed earnings

Receivables & Working Capital

- Days sales outstanding declined significantly
- Suggests improved collection efficiency and revenue quality

Inventory Management

- Inventory days slightly decreased
- Indicates stable demand and efficient inventory control

Other Current Assets

- Other current assets declined while revenue increased
- Suggests conservative accounting practices

Depreciation Trends

- Depreciation increased proportionally with asset base
- No indication of aggressive depreciation adjustments

Total Assets

- Total assets declined slightly year-over-year
- Indicates controlled expansion and disciplined capital allocation

Overall, the Modified C-score analysis indicates **high-quality, sustainable earnings** with no accounting red flags.

5. Key Insights

- Beneish M-score indicates low probability of earnings manipulation.
- Piotroski score of 7 reflects strong financial health and improving operational efficiency.
- Operating cash flow trends closely match net income, supporting earnings reliability.
- Working capital management improved with better receivable and inventory control.
- No significant accounting red flags observed in asset or depreciation trends.
- Overall earnings quality appears strong and sustainable.

6. Conclusion

Based on Beneish M-score, Piotroski F-score and Modified C-score analysis, ColgatePalmolive demonstrates strong earnings quality and financial reliability for FY2023–FY2024.

The company shows consistent profitability supported by stable operating cash flows and efficient working capital management. There is no statistical indication of earnings manipulation, and financial fundamentals remain strong.

From an analytical perspective, Colgate-Palmolive reflects a **financially stable, low-risk and high earnings-quality profile**, making it suitable for long-term fundamental evaluation from both equity and credit viewpoints.

7. Learning Outcome

This project enhanced my understanding of forensic accounting tools used to assess earnings quality and detect manipulation risk.

It strengthened my ability to apply Beneish M-score, Piotroski F-score and modified C-score in a practical Excel-based analysis. The exercise improved my skills in interpreting financial statements beyond ratios and evaluating the reliability of reported earnings from an analyst's perspective.