



TM

SYSTEMATIX INSTITUTIONAL EQUITIES

Systematix

Institutional Equities

16 February 2023

## Nestlé India

## Volume weakness offset by unexpected margin improvement

## RESULT UPDATE

Sector: FMCG Rating: BUY  
CMP: Rs 19,385 Target Price: Rs 22,515

## Stock Info

Sensex/Nifty	61,320/ 18,036
Bloomberg	NEST IN
Equity shares (mn)	96.42
52-wk High/Low	Rs21053/16000
Face value	Rs 10
M-Cap	Rs1891bn/\$23bn
3-m Avg volume	US\$ 15.3mn

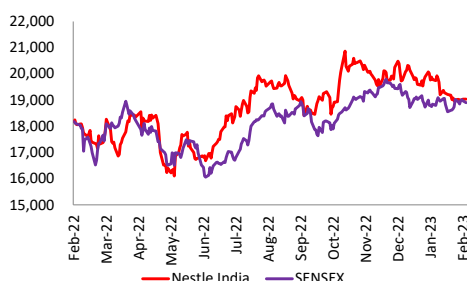
## Financial Snapshot (Rs mn)

Y/E Mar	CY22	CY23E	CY24E
Sales	168,970	189,230	213,384
PAT	23,905	29,362	35,015
EPS (Rs)	247.9	304.5	363.1
PE (x)	79.1	64.4	54.0
EV/EBITDA (x)	50.7	42.0	35.7
P/BV (x)	76.9	64.0	51.8
EV/Sales	11.1	9.9	8.8
RoE (%)	105.2	108.4	106.0
RoCE (%)	147.9	149.1	145.5
NWC (days)	4	-2	-2
Net gearing (x)	(0.4)	(0.4)	(0.2)

## Shareholding Pattern (%)

	Dec 22	Sept 22	Jun 22
Promoter	62.8	62.8	62.8
-Pledged	-	-	-
FII	12.1	12.1	11.7
DII	9.0	8.9	9.1
Others	16.1	16.3	16.5

## Stock Performance (1-year)



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Nestlé India (NEST IN) had a mixed quarter with a muted volume performance offset by an unexpected improvement in margins. Revenue growth at 13.6% fell short of expectations mainly given pressure on Maggi LUP volumes and some slowdown in mega cities and Tier 2-6 markets. While volumes declined 1% YoY, mix contributed ~4% and pricing ~10% in our view. Growth continued to be driven by *Nescafe*, *Milkmaid*, *Kitkat*, *Munch* and mass and premium variants of *Maggi*. Gross margins were down 206bps to 54.9% given sharp inflation in milk, cereals and grains. However, EBITDA margins improved 30bps led by savings of 80bps in employee expenses and 150bps in other expenses given lower marketing spends (given lower spends on new products and focus on core brands) and cost control measures (150bps savings in CY22). Growth saw a boost from e-commerce acceleration (+41% in CY22), recovery in Out of Home channel (+39%) and opening up of exports in new categories (+8%). Other key highlights were the consolidation of petcare business, continued distribution ramp-up in rural markets and focus on the millets opportunity.

We expect NEST's continued dominance in its core categories, diversified portfolio and aggressive innovation initiatives backed by the global parent to drive penetration-led growth. The new-found focus on rural markets and success in emerging distribution channels should also support growth. Margins should also start improving once inflation subsides and new premium products start scaling up, in addition to benefits of operating leverage. We have built in revenue/PAT CAGR of 12.4%/21% over CY22-24E for the company, and value NEST at a target P/E of 62x (in line with its 5-year average) on our CY24E EPS, yielding a TP of Rs 22,515. We maintain our BUY rating and expect the stock to outperform large FMCG peers on both growth and margin fronts.

**Broad-based 13.8% growth in the domestic business:** NEST's overall revenue grew 13.6% YoY (13.8% domestic sales growth) in 4QCY22, which is a combination of flattish volumes, 4% mix and 10% pricing benefit in our view. Volumes were impacted mainly on account of the 40% price hike in *Maggi* LUP and price hikes in the dairy segment. Mix got better given uptrading to larger and premium packs in *Maggi* and strong growth in coffee and chocolates. Key highlights were continued growth in General Trade channel, e-commerce (41% growth in CY22 now contributing 6.5% to sales) and Out of Home channels (39% YoY growth in CY22), which saw accelerated growth. All key brands Milkmaid, Maggi, Nescafe and Kit Kat delivered strong growth. New products contributed 5.4% to domestic sales; Export sales increased by 17.1% YoY in 4Q. After sharp price hikes this year, we expect pricing/mix contribution to come down to 3% and volume CAGR to increase to about 9% in CY23 and CY24, driving a 12.4% revenue CAGR over CY22-24E. Stronger growth is expected from the prepared dishes and confectionary segments which are the priority segments for the ongoing Rs 50bn expansion plan over CY23-25.

**RM inflation continues to impact margins:** Gross margin declined 206bps YoY to 54.9%, given the sharp inflation in milk, cereals and grains, which have resulted in a 18.5% commodity inflation for the company against an average of 3%, which the company has offset via calibrated price hikes, mix improvement and very aggressive cost saving initiatives. Eight out of the thirteen key commodity prices still remain at 10-year highs which have now started showing some signs of cooling-off but remain at elevated levels. Given the pricing actions taken by the company and continued premiumization across the portfolio, gross margins are expected to improve from CY22 levels, which should help restore EBITDA margins to normalized levels of ~24% helped by further cost savings under project SHARK.

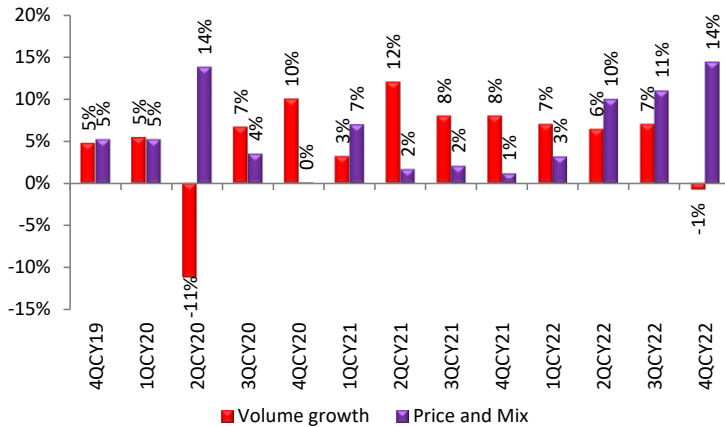
**Segmental growth drivers:** Growth in prepared dishes was driven by higher media and distribution spends in *Maggi*, milk products by *Milkmaid*, beverages by *Nescafe Classic and Sunrise*, while media spends, festive promotions and focused execution drove growth in the confectionery segment. Management focus will be on increasing penetration and traction in core products along with launch of new products including a few in the millets space.

**Sector-leading growth prospects warrant maintaining BUY rating:** We see this quarter as a one-off where volume growth came under pressure and marketing spends declined, on account of sharp price hikes impacting volumes and a slight pause on the new product push agenda. We remain confident on the management's commitment and execution on its agendas of penetration-led growth, innovation and premiumisation, supported by aggressive marketing spends. The ongoing Rs 50bn capex programme over three years also gives confidence that the global parent sees India as a priority market and would continue to provide both financial and technical support to drive industry-leading growth here. We have built in revenue/EPS CAGR of 12.4%/21% over CY22-24E, and believe the company would continue to generate robust FCF; liberal dividend payouts would help sustain the high return ratios and premium valuation multiples.

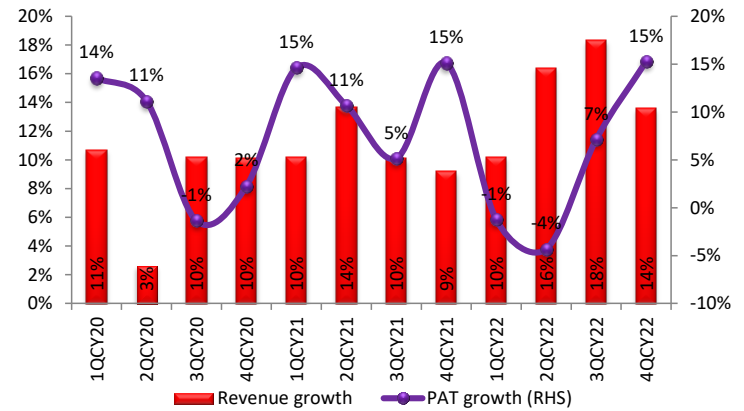
#### Exhibit 1: 4QCY22 quarterly performance snapshot

YE March (Rs mn)	Q4CY22	Q4CY21	Q3CY22	YoY (%)	QoQ (%)
<b>Net Revenues</b>	<b>42,568</b>	<b>37,480</b>	<b>46,018</b>	<b>13.6</b>	<b>(7.5)</b>
Raw material cost	19,215	16,146	21,777	19.0	(11.8)
(% of sales)	45.1	43.1	47.3		
Gross profit	23,353	21,334	24,241	9.5	(3.7)
<b>(% of sales)</b>	<b>54.9</b>	<b>56.9</b>	<b>52.7</b>		
Employee cost	4,070	3,889	4,200	4.6	(3.1)
(% of sales)	9.6	10.4	9.1		
Others	9,419	8,858	10,000	6.3	(5.8)
(% of sales)	22.1	23.6	21.7		
<b>EBITDA</b>	<b>9,864</b>	<b>8,587</b>	<b>10,041</b>	<b>14.9</b>	<b>(1.8)</b>
<b>EBITDA margin (%)</b>	<b>23.2</b>	<b>22.9</b>	<b>21.8</b>		
Other income	296	274	306	8.0	(3.6)
<b>PBIDT</b>	<b>10,160</b>	<b>8,860</b>	<b>10,347</b>	<b>14.7</b>	<b>(1.8)</b>
Depreciation	987	1,060	982	(6.9)	0.5
Interest	448	436	372	2.8	20.5
<b>PBT</b>	<b>8,725</b>	<b>7,365</b>	<b>8,994</b>	<b>18.5</b>	<b>(3.0)</b>
Tax	2,310	1,801	2,379	28.3	(2.9)
ETR (%)	26.5	24.5	26.5		
<b>Adjusted PAT</b>	<b>6,415</b>	<b>5,564</b>	<b>6,615</b>	<b>15.3</b>	<b>(3.0)</b>
PATAMI margin	15.1	14.8	14.4		
Extraordinary income/ (exp.)	134	1,769	0		
<b>Reported PAT</b>	<b>6,281</b>	<b>3,795</b>	<b>6,615</b>	<b>65.5</b>	<b>(5.1)</b>
<b>Adj EPS (Rs)</b>	<b>66.5</b>	<b>57.7</b>	<b>68.6</b>		

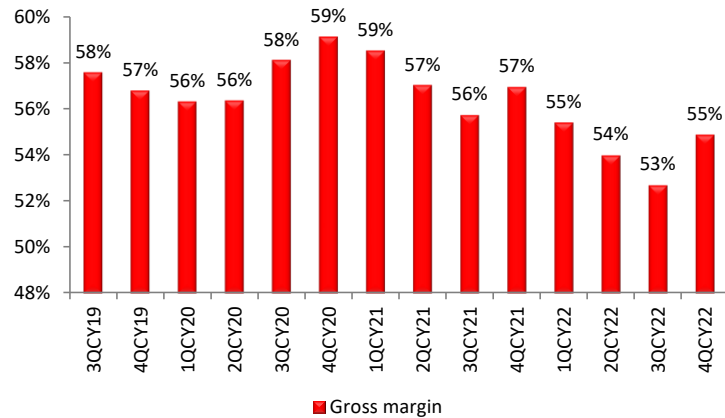
Source: Company, Systematix Institutional Research

**Exhibit 2: Muted volumes saw a decline of ~1% YoY**

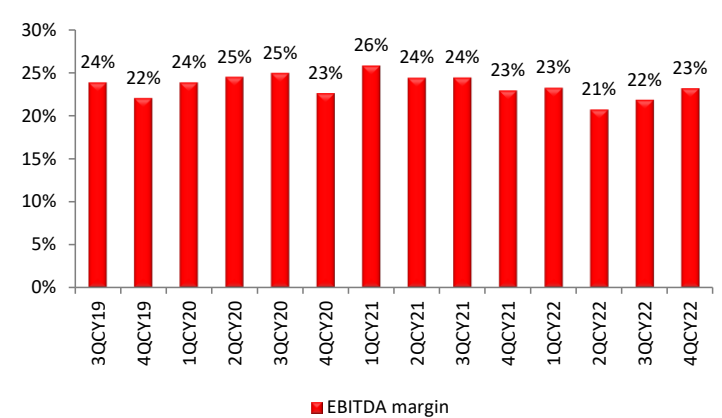
Source: Company, Systematix Institutional Research

**Exhibit 3: PAT grew 15% YoY led by double-digit revenue growth**

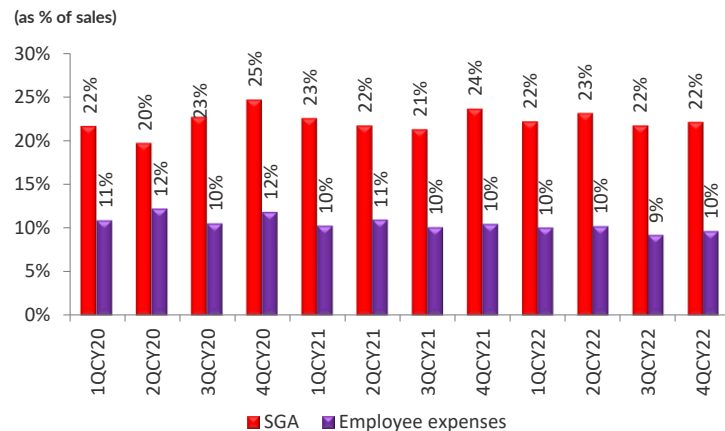
Source: Company, Systematix Institutional Research

**Exhibit 4: Gross margin contracted 206bps YoY**

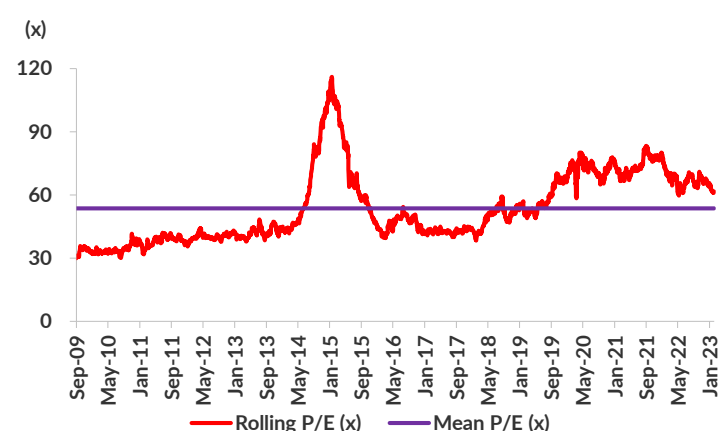
Source: Company, Systematix Institutional Research

**Exhibit 5: EBITDA margin up 26bps YoY**

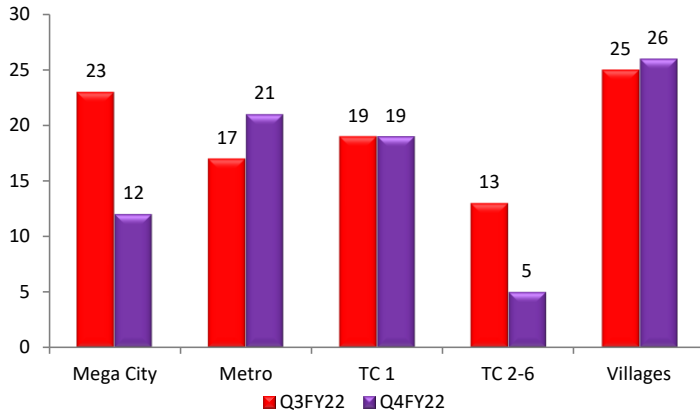
Source: Company, Systematix Institutional Research

**Exhibit 6: SGA expenses declined 150bps YoY**

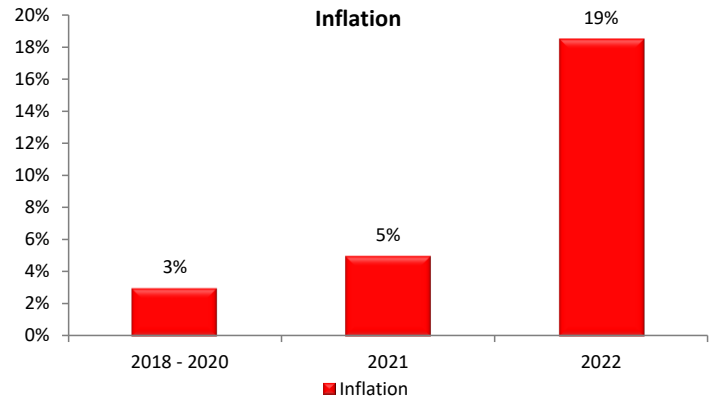
Source: Company, Systematix Institutional Research

**Exhibit 7: The stock currently trades at 62x one-yr fwd earnings**

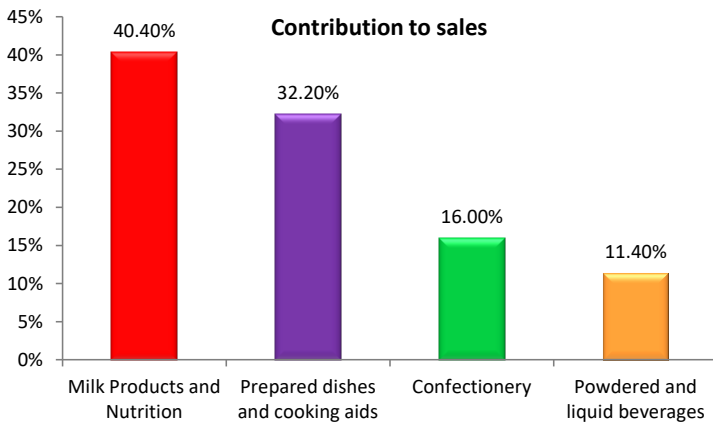
Source: Company, Systematix Institutional Research

**Exhibit 8: Some slowdown in mega cities and Tier 2-6 markets**

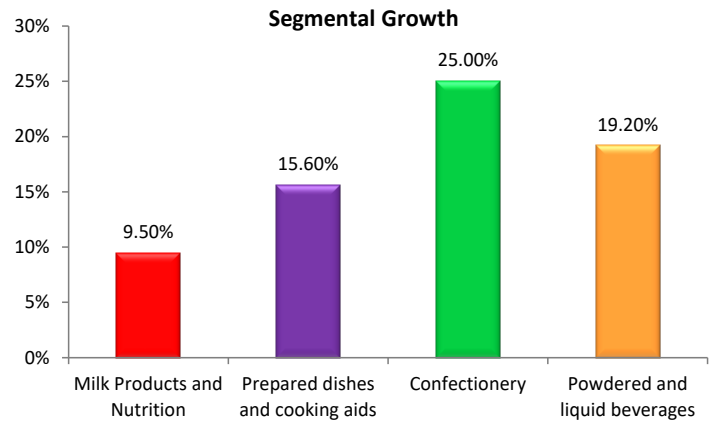
Source: Company, Systematix Institutional Research

**Exhibit 9: Commodity headwinds – Inflation 6x of normal in 2022**

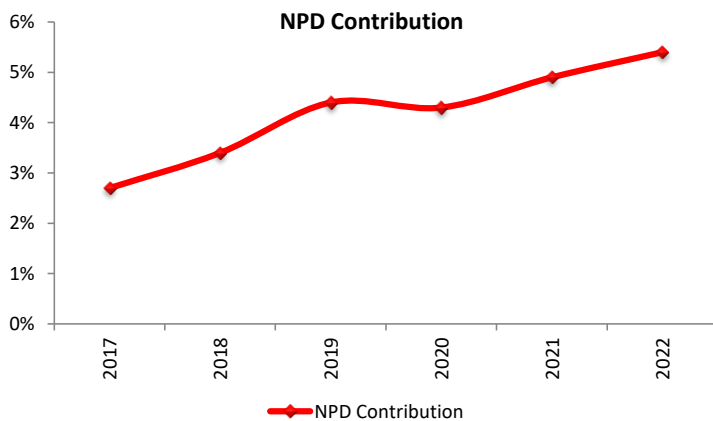
Source: Company, Systematix Institutional Research

**Exhibit 10: Milk based and prepared dishes share more than 70%**

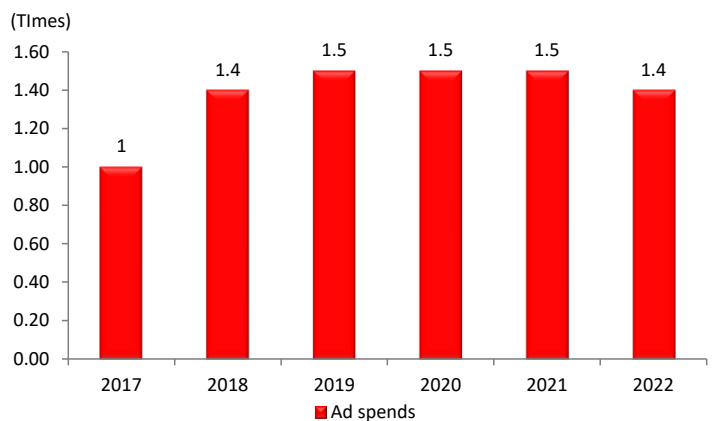
Source: Company, Systematix Institutional Research

**Exhibit 11: Strong double-digit growth in confectionery and powered liquid beverages**

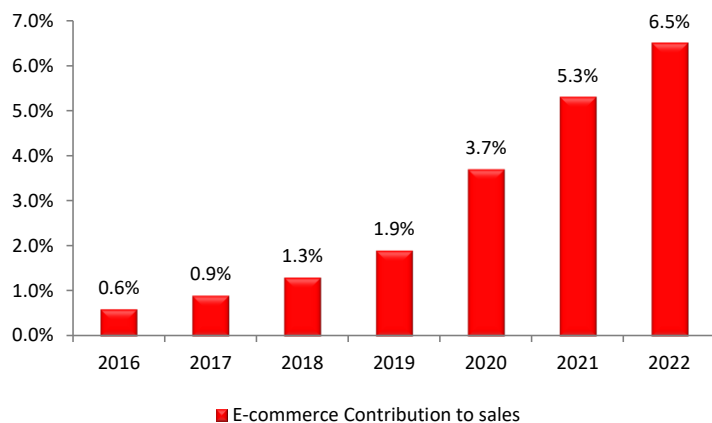
Source: Company, Systematix Institutional Research

**Exhibit 12: New products contributed 5.4% to sales**

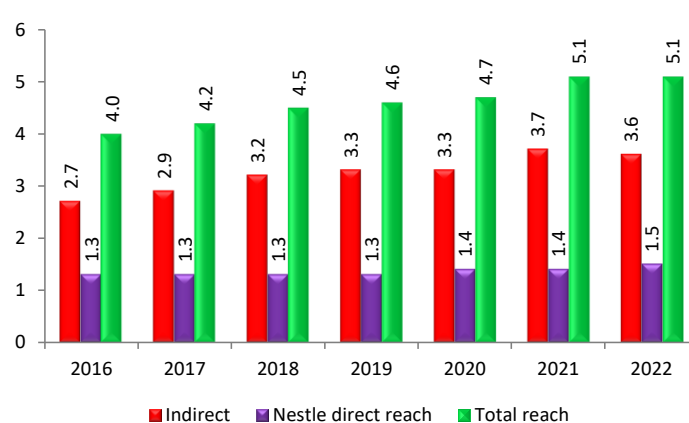
Source: Company, Systematix Institutional Research

**Exhibit 13: Ad spends came down given focus on core brands**

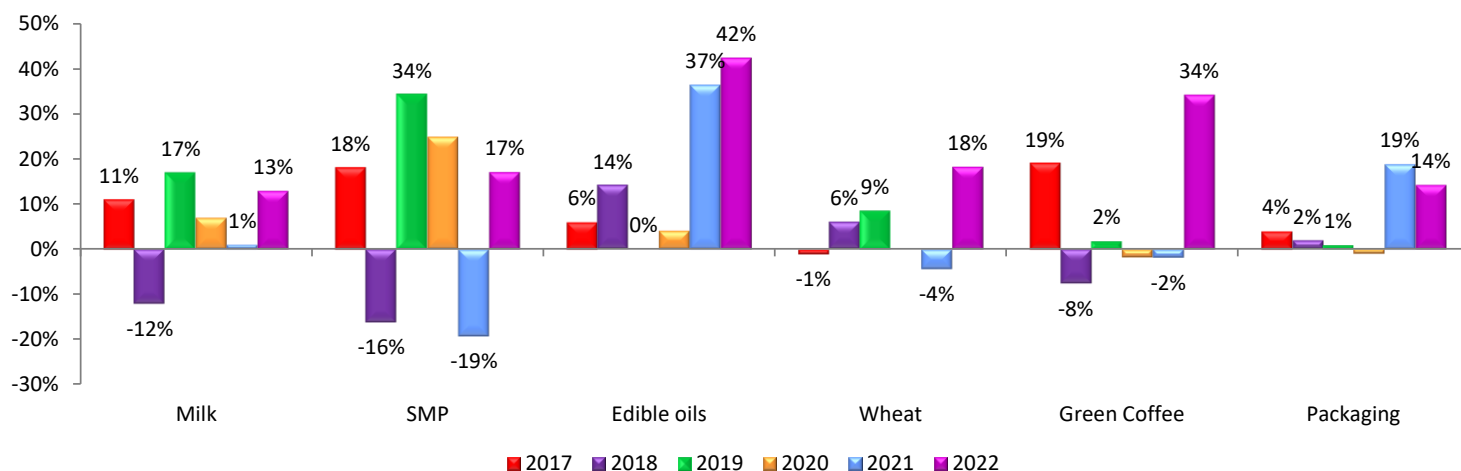
Source: Company, Systematix Institutional Research

**Exhibit 14: E-commerce contribution increased to 6.5%**

Source: Company, Systematix Institutional Research

**Exhibit 15: Distribution stable while direct reach increased (mn)**

Source: Company, Systematix Institutional Research

**Exhibit 16: Increase in commodities price**

Source: Company, Systematix Institutional Research

## FINANCIALS

## Profit &amp; Loss Statement

YE: Mar (Rs mn)	CY20	CY21	CY22	CY23E	CY24E
<b>Revenue</b>	<b>1,33,500</b>	<b>1,47,094</b>	<b>1,68,970</b>	<b>1,89,230</b>	<b>2,13,384</b>
Gross profit	76,761	83,905	91,471	1,06,089	1,21,509
GP margin (%)	57.5%	57.0%	54.1%	56.1%	56.9%
<b>Operating profit</b>	<b>32,015</b>	<b>35,915</b>	<b>37,126</b>	<b>44,778</b>	<b>52,800</b>
OP margin (%)	24.0%	24.4%	22.0%	23.7%	24.7%
Depreciation	3,704	3,902	4,030	5,095	5,601
Interest expense	1,642	2,012	1,546	1,610	1,770
Other income	1,459	1,201	1,010	1,182	1,383
Profit before tax	28,128	31,203	32,560	39,254	46,811
Taxes	7,304	7,985	8,655	9,892	11,796
Tax rate (%)	26.0%	25.6%	26.6%	25.2%	25.2%
<b>Adj. PAT</b>	<b>20,824</b>	<b>23,218</b>	<b>23,905</b>	<b>29,362</b>	<b>35,015</b>
Exceptional loss	140	1,769	-	-	-
Net profit	20,685	21,449	23,905	29,362	35,015
<b>EPS</b>	<b>216</b>	<b>241</b>	<b>248</b>	<b>305</b>	<b>363</b>

Source: Company, Systematix Institutional Research

## Cash Flow

YE: Mar (Rs mn)	CY20	CY21	CY22	CY23E	CY24E
PBIT	29,770	33,215	34,105	40,864	48,581
Depreciation	3,704	3,902	4,030	5,095	5,601
Tax paid	(7,304)	(7,985)	(8,655)	(9,892)	(11,796)
Working capital Δ	556	(1,347)	348	910	1,020
Other operating items	-	-	-	-	-
<b>Operating cashflow</b>	<b>26,726</b>	<b>27,785</b>	<b>29,829</b>	<b>36,978</b>	<b>43,405</b>
Capital expenditure	(7,249)	(6,828)	(5,680)	(13,000)	(20,000)
<b>Free cash flow</b>	<b>19,477</b>	<b>20,957</b>	<b>24,149</b>	<b>23,978</b>	<b>23,405</b>
Equity raised	5,389	(1,513)	1,054	-	-
Investments	2,873	6,898	(36)	-	-
Debt financing/disposal	(183)	(8)	-	-	-
Interest Paid	(1,642)	(2,012)	(1,546)	(1,610)	(1,770)
Dividends paid	(25,069)	(19,284)	(21,212)	(24,394)	(28,053)
Other items	4,085	(15,291)	(362)	1,774	1,951
<b>Net Δ in cash</b>	<b>4,930</b>	<b>(10,253)</b>	<b>2,048</b>	<b>(253)</b>	<b>(4,467)</b>

Source: Company, Systematix Institutional Research

## Balance Sheet

YE: Mar (Rs mn)	CY20	CY21	CY22	CY23E	CY24E
Equity capital	964	964	964	964	964
Reserves	19,229	19,881	23,628	28,595	35,556
Debt	348	341	341	341	341
Deferred tax liab (net)	(98)	(258)	(256)	(256)	(256)
Other non current liabili.	34,030	35,363	34,630	37,853	41,397
<b>Total liabilities</b>	<b>54,474</b>	<b>56,290</b>	<b>59,306</b>	<b>67,496</b>	<b>78,002</b>
Fixed Asset	28,180	32,402	30,642	38,546	52,945
Investments	14,638	7,740	7,775	7,775	7,775
Other Non-current Assets	1,483	14,947	18,427	15,938	17,532
<b>Inventories</b>	<b>14,165</b>	<b>15,802</b>	<b>19,288</b>	<b>19,701</b>	<b>22,215</b>
Sundry debtors	1,649	1,653	1,919	2,074	2,338
<b>Cash &amp; equivalents</b>	<b>17,699</b>	<b>7,354</b>	<b>9,456</b>	<b>13,140</b>	<b>8,673</b>
Loans and Advances	985	1,943	2,066	2,678	2,960
Sundry creditors	15,166	17,349	19,338	22,811	25,723
Other current liabilities	9,158	8,203	10,927	9,544	10,714
<b>Total Assets</b>	<b>54,474</b>	<b>56,290</b>	<b>59,306</b>	<b>67,496</b>	<b>78,002</b>

Source: Company, Systematix Institutional Research

## Ratios

YE: Mar	CY20	CY21	CY22	CY23E	CY24E
Revenue growth (%)	7.9	10.2	14.9	12.0	12.8
Op profit growth (%)	9.4	12.2	3.4	20.6	17.9
Net profit growth (%)	5.8	11.5	3.0	22.8	19.3
OPM (%)	24.0	24.4	22.0	23.7	24.7
Net profit margin (%)	15.6	15.8	14.1	15.5	16.4
RoCE (%)	147.9	159.2	147.9	149.1	145.5
RoNW (%)	105.8	113.2	105.2	108.4	106.0
EPS (Rs)	216.0	240.8	247.9	304.5	363.1
DPS (Rs)	260.0	200.0	220.0	253.0	291.0
BVPS (Rs)	209.4	216.2	255.0	306.6	378.8
Debtor days	5	4	4	4	4
Inventory days	39	39	42	38	38
Creditor days	41	43	42	44	44
P/E (x)	90.8	81.5	79.1	64.4	54.0
P/B (x)	93.7	90.8	76.9	64.0	51.8
EV/EBITDA (x)	58.5	52.4	50.7	42.0	35.7

Source: Company, Systematix Institutional Research

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## DISCLOSURES/APPENDIX

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