



TM

SYSTEMATIX INSTITUTIONAL EQUITIES

Systematix

Institutional Equities

25 April 2024

Nestlé India

Decent beat on both growth and margins; negative news flow-led weakness can provide buying opportunity

RESULT UPDATE

Sector: FMCG **Rating:** HOLD
CMP: Rs 2,563 **Target Price:** Rs 2,863

Stock Info

Sensex/Nifty	74,339/ 22,570
Bloomberg	NEST IN
Equity shares (mn)	964.2
52-wk High/Low	Rs2,771/2,049
Face value	Rs 1
M-Cap	Rs2,471bn/\$29bn
3-m Avg volume	US\$ 28mn

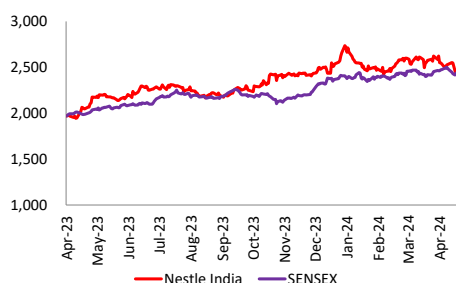
Financial Snapshot (Rs mn) *FY24–15 months

Y/E Mar	FY24*	FY25E	FY26E
Sales	243,939	217,913	245,390
PAT	39,339	36,486	42,472
EPS (Rs)	40.8	37.8	44.0
PE (x)	63.4	68.3	58.7
EV/EBITDA (x)	42.7	46.2	40.2
P/BV (x)	74.6	61.3	50.7
EV/Sales	10.2	11.4	10.1
RoE (%)	135.6	98.5	94.5
RoCE (%)	185.5	135.6	129.9
NWC (days)	2	-2	-2
Net gearing (x)	(0.1)	(0.3)	(0.2)

Shareholding Pattern (%)

	Mar24	Dec23	Sep23
Promoter	62.8	62.8	62.8
–Pledged	-	-	-
FII	12.1	12.1	12.1
DII	9.0	9.2	9.3
Others	16.1	16.0	15.8

Stock Performance (1-year)



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Investors are advised to refer disclosures made at the end of the research report.

Nestlé India (NEST IN) delivered a marginal beat on topline and a strong beat on EBITDA and PAT with revenue/EBITDA/PAT growth of 9%/22%/24%. Reported growth was broad-based across key brands, with volume growth of ~3% as per our estimate with strong contribution from pricing and mix. Domestic sales grew 8.9% YoY led by strong growth in core brands, targeted brand spends and traction in alternate channels like Out of Home, e-commerce and rural markets. Gross margins improved sharply by 300bps with moderation in RM prices and continued premiumization which flowed through to EBITDA which improved 270bps YoY to 25.6%. The core brands seem to be responding well to the marketing and distribution initiatives of the company and strong execution is visible on the OOH and rural initiatives. The innovation pipeline continued to churn out new launches under Maggi, Milk products and nutrition and Confectionary. Launch of Nespresso and JV with Dr. Reddy's for nutritional health solutions should further strengthen the product portfolio.

We expect NEST's continued dominance in its core categories, diversified portfolio and aggressive innovation/renovation initiatives to drive penetration-led growth. The company's low rural salience (~20%), category tailwinds and low penetration levels, lesser competitive intensity and global parent support will likely help drive continued outperformance. Margins have seen a strong recovery and new launches in categories like nutritional supplements, pet care, canned beverages and breakfast cereals should provide further impetus. We have increased our estimates for FY25/FY26 to factor in better growth/margins and now build in revenue/PAT CAGR of 12%/15% over FY24-26E for the company, and value NEST at a P/E of 65x (in line with its 5-year average) FY26 earnings to arrive a target price of Rs 2,863 (Rs 2,730 earlier). We maintain our HOLD rating for now given limited one-year upside but would suggest aggressively increasing exposure for the medium-term in case of any weakness on account of the ongoing controversy around baby cereals and/or the recently announced royalty increase proposal. We see NEST sustaining premium multiples given best-in-class growth prospects, return ratios and competitive positioning.

Broad-based 8.9% growth in domestic market driven by pricing and mix: NEST's domestic revenue grew 8.9% YoY while consolidated growth stood at 9% during the quarter. Growth was primarily led by pricing and mix with strong growth momentum in ecommerce and OOH channels. Key highlights for FY24 - Nescafe Classic, Nescafe Sunrise, and Nescafe Gold saw robust double-digit growth. As a result, in 2023, household penetration and market share increased at their fastest rate ever. The introduction of new products, greater media attention, a wider and longer distribution network, and creative brand activations all contributed to the growth of confectionery. Milkmaid and Ready-To-Drink (RTD) delivered strong growth. Increased Rural penetration, media campaigns, innovations, and strong consumer engagements all contributed to the increasing momentum of prepared dishes and cooking aids. With a strong focus on innovation and renovation, Maggi Oats Noodles, Korean Noodles, Maggi Teekha Masala, and Maggi Chatpata Masala varieties were introduced. A major emphasis on e-commerce in the pet care industry has increased the product portfolio's reach to more pet families. Total village coverage now stands

at 2 lakh+. With new capacities coming in and marketing and distribution investments continuing, we expect a 12% revenue CAGR to sustain over CY24-26E with a healthy volume and pricing/mix growth.

Softness in RM prices, premiumization and cost initiatives supporting margin expansion: Gross margin expanded 300bps YoY to 56.8%, given the softness in edible oils, wheat and packaging material. With all-time high prices and a continuing price surge, coffee and cocoa are experiencing historic headwinds for commodity prices. Grain and cereal prices are structurally rising, supported by MSP. Due to the anticipated hard summer, milk costs are predicted to increase. EBITDA margin stood at 25.6% (+269 bps) with a controlled 46 bps rise in other expenses offset by 16 bps decline in employee cost. We expect margins to expand gradually towards 25% in case the RM situation remains stable on the back of continued premiumization and margin-accretive innovation from the company. Even in case of more than expected inflation, we see NEST having enough pricing power to protect its margins.

Strong growth across distribution channels: The out-of-home business saw rapid expansion, while e-commerce continued to rise, accounting for 6.8% of total sales. Out of Home (OOH) kept up its fast pace of growth by emphasizing pertinent innovations and strong penetration in new channels. Growth was also facilitated by geographic expansion into Tier-1 towns outside of metro areas, utilizing popular tourism destinations, and concentrating on geographic clusters. With notable development in both click-and-mortar and quick commerce, e-commerce kept growing at an accelerated rate due to brands like Kitkat and Maggi Noodles. Targeted digital communication across several touchpoints and the acquisition of new customers contributed to the rapid expansion of Quick Commerce. Organized trade's robust, broad-based growth across categories was fueled by increased customer footfall and store expansion. Exports contributed to robust growth (19% growth during the quarter). Key areas like Singapore, Australia, New Zealand, Canada, and the US have seen a rise in demand for Maggi noodles and sauces. Nescafe Sunrise was introduced to Canada for the first time and kept gaining popularity in well-established markets like Singapore and Taiwan.

Nespresso brand of coffee and machines coming to India: NEST will launch its popular and premium coffee brand Nespresso in India, to cater to growing demand. Nespresso coffees and machines will be sold via online channels to consumers, and a boutique will also be opened, first in Delhi, to be later expanded to other key cities. A growing preference for in-home coffee consumption has been seen in recent years, which the company is trying to leverage.

NEST to form JV with Dr Reddy's for nutritional health solutions: NEST has formed a joint venture with Dr Reddy's Laboratories to sell its global range of nutritional health solutions as well as vitamins, minerals, herbals and supplements. The joint venture, to be based in Hyderabad, will aim to widen the reach of NEST's nutritional solutions to customers across the country by leveraging Dr Reddy's retail and distribution network. Dr Reddy's will hold a 51% stake in the joint venture, with NEST holding the remaining. NEST will have the option to increase its shareholding to up to 60% after 6 years, while Dr Reddy's will retain a minimum of 40% shareholding after NEST exercises its call option.

Company clarification on Cerelac sugar content controversy - NEST has stated that it has reduced added sugar content by upto 30% over the last 5 years depending upon variants. Company clarified that its products manufactured in India are in full compliance with international standards as well as local specifications with regard to the requirements of all nutrients including added sugars.

Exhibit 1: Quarterly performance snapshot

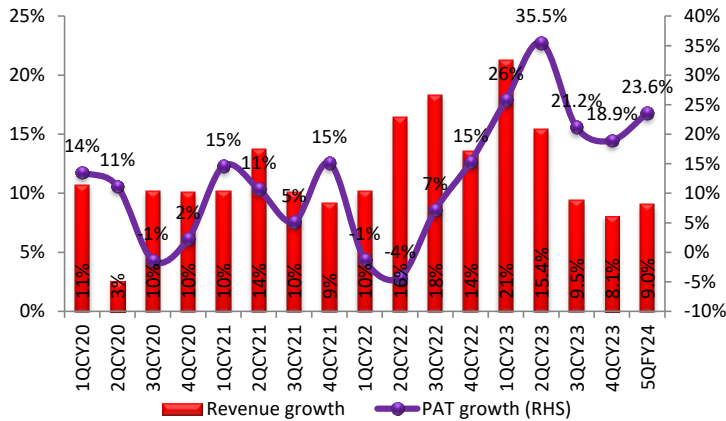
YE March (Rs mn)	Q5FY24	Q1CY23	Q4CY23	YoY (%)	QoQ (%)
Net Revenues	52,676	48,305	46,004	9.0	14.5
Raw material cost	22,759	22,315	19,046	2.0	19.5
(% of sales)	43.2	46.2	41.4		
Gross profit	29,917	25,990	26,959	15.1	11.0
(% of sales)	56.8	53.8	58.6	2.99	
Employee cost	4,869	4,543	4,201	7.2	15.9
(% of sales)	9.2	9.4	9.1		
Others	11,560	10,380	11,807	11.4	(2.1)
(% of sales)	21.9	21.5	25.7		
EBITDA	13,488	11,068	10,951	21.9	23.2
EBITDA margin (%)	25.6	22.9	23.8	2.69	
Other income	268	337	303	(20.6)	(11.7)
PBIDT	13,756	11,405	11,254	20.6	22.2
Depreciation	1,089	1,017	1,087	7.1	0.2
Interest	262	370	229	(29.2)	14.4
PBT	12,405	10,018	9,938	23.8	24.8
Tax	3,164	2,538	2,309	24.7	37.1
ETR (%)	25.5	25.3	23.2		
Adjusted PAT	9,241	7,479	7,630	23.6	21.1
PATAMI margin	17.5	15.5	16.6		
Extraordinary income/ (exp.)	(101)	113	1,073		
Reported PAT	9,342	7,366	6,557	26.8	42.5
Adj EPS (Rs)	9.6	7.8	7.9		

Source: Company, Systematix Institutional Research

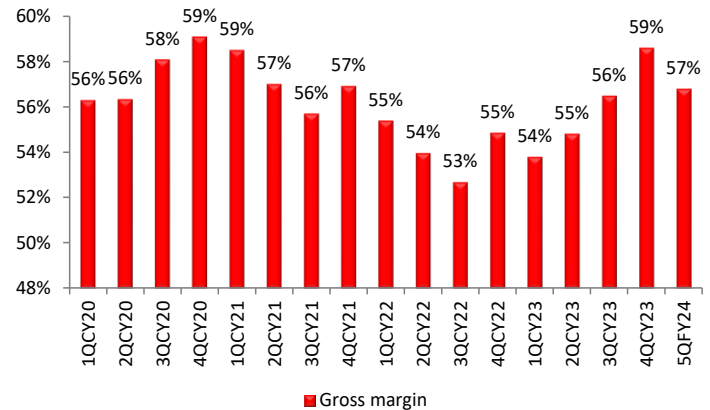
Exhibit 2: Change in estimates

	Revised estimates		Old estimates		Variation (%)	
	FY25E	FY26E	FY25E	FY26E	FY25E	FY26E
Net sales	217,913	245,390	214,128	238,906	2%	3%
EBITDA	53,666	61,827	51,068	57,779	5%	7%
EBITDA margin	24.63%	25.20%	23.8%	24.2%		
Adj. PAT	36,486	42,472	34,450	39,064	6%	9%

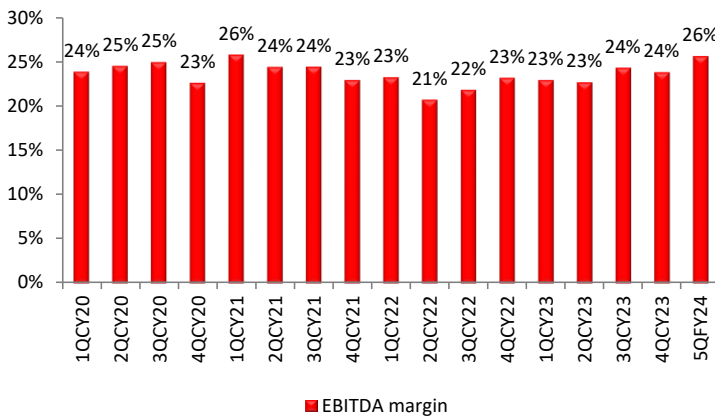
Source: Company, Systematix Institutional Research

Exhibit 3: Revenue/Adj. PAT growth stood at 9%/ 23.6% YoY

Source: Company, Systematix Institutional Research

Exhibit 4: Gross margin expanded 300bps YoY

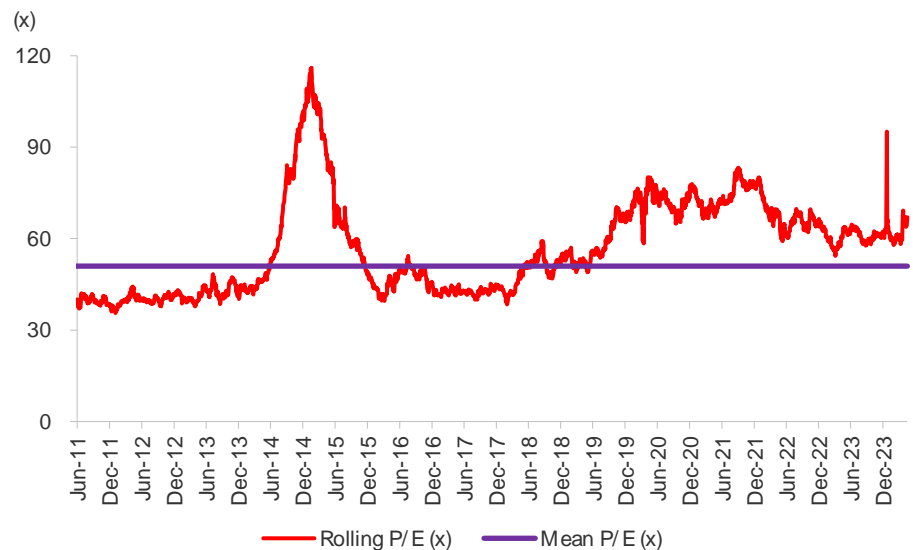
Source: Company, Systematix Institutional Research

Exhibit 5: EBITDA margin up 269 bps YoY

Source: Company, Systematix Institutional Research

Exhibit 6: Rise in SGA exps (+46 bps), fall in emp exps (-16bps)

Source: Company, Systematix Institutional Research

Exhibit 7: NEST currently trades at 67x one-year forward earnings

Source: Company, Systematix Institutional Research

FINANCIALS

Profit & Loss Statement

YE: Mar (Rs mn)	CY21	CY22	FY24*	FY25E	FY26E
Revenue	1,47,094	1,68,970	2,43,939	2,17,913	2,45,390
Gross profit	83,905	91,471	1,36,853	1,23,398	1,40,107
GP margin (%)	57.0%	54.1%	56.1%	56.6%	57.1%
Operating profit	35,915	37,126	58,252	53,666	61,827
OP margin (%)	24.4%	22.0%	23.9%	24.6%	25.2%
Depreciation	3,902	4,030	5,378	4,677	4,967
Interest expense	2,012	1,546	1,455	1,570	1,725
Other income	1,201	1,010	1,480	1,702	1,957
Profit before tax	31,203	32,560	52,899	49,120	57,092
Taxes	7,985	8,655	13,560	12,634	14,619
Tax rate (%)	25.6%	26.6%	25.6%	25.7%	25.6%
Adj. PAT	23,218	23,905	39,339	36,486	42,472
Exceptional loss	1,769	-	-	-	-
Net profit	21,449	23,905	39,339	36,486	42,472
EPS	24.1	24.8	40.8	37.8	44.0

Source: Company, Systematix Institutional Research; Note: *FY24 is of 15 months

Balance Sheet

YE: Mar (Rs mn)	CY21	CY22	FY24	FY25E	FY26E
Equity capital	964	964	964	964	964
Reserves	19,881	23,628	32,445	39,742	48,236
Debt	341	300	311	311	311
Deferred tax liab (net)	(258)	(256)	120	120	120
Other non current liabil.	35,363	34,630	32,581	35,526	38,765
Total liabilities	56,290	59,266	66,422	76,663	88,397
Fixed Asset	32,402	30,642	47,974	55,297	68,330
Investments	7,740	7,775	4,639	3,639	3,639
Other Non-current Assets	14,947	18,386	13,637	12,273	13,500
Inventories	15,802	19,288	20,894	22,687	25,547
Sundry debtors	1,653	1,919	3,005	2,388	2,689
Cash & equivalents	7,354	9,456	7,789	17,322	14,292
Loans and Advances	1,943	2,066	3,506	3,623	4,001
Sundry creditors	17,349	19,338	22,379	26,269	29,581
Other current liabilities	8,203	10,927	12,641	14,295	14,019
Total Assets	56,290	59,266	66,422	76,663	88,397

Source: Company, Systematix Institutional Research

Cash Flow

YE: Mar (Rs mn)	CY21	CY22	FY24	FY25E	FY26E
PBIT	33,215	34,105	54,354	50,690	58,817
Depreciation	3,902	4,030	5,378	4,677	4,967
Tax paid	(7,985)	(8,655)	(13,560)	(12,634)	(14,619)
Working capital Δ	(1,347)	348	(4,828)	3,605	(503)
Other operating items	-	-	-	-	-
Operating cashflow	27,785	29,829	41,343	46,338	48,661
Capital expenditure	(6,828)	(5,680)	(11,931)	(12,000)	(18,000)
Free cash flow	20,957	24,149	29,413	34,338	30,661
Equity raised	(1,513)	1,054	1,421	-	0
Investments	6,898	(36)	2,626	1,000	-
Debt financing/disposal	(8)	(40)	(3)	-	-
Interest Paid	(2,012)	(1,546)	(1,455)	(1,570)	(1,725)
Dividends paid	(19,284)	(21,212)	(38,279)	(29,189)	(33,978)
Other items	(15,291)	(322)	1,252	4,308	2,012
Net Δ in cash	(10,253)	2,048	(5,025)	8,888	(3,030)

Source: Company, Systematix Institutional Research

Ratios

YE: Mar	CY21	CY22	FY24	FY25E	FY26E
Revenue growth (%)	10.2	14.9	44.4	-10.7	12.6
Op profit growth (%)	12.2	3.4	56.9	-7.9	15.2
Net profit growth (%)	11.5	3.0	64.6	-7.3	16.4
OPM (%)	24.4	22.0	23.9	24.6	25.2
Net profit margin (%)	15.8	14.1	16.1	16.7	17.3
RoCE (%)	159.2	148.0	185.5	135.6	129.9
RoNW (%)	113.2	105.2	135.6	98.5	94.5
EPS (Rs)	24.1	24.8	40.8	37.8	44.0
DPS (Rs)	20.0	22.0	39.7	30.3	35.2
BVPS (Rs)	21.6	25.5	34.6	42.2	51.0
Debtor days	4	4	4	4	4
Inventory days	39	42	31	38	38
Creditor days	43	42	33	44	44
P/E (x)	107.4	104.3	63.4	68.3	58.7
P/B (x)	119.6	101.4	74.6	61.3	50.7
EV/EBITDA (x)	69.2	66.9	42.7	46.2	40.2

Source: Company, Systematix Institutional Research

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DISCLOSURES/APPENDIX

I. ANALYST CERTIFICATION

I, **Himanshu Nayyar, Chetan Mahadik**; hereby certify that (1) views expressed in this research report accurately reflect my/our personal views about any or all of the subject securities or issuers referred to in this research report, (2) no part of my/our compensation was, is, or will be directly or indirectly related to the specific recommendations or views expressed in this research report by **Systematix Shares and Stocks (India) Limited (SSSIL)** or its group/associate companies, (3) reasonable care is taken to achieve and maintain independence and objectivity in making any recommendations.

Disclosure of Interest Statement	Update
Analyst holding in the stock	No
Served as an officer, director or employee	No

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BUY (B): The stock's total return is expected to exceed 15% over the next 12 months.

HOLD (H): The stock's total return is expected to be within -15% to +15% over the next 12 months.

SELL (S): The stock's total return is expected to give negative returns of more than 15% over the next 12 months.

NOT RATED (NR): The analyst has no recommendation on the stock under review.

INDUSTRY VIEWS

ATTRACTIVE (AT): Fundamentals/valuations of the sector are expected to be attractive over the next 12-18 months.

NEUTRAL (NL): Fundamentals/valuations of the sector are expected to neither improve nor deteriorate over the next 12-18 months.

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