

# Nestle India

11 November 2019

Reuters: NEST.BO; Bloomberg: NEST IN

## Momentum sustained

Nestle India (NEST) continued to deliver strong topline growth in 3QCY19 as well. Revenue grew by 9.4% YoY to Rs. 32.2bn (vs our est. 7% growth to Rs. 31.5bn). Domestic sales grew by 10.5% YoY to Rs. 30.4bn, driven largely by volume and mix. Maggi, Kitkat, Nestle Munch, Nescafe RTD, Nangrow and Ceregrow delivered strong performances. The overall performance was to some extent pulled down by exports, which were down by 7.1% YoY to Rs. 1.6bn on account of lower coffee exports to Turkey. Overall EBITDA grew by 2.4% YoY to Rs. 7.6bn (vs our est. 4.9% growth to Rs. 7.8bn). Adj. PAT grew by 30.4% to Rs. 6bn (vs our est. 18.4% growth to Rs. 5.5bn) as tax rate came in at 14.8% vs our estimate of 25.2%. Other income decreased (down 15.9% YoY) due to lower average liquidities following the payment of special interim dividend and lower yields. Gross margin contracted 220bps YoY to 57.6% due to higher commodity prices, particularly in milk and its derivatives, which is expected to continue in the near term. EBITDA margin contracted 160bps YoY to 23.6% (vs our est. 24.7%) as other expenses as a % of sales were down 70bps YoY. We expect the company to continue to roll out innovative products by leveraging its strong R&D, sourcing and supply chain capabilities. Considering the fact that the company continues to maintain its launch pipeline, we are fairly confident that it will be able to sustain healthy earnings growth (16-18% over the next two years) driven by volume. We feel the valuation is fair, the stock trades at ~58x FY21E EPS. We thus maintain Accumulate rating with a target price (TP) of Rs14,600 (Rs14,520 earlier), based on an unchanged P/E multiple of 52x Sep'21 EPS.

**Healthy growth in domestic sales:** NEST's domestic sales growth for the quarter was above our estimate. However, export sales remained weak on account of reduced exports to markets such as Turkey, which dragged down the overall performance. Continuing with its new launch strategy for the domestic business, during the quarter the company brought back Milo (a cocoa-malt beverage) to the India market.

**9MCY19 performance:** Sales, EBITDA and Adj. PAT grew 9.8%, 4.6% and 15.9%, respectively. Gross margin was down 140bps YoY to 57.6% while EBITDA margin contracted by 120bps to 24%.

**Change in management:** Board of Directors has appointed Mr. David McDaniel as Whole-time Director, designated as 'Executive Director - Finance & Control and Chief Financial Officer' with effect from 1st March, 2020, for a term of five years in place of Mr. Shobinder Duggal, who will continue as the CFO till 29th February, 2020.

**Outlook and valuation:** There are minor changes to our CY19/CY20/CY21 EPS. NEST continues to deliver strong domestic topline growth. We believe it can easily deliver 16-18% earnings growth over the next two years driven by volume and mix led topline growth. The stock has run-up quite well and now trades at ~58x FY21E EPS. We thus maintain Accumulate rating with a target price (TP) of Rs14,600 (Rs14,475 earlier), based on an unchanged P/E multiple of 52x Sep'21 EPS.

## ACCUMULATE

**Sector:** FMCG

**CMP:** Rs14,471

**Target Price:** Rs14,600

**Upside:** 1%

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### Key Data

Current Shares O/S (mn)	96.4
Mkt Cap (Rsbn/US\$bn)	1,397.1/19.6
52 Wk H / L (Rs)	15,150/9,875
Daily Vol. (3M NSE Avg.)	103,928

### Price Performance (%)

	1 M	6 M	1 Yr
Nestle India	6.5	42.9	44.0
Nifty Index	7.0	4.8	12.4

Source: Bloomberg

Y/E Dec. (Rsmn)	3QCY18	2QCY19	3QCY19	YoY (%)	QoQ (%)	9MCY18	9MCY19	YoY (%)
<b>Net Sales</b>	<b>29,394</b>	<b>30,009</b>	<b>32,158</b>	<b>9.4</b>	<b>7.2</b>	<b>83,950</b>	<b>92,196</b>	<b>9.8</b>
COGS	11,841	12,522	13,650	15.3	9.0	34,008	38,625	13.6
% of sales	40.3	41.7	42.4	220bps	70bps	40.5	41.9	140bps
<b>Gross margin %</b>	<b>59.7</b>	<b>58.3</b>	<b>57.6</b>	<b>(220bps)</b>	<b>(70bps)</b>	<b>59.5</b>	<b>58.1</b>	<b>(140bps)</b>
Employee costs	2,904	3,146	3,220	10.9	2.4	8,443	9,403	11.4
% of sales	9.9	10.5	10.0	10bps	(50bps)	10.1	10.2	10bps
Other expenses	7,228	7,269	7,693	6.4	5.8	20,313	22,006	8.3
% of sales	24.6	24.2	23.9	(70bps)	(30bps)	24.2	23.9	(30bps)
<b>EBITDA</b>	<b>7,420</b>	<b>7,073</b>	<b>7,595</b>	<b>2.4</b>	<b>7.4</b>	<b>21,187</b>	<b>22,162</b>	<b>4.6</b>
<b>EBITDA margin %</b>	<b>25.2</b>	<b>23.6</b>	<b>23.6</b>	<b>(160bps)</b>	<b>0.0</b>	<b>25.2</b>	<b>24.0</b>	<b>(120bps)</b>
Depreciation	930	808	780	(16.1)	(3.5)	2,573	2,368	(8.0)
EBIT	6,490	6,264	6,815	5.0	8.8	18,614	19,794	6.3
<b>EBIT margin %</b>	<b>22.1</b>	<b>20.9</b>	<b>21.2</b>	<b>(90bps)</b>	<b>30bps</b>	<b>22.2</b>	<b>21.5</b>	<b>(70bps)</b>
Interest expense	275	299	299	9.0	0.0	868	915	5.4
Other income	670	726	564	(15.9)	(22.3)	1,837	2,022	10.1
Exceptional items	-	-	-	0.0	0.0	-	-	-
PBT	6,886	6,691	7,080	2.8	5.8	19,583	20,902	6.7
Tax	2,257	2,213	1,045	(53.7)	(52.8)	6,416	5,638	(12.1)
<b>Effective tax rate %</b>	<b>32.8</b>	<b>33.1</b>	<b>14.8</b>	<b>(18.0)</b>	<b>(18.3)</b>	<b>32.8</b>	<b>27.0</b>	<b>(5.8)</b>
<b>Adj. PAT</b>	<b>4,629</b>	<b>4,478</b>	<b>6,035</b>	<b>30.4</b>	<b>34.8</b>	<b>13,168</b>	<b>15,263</b>	<b>15.9</b>
<b>Adj. PAT margin %</b>	<b>15.4</b>	<b>14.6</b>	<b>18.4</b>	<b>300bps</b>	<b>390bps</b>	<b>15.3</b>	<b>16.2</b>	<b>90bps</b>

Source: Company, Nirmal Bang Institutional Equities Research

## Exhibit 1: Financial summary

Y/E Dec. (Rsmn)	CY17	CY18	CY19E	CY20E	CY21E
Net revenues	1,00,096	1,12,923	1,24,202	1,40,091	1,57,644
YoY growth (%)	9.5	12.8	10.0	12.8	12.5
EBITDA	22,214	27,324	29,536	33,958	38,923
EBITDA margin (%)	22.2	24.2	23.8	24.2	24.7
PAT	13,500	17,217	20,707	24,217	28,026
EPS (Rs)	140.0	178.6	214.8	251.2	290.7
YoY growth (%)	13.2	27.5	20.3	17.0	15.7
RoCE (%)	41.7	50.2	72.7	105.0	110.8
RoE (%)	40.3	48.5	70.5	102.3	108.0
P/E (x)	103.4	81.1	67.4	57.6	49.8
P/BV (x)	40.8	38.0	63.3	55.2	52.5
EV/EBITDA (x)	61.3	49.5	46.2	40.0	34.7

Source: Company, Nirmal Bang Institutional Equities Research

## Exhibit 2: Our estimates versus actual performance

Y/E Dec. (Rsmn)	3QCY18	2QCY19	3QCY19	YoY (%)	QoQ (%)	NBIE estimate	Variation (%)
Net sales	29,394	30,009	32,158	9.4	7.2	31,451	2.2
EBITDA	7,420	7,073	7,595	2.4	7.4	7,782	-2.4
EBITDA margin (%)	25.2	23.6	23.6	(70 bps)	(130 bps)	24.7	(100 bps)
Net income	4,629	4,478	6,035	30.4	34.8	5,481	10.1

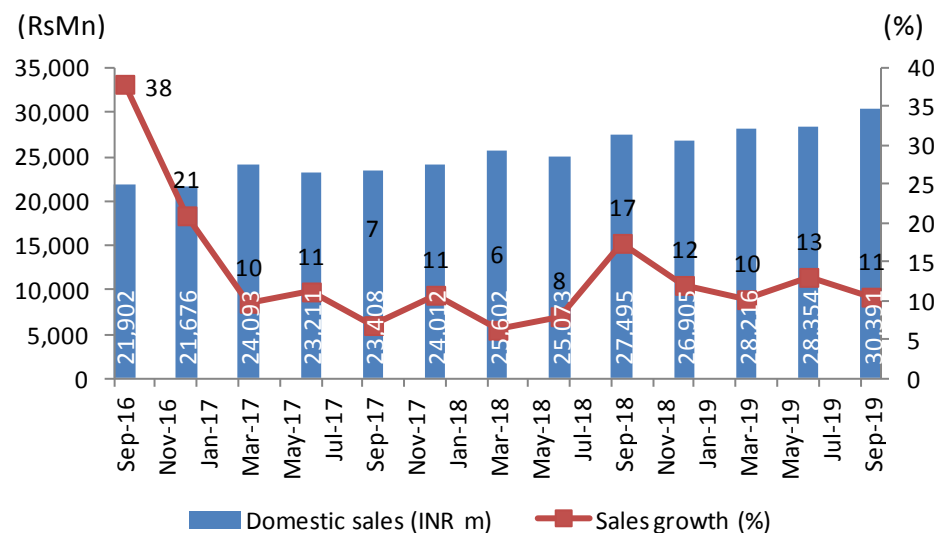
Source: Company, Nirmal Bang Institutional Equities Research

## Exhibit 3: Change in our estimates

Y/E Dec. (Rsmn)	Old estimate			New estimate			Change (%)		
	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E
Net sales	123602	139476	156959	1,24,202	1,40,091	1,57,644	0.5	0.4	0.4
EBITDA	29,579	33,782	38,723	29,536	33,958	38,923	-0.1	0.5	0.5
EBITDA (%)	23.9	24.2	24.7	23.8	24.2	24.7	(10bps)	0.0	0.0
Adj. PAT	20,939	24,094	27,872	20,707	24,217	28,026	-1.1	0.5	0.5

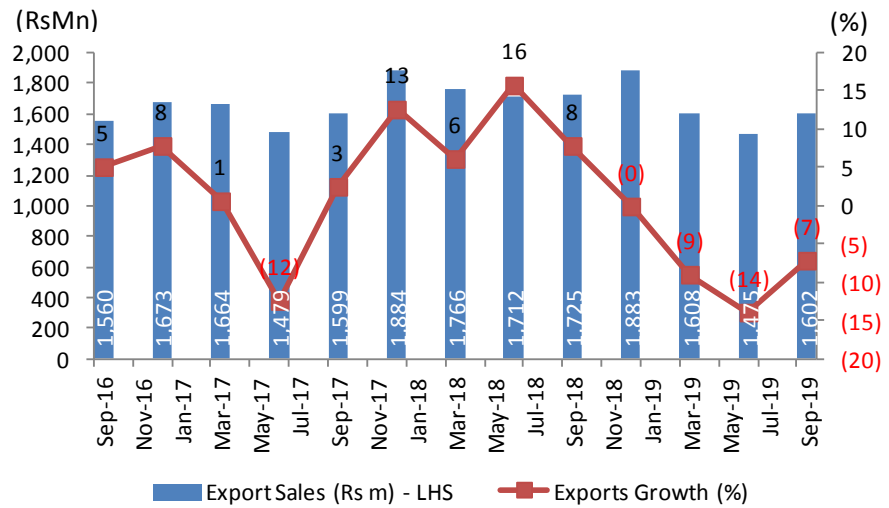
Source: Company, Nirmal Bang Institutional Equities Research

## Exhibit 4: Domestic sales growth trend



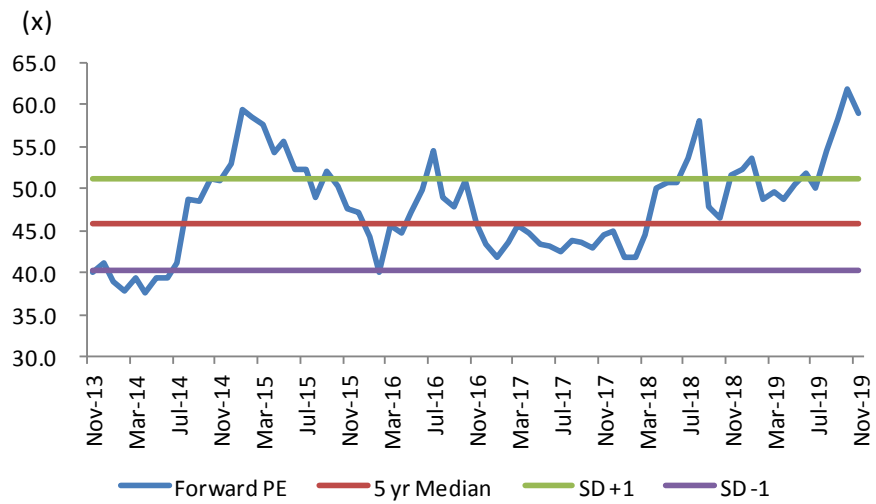
Source: Company, Nirmal Bag Institutional Equities Research

**Exhibit 5: Export sales growth trend**



Source: Company, Nirmal Bang Institutional Equities Research

**Exhibit 6: One year forward P/E**



Source: Company, Nirmal Bang Institutional Equities Research

## Financials (standalone)

### Exhibit 7: Income statement

Y/E December (Rsmn)	CY17	CY18	CY19E	CY20E	CY21E
Net sales	1,00,096	1,12,923	1,24,202	1,40,091	1,57,644
<b>% Growth</b>	<b>9.5</b>	<b>12.8</b>	<b>10.0</b>	<b>12.8</b>	<b>12.5</b>
COGS	43,269	45,902	52,219	58,142	64,983
Staff costs	10,577	11,732	12,595	14,760	16,924
Other expenses	24,037	27,965	29,851	33,231	36,814
Total expenses	77,882	85,599	94,666	1,06,133	1,18,721
EBITDA	22,214	27,324	29,536	33,958	38,923
<b>% growth</b>	<b>9.4</b>	<b>23.0</b>	<b>8.1</b>	<b>15.0</b>	<b>14.6</b>
<b>EBITDA margin (%)</b>	<b>22.2</b>	<b>24.2</b>	<b>23.8</b>	<b>24.2</b>	<b>24.7</b>
Other income	1,769	2,589	2,690	3,549	4,216
Interest costs	919	1,120	1,220	1,342	1,477
Depreciation	3,423	3,357	3,334	3,802	4,210
Profit before tax (before Exceptional items)	19,641	25,437	27,672	32,362	37,452
Exceptional items	-1,248	-1,148	-702	-702	-702
Tax	6,141	8,220	6,965	8,146	9,427
PAT	12,252	16,069	20,005	23,515	27,324
Adj. PAT	13,500	17,217	20,707	24,217	28,026
<b>Adj. PAT margin (%)</b>	<b>13.3</b>	<b>14.9</b>	<b>16.3</b>	<b>16.9</b>	<b>17.3</b>
<b>% Growth</b>	<b>22.4</b>	<b>31.2</b>	<b>14.8</b>	<b>17.5</b>	<b>12.8</b>

Source: Company, Nirmal Bang Institutional Equities Research

### Exhibit 9: Balance sheet

Y/E December (Rsmn)	CY17	CY18	CY19E	CY20E	CY21E
Share capital	964	964	964	964	964
Reserves	33,242	35,773	21,067	24,334	25,624
Net worth	34,206	36,737	22,031	25,298	26,588
Total debt	351	351	351	351	351
Deferred tax liability	1,220	588	588	588	588
<b>Total liabilities</b>	<b>35,777</b>	<b>37,677</b>	<b>22,971</b>	<b>26,238</b>	<b>27,528</b>
Gross block	33,584	34,854	36,854	42,354	45,354
Depreciation	7,423	10,848	14,182	17,984	22,194
Net block	26,162	24,006	22,672	24,370	23,160
Capital work-in-progress	942	1,052	1,052	1,052	1,052
Investments	19,789	26,585	28,510	30,628	32,957
Inventories	9,025	9,656	10,867	12,110	13,512
Debtors	890	1,246	1,015	1,144	1,288
Cash	14,574	16,101	4,288	8,292	13,276
Loans & advances	2,245	2,236	2,965	3,379	3,847
Total current assets	26,734	29,238	19,135	24,926	31,923
Creditors	9,846	12,404	13,877	15,770	17,625
Other current liabilities & -----	28,002	30,800	34,520	38,967	43,938
Total current liabilities	37,849	43,204	48,398	54,737	61,564
Net current assets	-11,115	-13,966	-29,263	-29,812	-29,641
<b>Total assets</b>	<b>35,777</b>	<b>37,677</b>	<b>22,970</b>	<b>26,238</b>	<b>27,528</b>

Source: Company, Nirmal Bang Institutional Equities Research

### Exhibit 8: Cash flow

Y/E December (Rsmn)	CY17	CY18	CY19E	CY20E	CY21E
PAT	18,393	24,290	26,202	30,156	34,713
Depreciation	3,423	3,357	3,334	3,802	4,210
Other income	1,353	2,477	2,690	3,549	4,216
(Inc./dec. in working capital	3,750	4,128	3,485	4,553	4,813
<b>Cash flow from operations</b>	<b>18,178</b>	<b>20,525</b>	<b>24,586</b>	<b>28,159</b>	<b>31,569</b>
Capital expenditure (-)	639	-2,592	3,458	5,054	6,253
<b>Net cash after capex</b>	<b>18,817</b>	<b>17,932</b>	<b>28,044</b>	<b>33,212</b>	<b>37,822</b>
Interest paid (-)	7	41	1,220	1,342	1,477
Dividends paid (-)	-8,292	-10,895	-34,711	-20,248	-26,033
Inc./(dec.) in investments	-1,118	-1,604	-1,925	-2,118	-2,329
<b>Cash from financial activities</b>	<b>-9,966</b>	<b>-13,174</b>	<b>-35,931</b>	<b>-21,590</b>	<b>-27,510</b>
Opening cash balance	8,800	14,574	16,101	4,288	8,292
Closing cash balance	14,574	16,101	20,686	32,868	36,970
Change in cash balance	5,774	1,526	4,585	28,580	28,677

Source: Company, Nirmal Bang Institutional Equities Research

### Exhibit 10: Key ratios

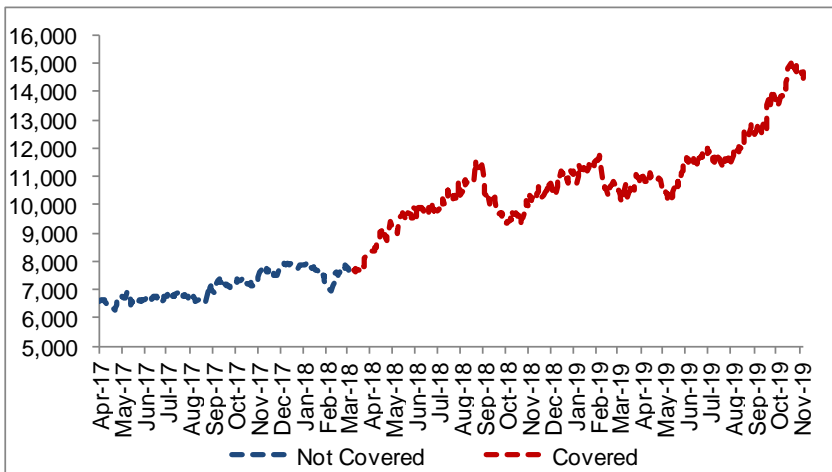
Y/E December	CY17	CY18	CY19E	CY20E	CY21E
<b>Per share (Rs)</b>					
EPS	140.0	178.6	214.8	251.2	290.7
Book value	354.8	381.0	228.5	262.4	275.8
DPS	86.0	113.0	300.0	175.0	225.0
<b>Valuation (x)</b>					
EV/sales	13.6	12.0	11.0	9.7	8.6
EV/EBITDA	61.3	49.5	46.2	40.0	34.7
P/E	103.4	81.1	67.4	57.6	49.8
P/BV	40.8	38.0	63.3	55.2	52.5
<b>Return ratios (%)</b>					
RoCE	41.7	50.2	72.7	105.0	110.8
RoE	40.3	48.5	70.5	102.3	108.0
<b>Profitability ratios (%)</b>					
Gross margin	56.8	59.4	58.0	58.5	58.8
EBITDA margin	22.2	24.2	23.8	24.2	24.7
EBIT margin	18.8	21.2	21.1	21.5	22.0
PAT margin	13.3	14.9	16.3	16.9	17.3
<b>Liquidity ratios (%)</b>					
Current ratio	0.7	0.7	0.4	0.5	0.5
Quick ratio	0.5	0.5	0.2	0.2	0.3
<b>Solvency ratio (%)</b>					
Debt to Equity ratio	0.0	0.0	0.0	0.0	0.0
<b>Turnover ratios</b>					
Total asset turnover ratio (x)	2.8	3.1	4.1	5.7	5.9
Fixed asset turnover ratio (x)	3.8	4.7	5.5	5.7	6.8
Inventory days	76	77	76	76	76
Debtors days	3	4	3	3	3
Creditor days	83	99	97	99	99

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
23 September 2019	Accumulate	13,502	14,650
9 October 2019	Accumulate	13,600	14,520
11 November 2019	Accumulate	14,471	14,600

**Rating track graph**



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BUY > 15%

ACCUMULATE -5% to 15%

SELL < -5%

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