

Nestle India

5 August 2019

Reuters: NEST.BO; Bloomberg: NEST IN

Tracking expectations

Nestle India's 2QCY19 (NEST) result is in line with expectations, driven by volume and mix improvement. However, export sales are weak on account of lower coffee exports to Turkey. Domestic revenue growth for the quarter is in double digits, led by volume growth, mix improvement and high innovation intensity. Operating margin declined slightly on YoY basis because of headwinds in commodity prices, but continue to remain in the operating band of 23%-24%. Operating margin is down by 70bps and may come under pressure given the hardening of commodity costs and softer demand conditions similar to other FMCG companies. Maggi, Kitkat and Munch continue to perform strongly and the company has announced its 9th factory in Sanand, Gujarat for Maggi Noodles, which will involve an initial investment of Rs7bn over the next two years. The company continues to strengthen its innovation agenda with new launches in CEREGROW NESTEA and Maggi range. We expect the company to continue performing well by leveraging its strong R&D, sourcing and supply chain capabilities. The stock has fared well and has tracked our expectations consistently. Going ahead, the demand conditions are expected to be soft given the slowdown in consumption being witnessed across the industry and headwinds from commodity costs. In view of the above scenario, we have revised our rating to Accumulate from Buy after revising our earnings estimates with a target price (TP) of Rs12,350 (Rs12,100 earlier), implying an upside of 8% from the current market price, based on an unchanged P/E multiple of 55x.

Healthy growth in domestic sales: NEST's domestic sales growth for the quarter is in double digits and is in line with our estimates. However, export sales remained weak on account of reduced exports to markets such as Turkey. Considering the fact that the company continues to strengthen its innovation agenda and with its recent plan to enter the organic food segment, we feel fairly confident that it will be able to deliver healthy volume growth.

Margins remain steady: Although the operating margin has declined by 70bps it has remained in the band of 23%-24%. Unlike the previous quarters, crude oil and other commodity headwinds have re-emerged and will have to be watched closely. But, considering the fact that the company has a good efficiency programme, we believe it remains in a good position to sustain margin expansion in CY19-CY20.

Outlook and valuation: The demand conditions are expected to be soft given the slowdown in consumption being witnessed across the industry while the commodity costs, which remained favourable, have started hardening. Therefore, we revise our rating to Accumulate from Buy after slightly revising our earnings estimates with a TP of Rs12,350 (Rs12,100 earlier), implying an upside of 8% from the current market price, on an unchanged P/E multiple of 55x.

ACCUMULATE

Sector: FMCG

CMP: Rs11,411

Target Price: Rs12,350

Upside: 8%

Ayush Chaturvedi

Research Associate

ayush.chaturvedi@nirmalbang.com

+91-22-6273 8244

Key Data

Current Shares O/S (mn)	96.4
Mkt Cap (Rsbn/US\$bn)	1,100.2/15.8
52 Wk H / L (Rs)	12,026/9,047
Daily Vol. (3M NSE Avg.)	64,462

Price Performance (%)

	1 M	6 M	1 Yr
Nestle India	(4.6)	(1.3)	6.1
Nifty Index	(7.7)	1.0	(2.2)

Source: Bloomberg

Y/E March (Rsmn)	2QCY18	1QCY19	2QCY19	YoY (%)	QoQ (%)	H1CY18	H1CY19	YoY (%)
Net Sales	26,984	30,030	30,009	11.2	(0.1)	54,556	60,038	10.0
COGS	10,890	12,453	12,522	15.0	0.5	22,167	24,975	12.7
% of sales	40.4	41.5	41.7	1.4	0.3	40.6	41.6	1.0
Gross margin %	59.6	58.5	58.3	(1.4)	(0.3)	59.4	58.4	(1.0)
Employee costs	2,849	3,038	3,146	10.4	3.6	5,539	6,183	11.6
% of sales	10.6	10.1	10.5	(0.1)	0.4	10.2	10.3	0.1
Other expenses	6,795	7,162	7,368	8.4	2.9	13,433	14,530	8.2
% of sales	25.2	23.8	24.6	(0.6)	0.7	24.6	24.2	(0.4)
EBITDA	6,450	7,377	6,973	8.1	(5.5)	13,418	14,350	6.9
EBITDA margin %	23.9	24.6	23.2	(0.7)	(1.3)	24.6	23.9	(0.7)
Depreciation	817	780	808	(1.1)	3.7	1,642	1,588	(3.3)
EBIT	5,633	6,598	6,165	9.4	(6.6)	11,776	12,762	8.4
EBIT margin %	20.9	22.0	20.5	(0.3)	(1.4)	21.6	21.3	(0.3)
Interest expense	283	316	299	5.9	(5.3)	593	615	3.7
Other income	602	732	726	20.5	(0.8)	1,167	1,458	25.0
Exceptional items	-	-	-	-	-	-	-	-
PBT	5,953	7,013	6,592	10.7	(6.0)	12,349	13,605	10.2
Tax	2,003	2,381	2,213	10.5	(7.0)	4,159	4,594	10.4
Effective tax rate %	33.6	33.9	33.6	(0.1)	(0.4)	33.7	33.8	0.1
PAT	3,950	4,633	4,378	10.9	(5.5)	8,190	9,011	10.0
PAT margin %	14.3	15.1	14.2	(0.1)	(0.8)	14.7	14.7	-
EPS	41.0	48.1	45.4	10.9	(5.5)	85	93.5	10.0

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 1: Financial summary

Y/E December (Rsmn)	CY16	CY17	CY18	CY19E	CY20E
Net revenues	91,413	1,00,096	1,12,923	1,25,990	1,41,723
YoY growth (%)	11.8	9.5	12.8	11.6	12.5
EBITDA	18,498	20,965	26,246	29,819	34,887
EBITDA margin (%)	20.2	20.9	23.2	23.7	24.6
PAT	10,014	12,252	16,070	18,446	21,682
EPS (Rs)	103.9	127.1	166.7	191.4	224.9
YoY growth (%)	77.8	22.4	31.2	14.8	17.5
RoCE (%)	47.0	51.8	63.7	66.0	70.0
RoE (%)	31.7	36.6	45.3	46.9	49.4
P/E (x)	58.0	78.3	62.1	59.6	46.0
P/BV (x)	17.7	28.1	27.2	26.2	21.7
EV/EBITDA (x)	30.3	44.4	36.7	35.6	27.1

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 2: Our estimates versus actual performance

Y/E Dec. (Rsmn)	2QCY18	1QCY19	2QCY19	YoY (%)	QoQ (%)	NBIE estimate	Variation (%)
Net sales	26,984	30,030	30,009	11.2	(0.1)	29,952	0.2
EBITDA	6,450	7,377	6,973	8.1	(5.5)	7,248	(3.8)
EBITDA margin (%)	23.9	24.6	23.2	(70 bps)	(130 bps)	24	(100 bps)
Net income	3,950	4,633	4,378	10.9	(5.5)	4,482	(2.3)

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 3: Change in our estimates

Y/E December (Rsmn)	Old estimate		New estimate		Change (%)	
	CY19E	CY20E	CY19E	CY20E	CY19E	CY20E
Net sales	1,24,764	1,38,189	1,25,990	1,41,723	1.0	2.6
EBITDA	29,815	33,848	29,819	34,887	0.0	3.1
EBITDA (%)	24	24	23.7	24.6	(20bps)	10bps
PAT	18,492	21,038	18,446	21,682	(0.2)	3.1

Source: Company, Nirmal Bang Institutional Equities Research

Financials (standalone)

Exhibit 4: Income statement

Y/E December (Rsmn)	CY16	CY17	CY18	CY19E	CY20E
Net sales	91,413	1,00,096	1,12,923	1,25,990	1,41,723
% Growth	11.8	9.5	12.8	11.6	12.5
COGS	38,828	43,269	45,902	51,718	57,111
Staff costs	9,016	10,175	11,241	12,614	14,203
Other expenses	25,071	25,688	29,534	31,839	35,522
Total expenses	72,915	79,131	86,676	96,171	1,06,836
EBITDA	18,498	20,965	26,246	29,819	34,887
% growth	13.5	13.3	25.2	13.6	17.0
EBITDA margin (%)	20.2	20.9	23.2	23.7	24.6
Other income	1,509	1,769	2,589	2,934	3,016
Interest costs	909	919	1,120	1,065	1,065
Depreciation	3,537	3,423	3,426	3,567	3,762
Profit before tax (before Exceptional items)	15,562	18,393	24,290	28,121	33,075
Exceptional items	(108)	0	0	0	0
Tax	5,440	6,141	8,220	9,675	11,393
PAT	10,014	12,252	16,070	18,446	21,682
Adj. PAT	10,122	12,252	16,070	18,446	21,682
Adj. PAT margin (%)	10.9	12.0	13.9	14.3	15.0
% Growth	77.8	22.4	31.2	14.8	17.5

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 6: Balance sheet

Y/E December (Rsmn)	CY16	CY17	CY18	CY19E	CY20E
Share capital	964	964	964	964	964
Reserves	31,859	33,241	35,773	40,973	44,918
Net worth	32,823	34,206	36,737	41,937	45,883
Total debt	332	351	351	504	567
Deferred tax liability	1,553	1,220	588	1,890	2,126
Total liabilities	54,437	58,699	62,331	70,537	77,770
Gross block	30,951	33,584	35,584	37,584	39,584
Depreciation	3,532	7,051	10,477	14,044	17,806
Impairment	118	372	372	372	372
Net block	27,301	26,162	24,736	23,169	21,407
Capital work-in-progress	1,882	942	1,052	1,200	1,000
Investments	17,557	19,789	26,585	25,828	29,053
Inventories	9,401	9,025	9,656	11,882	11,275
Debtors	979	890	1,246	825	1,505
Cash	8,800	14,574	16,101	20,686	32,868
Loans & advances	810	752	580	992	1,223
Other current assets	669	661	937	882	1,134
Total current assets	32,828	39,374	47,370	51,645	66,428
Creditors	7,992	9,846	12,404	8,567	14,590
Other current liab & prov.	5,138	4,206	4,573	6,299	7,086
Total current liabilities	13,668	14,927	18,550	16,126	23,094
Net current assets	19,161	24,447	28,820	35,519	43,334
Total assets	54,437	58,699	62,331	70,537	77,770

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 5: Cash flow

Y/E December (Rsmn)	CY16	CY17	CY18	CY19E	CY20E
PAT	10,014	12,252	16,070	18,446	21,682
Depreciation	3,537	3,423	3,426	3,567	3,762
Other income	(1,509)	(1,769)	(2,589)	(2,934)	(3,016)
(Inc./dec. in working capital)	(177)	1,610	2,469	(4,357)	6,491
Cash flow from operations	11,864	15,516	19,375	14,722	28,919
Capital expenditure (-)	(2,070)	(2,500)	(2,500)	(2,500)	(2,500)
Net cash after capex	9,794	13,016	16,875	12,222	26,419
Interest paid (-)	909	919	1,120	1,065	1,065
Dividends paid (-)	(5,640)	(8,292)	(10,445)	(11,990)	(14,744)
DDT paid (-)	(1,148)	(1,688)	(2,120)	(2,434)	(2,993)
Inc./(dec.) in investments	(4,259)	(2,232)	(6,796)	757	(3,225)
Cash from financial activities	(3,071)	(7,100)	(11,465)	(11,418)	(14,449)
Opening cash balance	4,996	8,800	14,574	16,101	20,686
Closing cash balance	8,800	14,574	16,101	20,686	32,868
Change in cash balance	3,805	5,774	1,526	4,585	12,182

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 7: Key ratios

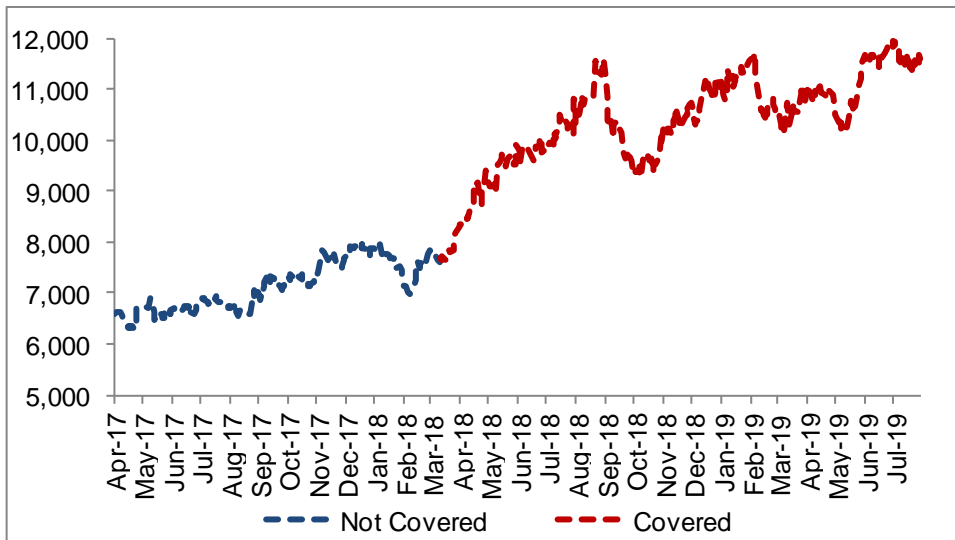
Y/E December (Rsmn)	CY16	CY17	CY18	CY19E	CY20E
Per share (Rs)					
EPS	103.9	127.1	166.7	191.4	224.9
Book value	340.5	354.8	381.1	435.0	476.0
DPS	58.5	86.0	108.4	124.4	152.9
Valuation (x)					
P/Sales	6.4	9.6	8.8	8.7	7.0
EV/sales	6.1	9.3	8.5	8.4	6.7
EV/EBITDA	30.3	44.4	36.7	35.6	27.1
P/E	58.0	78.3	62.1	59.6	46.0
P/BV	17.7	28.1	27.2	26.2	21.7
Return ratios (%)					
RoCE	47.0	51.8	63.7	66.0	70.0
RoE	31.7	36.6	45.3	46.9	49.4
Profitability ratios (%)					
Gross margin	57.5	56.8	59.4	59.0	59.7
EBITDA margin	20.2	20.9	23.2	23.7	24.6
EBIT margin	16.4	17.5	20.2	20.8	22.0
PAT margin	10.8	12.0	13.9	14.3	15.0
Liquidity ratios (%)					
Current ratio	2.4	2.6	2.6	3.2	2.9
Quick ratio	1.7	2.0	2.0	2.5	2.4
Solvency ratio (%)					
Debt- to-equity ratio	0.0	0.0	0.0	0.0	0.0
Turnover ratios					
Total-asset turnover ratio (x)	1.3	1.4	1.4	1.5	1.4
Fixed-asset turnover ratio (x)	3.3	3.8	4.7	5.4	6.6
Inventory days	83	78	74	76	74
Debtor days	4	3	3	3	3
Creditor days	73	75	88	74	74

Source: Company, Nirmal Bang Institutional Equities Research

Rating track

Date	Rating	Market price (Rs)	Target price (Rs)
13 March 2018	Buy	7,619	9,400
11 May 2018	Buy	8,981	10,700
6 August 2018	Buy	10,325	11,900
29 October 2018	Buy	9,569	11,200
19 February 2019	Buy	10,350	12,500
9 April 2019	Buy	10,878	12,500
15 May 2019	Buy	10,470	12,100
5 August 2019	Accumulate	11,411	12,350

Rating track graph



DISCLOSURES

Research Reports that are published by Nirmal Bang Securities Private Limited (hereinafter referred to as “NBSPL”) are for private circulation only. NBSPL is a registered Research Analyst under SEBI (Research Analyst) Regulations, 2014 having Registration no. INH000001766. NBSPL is also a registered Stock Broker with National Stock Exchange of India Limited , BSE Limited ,Metropolitan Stock Exchange of India Limited , Multi Commodity Exchange of India Limited , National Commodity and Derivative Exchange Limited and Indian Commodity Exchange Limited in cash and Equity and Commodities derivatives segments.

NBSPL has other business divisions with independent research teams separated by Chinese walls, and therefore may, at times, have different or contrary views on stocks and markets.

NBSPL or its associates have not been debarred / suspended by SEBI or any other regulatory authority for accessing / dealing in securities Market. NBSPL, its associates or analyst or his relatives do not hold any financial interest (Except Investment) in the subject company. NBSPL or its associates or Analyst do not have any conflict or material conflict of interest at the time of publication of the research report with the subject company. NBSPL or its associates or Analyst or his relatives may or may not hold beneficial ownership of 1% or more in the subject company at the end of the month immediately preceding the date of publication of this research report.

NBSPL or its associates / analyst has not received any compensation / managed or co-managed public offering of securities of the company covered by Analyst during the past twelve months. NBSPL or its associates have not received any compensation or other benefits from the company covered by Analyst or third party in connection with the research report. Analyst has not served as an officer, director or employee of Subject Company. NBSPL / analyst has not been engaged in market making activity of the subject company.

Analyst Certification: I, Ayush Chaturvedi, the research associate and authors of these reports, hereby certify that the views expressed in this research report accurately reflects my/our personal views about the subject securities, issuers, products, sectors or industries. It is also certified that no part of the compensation of the analyst(s) was, is, or will be directly or indirectly related to the inclusion of specific recommendations or views in this research. The analyst(s) principally responsible for the preparation of this research report and has taken reasonable care to achieve and maintain independence and objectivity in making any recommendations.

Disclaimer

Stock Ratings Absolute Returns

BUY > 15%

ACCUMULATE -5% to 15%

SELL < -5%

DISCLAIMER

This report is for the personal information of the authorized recipient and does not constitute to be any investment, legal or taxation advice to you. NBSPL is not soliciting any action based upon it. Nothing in this research shall be construed as a solicitation to buy or sell any security or product, or to engage in or refrain from engaging in any such transaction. In preparing this research, we did not take into account the investment objectives, financial situation and particular needs of the reader.

This research has been prepared for the general use of the clients of NBSPL and must not be copied, either in whole or in part, or distributed or redistributed to any other person in any form. If you are not the intended recipient you must not use or disclose the information in this research in any way. Though disseminated to all the customers simultaneously, not all customers may receive this report at the same time. NBSPL will not treat recipients as customers by virtue of their receiving this report. This report is not directed or intended for distribution to or use by any person or entity resident in a state, country or any jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject NBSPL & its group companies to registration or licensing requirements within such jurisdictions.

The report is based on the information obtained from sources believed to be reliable, but we do not make any representation or warranty that it is accurate, complete or up-to-date and it should not be relied upon as such. We accept no obligation to correct or update the information or opinions in it. NBSPL or any of its affiliates or employees shall not be in any way responsible for any loss or damage that may arise to any person from any inadvertent error in the information contained in this report. NBSPL or any of its affiliates or employees do not provide, at any time, any express or implied warranty of any kind, regarding any matter pertaining to this report, including without limitation the implied warranties of merchantability, fitness for a particular purpose, and non-infringement. The recipients of this report should rely on their own investigations.

This information is subject to change without any prior notice. NBSPL reserves its absolute discretion and right to make or refrain from making modifications and alterations to this statement from time to time. Nevertheless, NBSPL is committed to providing independent and transparent recommendations to its clients, and would be happy to provide information in response to specific client queries.

Before making an investment decision on the basis of this research, the reader needs to consider, with or without the assistance of an adviser, whether the advice is appropriate in light of their particular investment needs, objectives and financial circumstances. There are risks involved in securities trading. The price of securities can and does fluctuate, and an individual security may even become valueless. International investors are reminded of the additional risks inherent in international investments, such as currency fluctuations and international stock market or economic conditions, which may adversely affect the value of the investment. Opinions expressed are subject to change without any notice. Neither the company nor the director or the employees of NBSPL accept any liability whatsoever for any direct, indirect, consequential or other loss arising from any use of this research and/or further communication in relation to this research. Here it may be noted that neither NBSPL, nor its directors, employees, agents or representatives shall be liable for any damages whether direct or indirect, incidental, special or consequential including lost revenue or lost profit that may arise from or in connection with the use of the information contained in this report.

Copyright of this document vests exclusively with NBEPL.

Our reports are also available on our website www.nirmalbang.com

Access all our reports on Bloomberg, Thomson Reuters and Factset.

Team Details:			
Name		Email Id	Direct Line
Rahul Arora	CEO	rahul.arora@nirmalbang.com	-
Girish Pai	Head of Research	girish.pai@nirmalbang.com	+91 22 6273 8017 / 18
Dealing			
Ravi Jagtiani	Dealing Desk	ravi.jagtiani@nirmalbang.com	+91 22 6273 8230, +91 22 6636 8833
Pradeep Kasat	Dealing Desk	pradeep.kasat@nirmalbang.com	+91 22 6273 8100/8101, +91 22 6636 8831
Michael Pillai	Dealing Desk	michael.pillai@nirmalbang.com	+91 22 6273 8102/8103, +91 22 6636 8830

Nirmal Bang Equities Pvt. Ltd.

Correspondence Address

B-2, 301/302, Marathon Innova,
 Nr. Peninsula Corporate Park,
 Lower Parel (W), Mumbai-400013.

Board No. : 91 22 6273 8000/1; Fax. : 022 6273 8010