

April 21, 2022

RESULT REPORT Q1 CY22 | Sector: Consumer Staples

# Nestle India

## Resilient growth performance and outlook; maintain ADD given rich valuations and near-term margin headwinds

### Our view

Nestle delivered strong topline in domestic business with volume growth of ~7% on base of 3.2% while margins were under pressure amidst elevated inflation across key raw materials. Growth was led by innovative campaigns, attractive promotions and tech-led insights and distribution drives. Strong rural growth despite rural headwinds indicates strong progress on the RURBAN journey with distribution efforts in semi-urban/rural markets continuing to drive increase in category penetration. While gross margins have come under severe pressure, company has been able to offset that partially with strong cost controls and calibrated price hikes. Double-digit growth across segments other than the challenging milk products business, strong 71% growth in e-commerce business and strong recovery in Out of Home business were positive takeaways. We continue to believe that NEST's core categories have a strong runway for growth given scope for increase in penetration with aggressive innovations also adding to the growth. Given continued outperformance over FMCG peers, we believe NEST should continue commanding a valuation premium and should deliver steady growth in the medium term despite inflation headwinds given strong innovation/distribution/premiumization initiatives. With confectionery and coffee segments growing well and prepared dishes set to benefit from recent capacity expansion, we see continued double-digit volume-led growth for the company with margins expected to normalize after correcting in CY22E helping keep up the margin trajectory from CY23 onwards in addition to high dividend payouts helping sustain the strong return ratios further. But as the stock has not participated in the recent sector correction, absolute upside remains limited, hence we maintain our ADD rating on the stock.

### Result Highlights

- **Results summary** - Nestle Q1 performance was slightly lower on margins front with revenue/EBITDA/PAT growth of 10.2%/-0.6%/-1.3% driven by high single-digit volume/mix growth with elevated inflation impacting margins. Company declared interim dividend of Rs 25/share.

### Valuation

Our key investment thesis of sustained double-digit domestic growth and premiumization potential of its categories, opportunities for further deepening distribution especially in rural markets and aggression on new launches and marketing spends remains intact. We cut our margin estimates for CY22 to incorporate near-term margin headwinds and now build in 12%/16% revenue/PAT CAGR over CY21-23E. We reiterate our ADD rating with a revised PT of Rs 19,387 based on 60x CY23E earnings, with premium valuations supported by best-in-class growth visibility and return ratios.

### Exhibit 1: Actual vs estimate

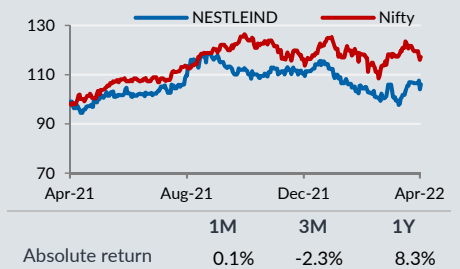
Rsmn	Actual	Estimate		% Variation		Remarks
		YES Sec	Consensus	YES Sec	Consensus	
Sales	39,807	39719	39614	0.2	0.5	
EBITDA	9,247	9453	9590	(2.2)	(3.6)	
EBITDA Margin (%)	23.2	23.8	24.2	(57.2) bps	(98.0) bps	Revenue in-line, gross margin dipped 310bps due to higher inflation in RM prices
Adjusted PAT	5,947	6208	6348	(4.2)	(6.3)	

Reco	: ADD
CMP	: Rs 18,300
Target Price	: Rs 19,387
Potential Return	: +5.9%

### Stock data (as on April 20, 2022)

Nifty	17,137
52 Week h/l (Rs)	20609 / 16255
Market cap (Rs/USD mn)	1764909 / 23158
Outstanding Shares (mn)	96
6m Avg t/o (Rs mn):	1,016
Div yield (%)	0.5
Bloomberg code:	NEST IN
NSE code:	NESTLEIND

### Stock performance



### Shareholding pattern (As of Mar'22 end)

Promoter	62.8%
FII+DII	20.2%
Others	17.0%

### Δ in stance

(1-Yr)	New	Old
Rating	ADD	ADD
Target Price	19,387	19,400

### Δ in earnings estimates

	CY22e	CY23e
EPS (New)	262.7	323.1
EPS (Old)	278.9	323.3
% change	-5.8	-

### Financial Summary

(Rs mn)	CY21	CY22E	CY23E
Revenue	1,47,094	1,65,453	1,85,105
YoY Growth (%)	10.2	12.5	11.9
EBIDTA	35,915	38,636	46,283
Margins (%)	24.4	23.4	25.0
PAT	23,218	25,331	31,156
YoY Growth (%)	11.5	9.1	23.0
ROE	113.2	111.8	111.2
ROCE	159.2	156.0	154.8
EPS	222.4	262.7	323.1
P/E	82.3	69.7	56.6
EV/EBITDA	48.9	45.4	37.7

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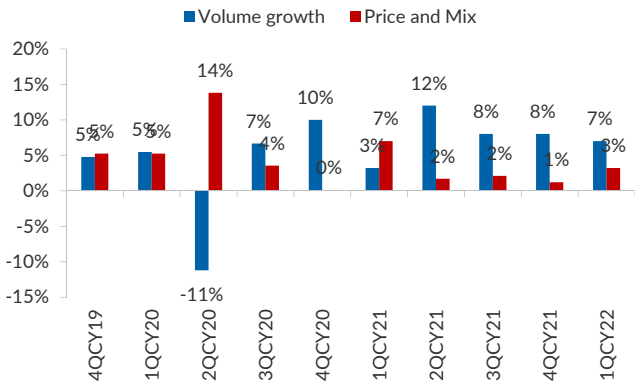
- **Topline** – Revenue came in at Rs 39.8bn, up 10.2% led by volume and mix-led growth in domestic sales led by double-digit growth in confectionary and beverages portfolio with strong performance from Kitkat, Munch, Nescafe Classic and Sunrise; export sales were lower by 1% due to change in product mix.
- **Margins** – Gross margins were down sharply by 310bps to 55.4% given inflation in edible oil, milk and packaging materials. EBITDA margins were also down 260bps yoy to 23.2% partially aided by a combination of higher cost savings and lower employee costs.
- **Management commentary** – Strong volume/mix growth amidst volatility and elevated inflation in RM led to 10.2% revenue growth in domestic sales. Key brands Maggi Noodles, KitKat, Nestlé Munch, Nescafé Classic and Sunrise posted double-digit growth with sustained rural growth. E-commerce grew 71% contributing 6.3% of domestic sales. Management indicated that consistent inflation in RM likely to continue in short to medium term which would be navigated with efficiencies, scale and calibrated price hikes.
- **Channel-wise performance** – New formats like ‘Quick commerce’ and ‘click and mortar’ led to 71% growth in Q1, organized trade channel delivered broad based growth as footfall normalized. OOH recovered faster after temporary blip in January sales driven by faster channel opening, channel & geographical initiatives and portfolio transformation. Channel expansion in UK and Australia and expanded offerings in Maggi range led to recovery in export sales.
- **Category-wise performance** – **Prepared dishes**- continued momentum with media campaigns drove growth in Maggi noodles, Masala-ae-Magic and sauces muted due to high high base and decreased in-home consumption; **Milk Products** – price hikes aided nutrition portfolio while milk products continue to face competition; **Confectionery** – Key brands Kitkat, Munch posted double-digit growth led by attractive promotion campaigns and distribution drives; **Beverages** – Strong double-digit growth in Nescafe Classic and Sunrise led by consumption season.
- **Commodity price outlook** – Prices of key commodities like wheat, coffee and edible oils should remain firm to bullish; packaging material prices continue to rise given supply constraints and rising fuel and transportation costs; milk prices to remain firm with higher demand and rising feed costs; company aggressively exploring more cost optimization and efficiency measures to counter this inflation.

## Exhibit 2: Quarterly snapshot

Particulars (Rs mn)	1QCY21	2QCY21	3QCY21	4QCY21	1QCY22	% yoy	% qoq	CY21	CY20	% yoy
Sales	36,108	34,767	38,826	37,393	39,807	10.2	6.5	1,47,094.1	1,33,500.3	10.2
EBITDA	9,299	8,480	9,480	8,657	9,247	(0.6)	6.8	35,915.4	32,015.0	12.2
EBITDA Margin %	25.8	24.4	24.4	23.2	23.2	(252.4) bps	7.8 bps	24.4	24.0	43.5 bps
Depreciation	936	953	955	1,058	1,043	11.4	(1.4)	3,901.9	3,703.8	5.3
EBIT	8,362.5	7,527.1	8,524.6	7,599.3	8,203.7	(1.9)	8.0	32,013.5	28,311.2	13.1
EBIT Margin %	23.2	21.7	22.0	20.3	20.6	(255.1) bps	28.6 bps	21.8	21.2	55.7 bps
Interest charges	540	517	519	436	356	(34.2)	(18.4)	2,011.9	1,641.8	22.5
Other Income	297	295	337	273	214	(27.7)	(21.6)	1,201.1	1,458.5	(17.6)
PBT	8,119	7,305	8,342	7,437	8,062	(0.7)	8.4	31,203	28,128	10.9
Tax	2,096	1,919	2,169	1,801	2,115	0.9	17.4	7,985.1	7,303.6	9.3
Effective Tax Rate (%)	25.8	26.3	26.0	24.2	26.2			25.6	26.0	
PAT	6,023	5,386	6,174	5,636	5,947	(1.3)	5.5	23,218	20,824	11.5
PAT Margin %	16.7	15.5	15.9	15.1	14.9	(173.9) bps	(13.1) bps	15.8	15.6	18.6 bps
EPS (Rs)	62.5	55.9	64.0	58.4	61.7	(1.3)	5.5	240.8	216.0	11.5

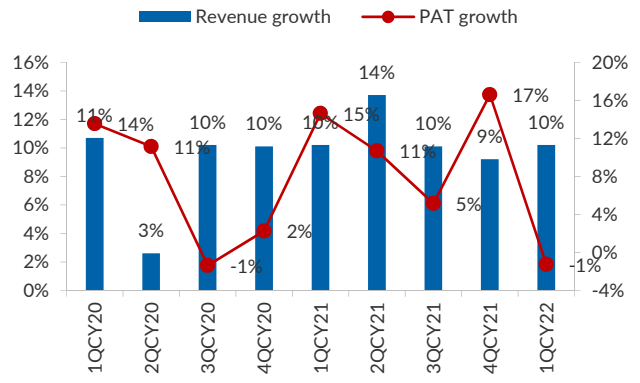
Source: Company, YES Sec

**Exhibit 3: Strong 7% volume growth driven by strong performance from rural with increase in penetration**



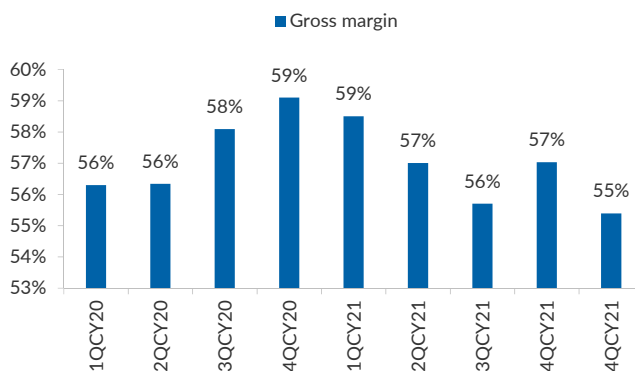
Source: Company, YES Sec

**Exhibit 4: PAT flat YoY owing to lower gross margin**



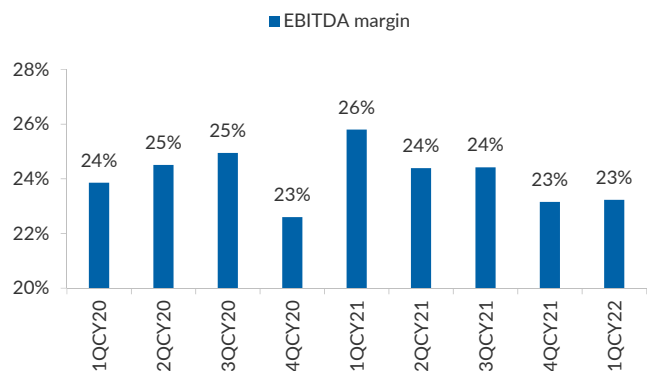
Source: Company, YES Sec

**Exhibit 5: Gross margin fell 310bps due to continued inflation in edible oil, milk and packing material**



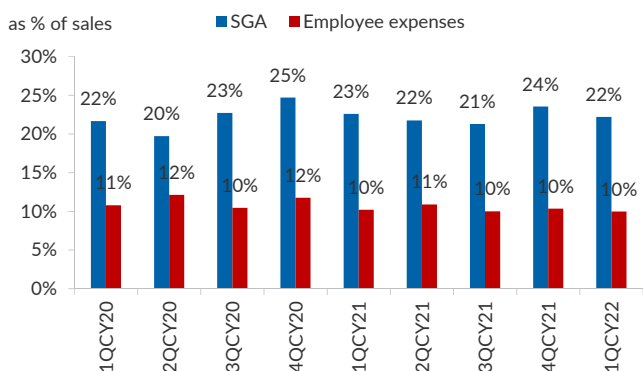
Source: Company, YES Sec

**Exhibit 6: Lower employee and other expenses partially helped EBITDA margin**



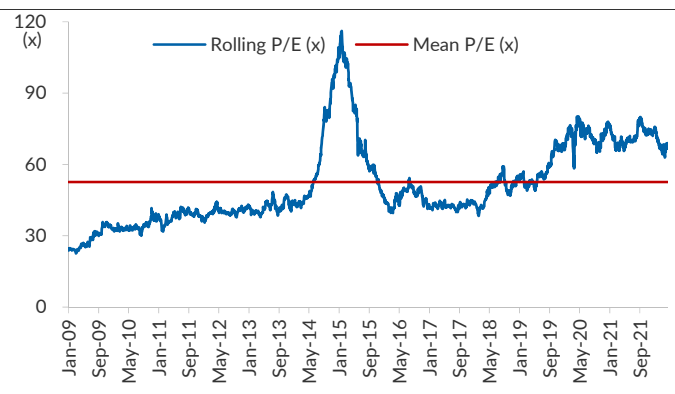
Source: Company, YES Sec

**Exhibit 7: Savings in employee and SGA expenses continue to offset gross margin contraction**



Source: Company, YES Sec

**Exhibit 8: Currently trading at 68x one-yr fwd earnings**



Source: Company, YES Sec

## FINANCIALS

### Exhibit 9: Balance Sheet

Y/e 31 Mar (Rs m)	CY19	CY20	CY21	CY22E	CY23E
Equity capital	964	964	964	964	964
Reserves	19,229	19,881	23,517	30,567	19,229
Net worth	20,193	20,845	24,481	31,532	20,193
Debt	348	341	341	341	348
Deferred tax liab (net)	199	0	0	0	199
Other non current liabilities	32,904	33,045	36,350	39,985	32,904
Total liabilities	53,645	54,231	61,171	71,857	53,645
Fixed Asset	26,066	28,992	32,436	35,859	26,066
Investments	14,638	7,740	7,740	7,740	14,638
Other Non-current Assets	1,483	14,947	16,442	18,086	1,483
Net Working Capital	-7,991	-6,645	-7,310	-8,177	-7,991
Inventories	14,165	15,802	17,225	19,271	14,165
Sundry debtors	1,649	1,653	1,813	2,029	1,649
Loans and Advances	132	119	453	507	132
Other current assets	387	1,333	1,467	1,613	387
Sundry creditors	15,166	17,349	19,945	22,314	15,166
Other current liabilities	8,102	6,817	6,799	7,607	8,102
Provision	1,056	1,385	1,524	1,676	1,056
Cash & equivalents	19,449	9,196	11,863	18,349	19,449
Total Assets	53,645	54,231	61,171	71,857	53,645

Source: Company, YES Sec

### Exhibit 10: Income statement

Y/e 31 Mar (Rs m)	CY19	CY20	CY21	CY22E	CY23E
Revenue	1,23,689	1,33,500	1,47,094	1,65,453	1,85,105
Operating profit	29,259	32,015	35,915	38,636	46,283
Depreciation	3,702	3,704	3,902	4,555	4,578
Interest expense	1,291	1,642	2,012	2,018	2,216
Other income	2,469	1,459	1,201	1,802	2,162
Profit before tax	26,735	28,128	31,203	33,865	41,652
Taxes	7,051	7,304	7,985	8,534	10,496
Adj. PAT	19,684	20,824	23,218	25,331	31,156
Exceptional loss	249	140	1,769	-	-
Net profit	19,436	20,685	21,449	25,331	31,156

Source: Company, YES Sec

## Exhibit 11: Cash flow statement

Y/e 31 Mar (Rs m)	CY19	CY20	CY21	CY22E	CY23E
PBIT	28,026	29,770	33,215	35,883	43,868
Depreciation	3,702	3,704	3,902	4,555	4,578
Tax paid	(7,051)	(7,304)	(7,985)	(8,534)	(10,496)
Working capital Δ	190	556	(1,347)	666	867
Other operating items					
Operating cashflow	24,867	26,726	27,785	32,570	38,816
Capital expenditure	(1,164)	(7,249)	(6,828)	(8,000)	(8,000)
<b>Free cash flow</b>	<b>23,703</b>	<b>19,477</b>	<b>20,957</b>	<b>24,570</b>	<b>30,816</b>
Equity raised	(1,422)	5,389	(1,513)	-	(0)
Investments	9,074	2,873	6,898	-	-
Debt financing/disposal	180	(183)	(8)	-	-
Interest Paid	(1,291)	(1,642)	(2,012)	(2,018)	(2,216)
Dividends paid	(35,563)	(25,069)	(19,284)	(21,695)	(24,105)
Other items	3,737	4,085	(15,291)	1,810	1,991
<b>Net Δ in cash</b>	<b>(1,582)</b>	<b>4,930</b>	<b>(10,253)</b>	<b>2,667</b>	<b>6,486</b>

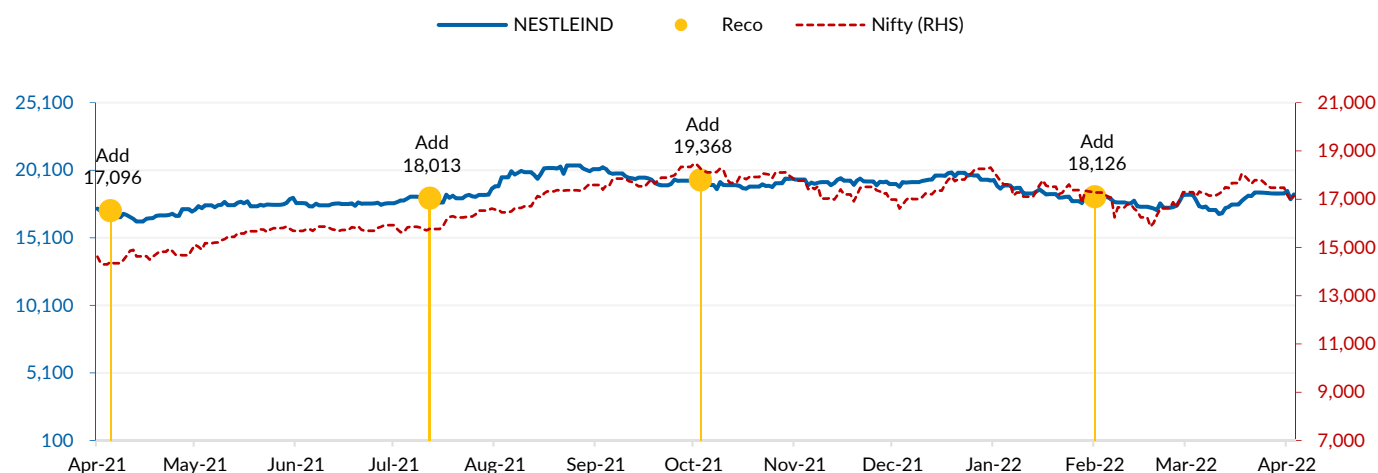
## Exhibit 12: Growth and Ratio matrix

Y/e 31 Mar	CY19	CY20	CY21	CY22E	CY23E
<b>Growth matrix (%)</b>					
Revenue growth	9.5	7.9	10.2	12.5	11.9
Op profit growth	7.1	9.4	12.2	7.6	19.8
EBIT growth	5.5	6.2	11.6	8.0	22.3
Net profit growth	14.3	5.8	11.5	9.1	23.0
<b>Profitability ratios (%)</b>					
OPM	23.7	24.0	24.4	23.4	25.0
EBIT margin	22.7	22.3	22.6	21.7	23.7
Net profit margin	15.9	15.6	15.8	15.3	16.8
RoCE	98.7	147.9	159.2	156.0	154.8
RoNW	70.4	105.8	113.2	111.8	111.2
RoA	25.9	28.0	29.4	29.9	32.3
<b>Per share ratios</b>					
EPS	204.2	216.0	240.8	262.7	323.1
Dividend per share	306.0	260.0	200.0	225.0	250.0
Cash EPS	242.5	254.4	281.3	310.0	370.6
Book value per share	199.0	209.4	216.2	253.9	327.0
<b>Valuation ratios</b>					
P/E	89.6	84.7	76.0	69.7	56.6

Y/e 31 Mar	CY19	CY20	CY21	CY22E	CY23E
P/CEPS	75.5	71.9	65.1	59.0	49.4
P/B	92.0	87.4	84.6	72.1	56.0
EV/EBIDTA	59.8	54.5	48.9	45.4	37.7
<b>Payout (%)</b>					
Dividend payout	180.7	120.4	83.1	85.6	77.4
Tax payout	26.4	26.0	25.6	25.2	25.2
<b>Liquidity ratios</b>					
Debtor days	4	5	4	4	4
Inventory days	38	39	39	38	38
Creditor days	44	41	43	44	44

Source: Company, YES Sec

## Recommendation Tracker



Source: Company, YES Sec

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