

27 July 2023

India | Equity Research | Q2CY23 results review

Nestle

Consumer Staples & Discretionary

Good. Ingredients to be great exist

Nestle's revenue growth of 15% YoY in Q2CY23 was largely in line with our estimates. Double-digit growth across segments for fifth consecutive quarter was driven by (1) deeper distribution expansion in lower-tier towns and villages ([see our report](#)), (2) strong performance in mega and metro cities, and (3) a portfolio which is better insulated to overall market slowdown. Further, acceleration of innovation engine should help in maintaining the growth trajectory. Gross margins were up 80bps QoQ as prices of most of the raw materials were stable, and we expect correction in milk prices to provide higher resources for ad-spends and innovations to drive growth ([see our report](#)). We continue to like NEST's incremental focus to drive RURBAN growth. In our opinion, Nestle is likely to witness industry-leading sales driven growth as they have plans to aggressively expand their distribution. Maintain **ADD**.

Strong double-digit across segments continues

Revenue grew 15% YoY in Q2CY23 with similar domestic sales growth trajectory. The performance was driven by volume- and price-led broad-based growth – all segments reported double-digit top-line growth (fifth quarter consecutively). Exports also saw robust sales growth of 25% YoY. It highlighted that (1) Rurban continued its growth trajectory driven by distribution-led penetration, (2) Mega cities and metro witnessed strong growth with robust performance in tier 1 to 6 towns and continued strength in rural markets, (3) OOH continued to deliver strong growth and (4) MT witnessed broad based growth and e-commerce witnessed strong growth driven by quick commerce.

In terms of segmental performance, (1) prepared dishes and cooking aid witnessed double-digit growth through MAGGI Noodles, (2) milk products and nutrition reported strong double-digit growth despite commodity pressure driven by Milkmaid and Peptamen, (3) confectionary delivered double-digit growth driven by KITKAT and MUNCH, (4) Beverages witnessed double-digit growth driven by penetration led growth in NESCAFÉ Classic, NESCAFÉ Sunrise and NESCAFÉ GOLD, (5) Pet care continues to build its momentum.

Further, Nestle has increased focus on innovation and renovation and launched three new products – 1) Resource Fiber Choice, 2) Everyday Zero and 3) MUNCH breakfast cereals.

Financial Summary

Y/E Decemcer (INR mn)	CY21A	CY22A	CY23E	CY24E
Net Revenue	1,46,649	1,67,895	1,94,055	2,15,797
EBITDA	34,669	36,508	45,183	52,582
EBITDA Margin (%)	23.6	21.7	23.3	24.4
Net Profit	23,549	23,905	30,295	35,733
EPS (Rs)	244.2	247.9	314.2	370.6
EPS % Chg YoY	13.1	1.5	26.7	18.0
P/E (x)	91.4	90.0	71.1	60.2
EV/EBITDA (x)	61.9	58.7	47.2	40.5
RoCE (%)	115.8	107.2	107.2	101.3
RoE (%)	118.8	108.5	109.4	104.5

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Market Data

Market Cap (INR)	2,153bn
Market Cap (USD)	26,267mn
Bloomberg Code	NEST IN
Reuters Code	NEST.BO
52-week Range (INR)	23,395 /17,880
Free Float (%)	37.0
ADTV-3M (mn) (USD)	19

Price Performance (%)	3m	6m	12m
Absolute	5.6	16.8	21.7
Relative to Sensex	10.1	12.7	20.2

ESG Disclosure	2021	2022	Change
ESG score	40.7	50.7	9.9
Environment	19.1	48.9	29.8
Social	24.4	24.4	0.0
Governance	78.6	78.6	0.0

Note - Score ranges from 0 - 100 with a higher score indicating higher ESG disclosures.

Source: Bloomberg, I-sec research

Earnings Revisions (%)	CY23E	CY24E
Revenue	-	-
EBITDA	1.3	1.2
EPS	0.7	0.0

Previous Reports

13-06-2023: [Company update](#)

25-04-2023: [Q1CY23 results review](#)

Stable raw material prices and higher ad-spends

Gross margin expanded by 80bps YoY and QoQ to 54.4%. Management highlighted that (1) price stability in fresh milk prices, (2) edible oils, wheat and packaging materials are at lower price range while fuel witnessed reversal of price trend and 3) Coffee (Robusta) prices are elevated and expected to remain volatile. Our analysis of Nestle's consumer-price retention power in milk products and nutrition segment (~40% of revenues and >50% of profits) indicates potential for material gross margin expansion in the event of milk price deflation (See our report - [link](#)). Company had accelerated its ad-spends and the focus on innovation and renovation has also increased and we expect gross margin expansion to provide Nestle with higher resources to drive faster growth. As a result of increased investment in ad-spends EBITDA margin declined by ~55bps QoQ to 22.1% (+160bps YoY). Adjusted net profit came in at INR 6.9bn (+34% YoY).

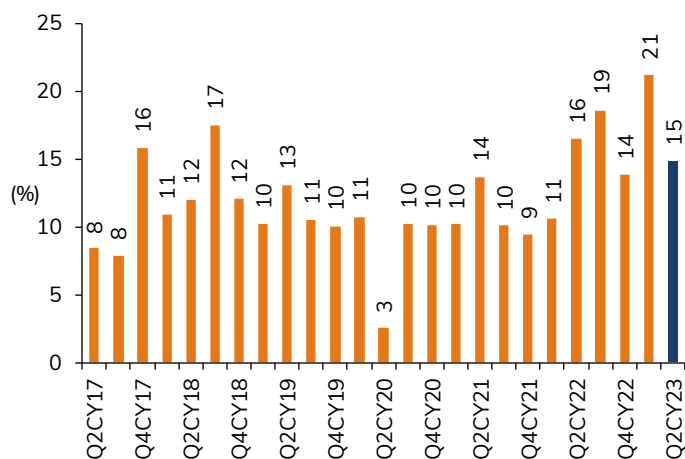
Valuation and risks

Our earnings estimates are largely unchanged CY23E-24E, modelling revenue / EBITDA / PAT CAGR of 13 / 20 / 22 (%) over CY22-24E. Maintain ADD rating with a DCF-based unchanged target price of INR 24,500. Key risks are consumption slowdown linked to economic performance.

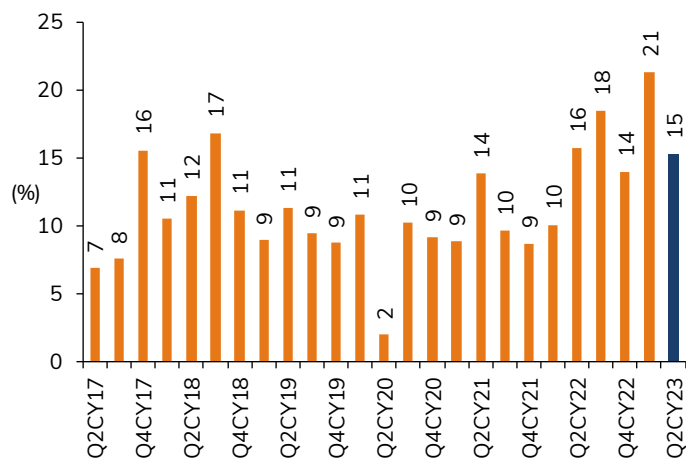
Exhibit 1: Q2CY23 result review

INR mn	Q2CY23	Q2CY22	YoY (%)	Q1CY23	QoQ (%)	YTDCY23	YTDCY22	YoY (%)
Net domestic revenue	44,208	38,484	15	46,127	(4)	90,335	76,546	18
Export revenue	1,987	1,584	25	1,957	2	3,944	3,151	25
Net Revenues	46,195	40,069	15	48,084	(4)	94,279	79,697	18
COGS	(21,050)	(18,583)	13	(22,315)	(6)	(43,366)	(36,434)	19
Gross profit	25,145	21,485	17	25,769	(2)	50,913	43,263	18
Staff cost	(4,572)	(4,084)	12	(4,543)	1	(9,115)	(8,067)	13
Other opex	(10,374)	(9,207)	13	(10,348)	0	(20,722)	(18,029)	15
Total opex	(14,947)	(13,291)	12	(14,890)	0	(29,837)	(26,096)	14
EBITDA	10,198	8,195	24	10,878	(6)	21,076	17,168	23
Other income	550	491	12	558	(1)	1,108	1,003	10
Finance Cost	(370)	(370)	0	(370)	(0)	(740)	(725)	2
D&A	(1,074)	(1,016)	6	(1,017)	6	(2,091)	(2,061)	1
PBT	9,305	7,300	27	10,049	(7)	19,354	15,385	26
Tax	(2,382)	(1,850)	29	(2,538)	(6)	(4,920)	(3,965)	24
PAT	6,923	5,450	27	7,511	(8)	14,434	11,420	26
Impairment of fixed assets	-	(160)		(113)		(118)	(160)	
Provision for contingencies	(33)	(137)	(76)	(32)	4	(1,685)	(198)	749
Recurring PAT	6,890	5,153	34	7,366	(6)	12,631	11,061	14
Extraordinary items	-	-		-		(108)	-	
Net profit (reported)	6,890	5,153	34	7,366	(6)	12,523	11,061	13
EPS	71.5	53.4	34	76.4	(6)	131.0	114.7	14
Costs as a % of sales								
COGS	45.6	46.4	-82 bps	46.4	-85 bps	46.0	45.7	28 bps
Gross margin (%)	54.4	53.6	81 bps	53.6	84 bps	54.0	54.3	-29 bps
Staff cost	9.9	10.2	-30 bps	9.4	45 bps	9.7	10.1	-46 bps
Other opex	22.5	23.0	-53 bps	21.5	93 bps	22.0	22.6	-65 bps
EBITDA margin (%)	22.1	20.5	162 bps	22.6	-55 bps	22.4	21.5	81 bps
Income tax rate (%)	25.6	25.3	25 bps	25.3	33 bps	25.4	25.8	-36 bps

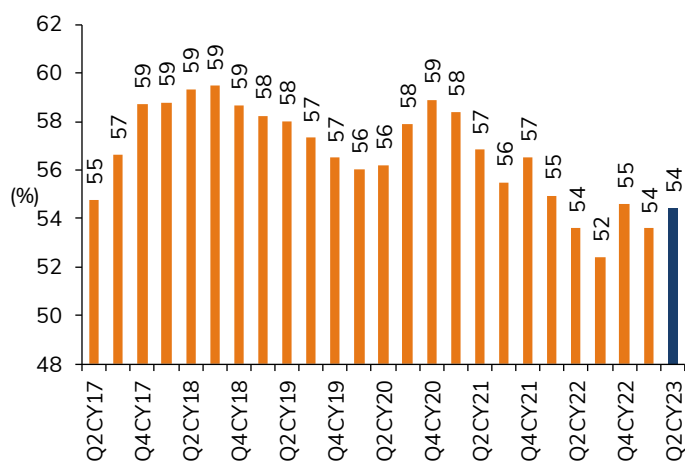
Source: Company data, I-Sec research

Exhibit 2: Domestic revenue growth

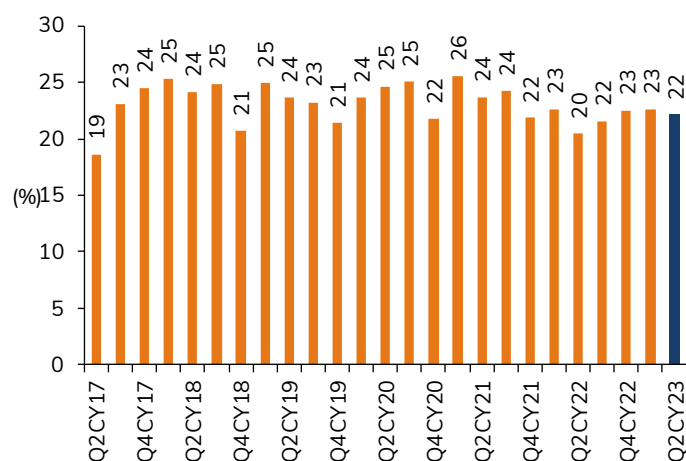
Source: Company data, I-Sec research

Exhibit 3: Revenue growth

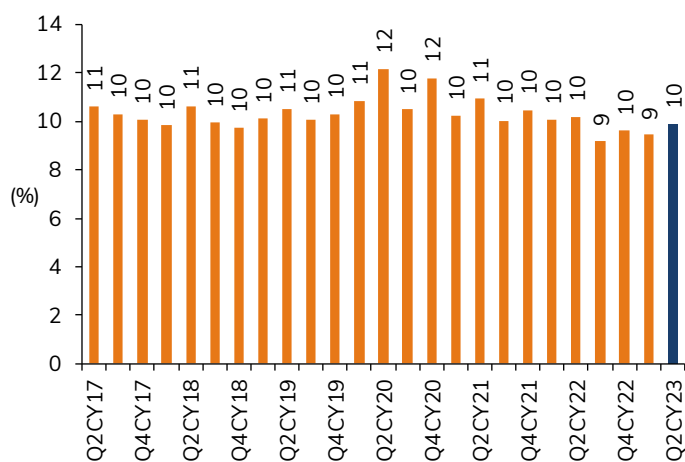
Source: Company data, I-Sec research

Exhibit 4: Gross margin

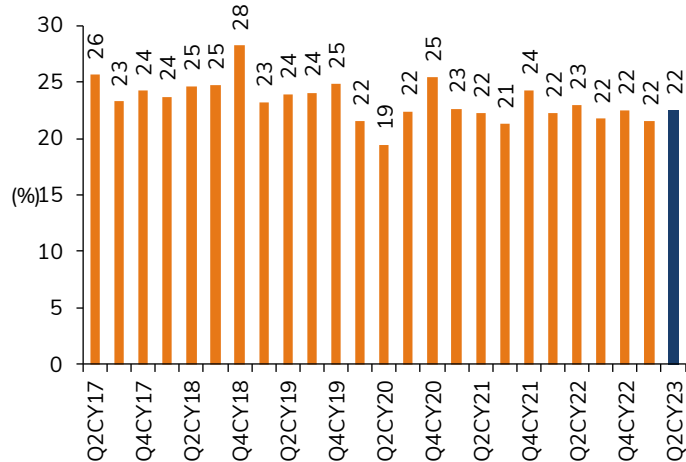
Source: Company data, I-Sec research

Exhibit 5: EBITDA margin

Source: Company data, I-Sec research

Exhibit 6: Employee costs (as a % of sales)

Source: Company data, I-Sec research

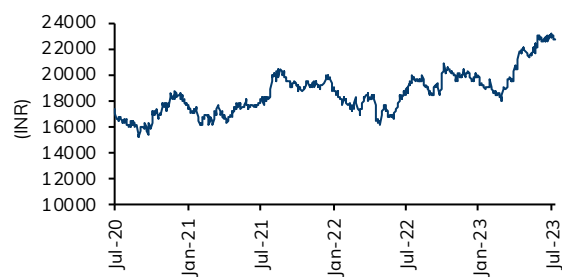
Exhibit 7: Other expenses (as a % of sales)

Source: Company data, I-Sec research

Exhibit 8: Shareholding pattern

%	Dec'22	Mar'23	Jun'23
Promoters	62.8	62.8	62.8
Institutional investors	21.2	21.3	21.5
MFs and others	4.4	4.5	4.9
FIs/Banks, Insurance	3.9	3.8	3.4
FIIIs	12.9	12.9	13.2
Others	16.0	15.9	15.7

Source: Bloomberg, I-Sec research

Exhibit 9: Price chart


Source: Bloomberg, I-Sec research

Financial Summary

Exhibit 10: Profit & Loss

(INR mn, year ending Decemcer)

	CY21A	CY22A	CY23E	CY24E
Net Sales	1,46,649	1,67,895	1,94,055	2,15,797
Operating Expenses	1,11,980	1,31,387	1,48,872	1,63,215
EBITDA	34,669	36,508	45,183	52,582
EBITDA Margin (%)	23.6	21.7	23.3	24.4
Depreciation & Amortization	3,910	4,030	4,394	5,043
EBIT	30,759	32,478	40,789	47,539
Interest expenditure	2,017	1,546	1,503	1,663
Other Non-operating Income	1,958	2,084	2,228	2,939
Recurring PBT	30,700	33,017	41,514	48,815
Profit / (Loss) from Associates	-	-	-	-
Less: Taxes	7,389	8,655	10,968	12,937
PAT	23,311	24,362	30,546	35,879
Less: Minority Interest	-	-	-	-
Extraordinaries (Net)	(2,365)	-	-	-
Net Income (Reported)	21,184	23,905	30,295	35,733
Net Income (Adjusted)	23,549	23,905	30,295	35,733

Source Company data, I-Sec research

Exhibit 11: Balance sheet

(INR mn, year ending Decemcer)

	CY21A	CY22A	CY23E	CY24E
Total Current Assets	27,622	34,902	44,957	54,782
of which cash & cash eqv.	7,987	11,629	18,351	25,373
Total Current Liabilities & Provisions	25,613	28,394	32,925	36,732
Net Current Assets	2,009	6,507	12,033	18,051
Investments	7,107	5,602	5,602	5,602
Net Fixed Assets	26,529	27,058	30,378	33,375
ROU Assets	-	-	-	-
Capital Work-in-Progress	2,462	3,584	3,584	3,584
Total Intangible Assets	-	-	-	-
Long Term Loans & Advances	14,945	15,007	17,346	19,289
Deferred Tax assets	-	-	-	-
Total Assets	56,470	61,137	72,321	83,279
Liabilities				
Borrowings	341	300	300	300
Deferred Tax Liability	(258)	(256)	(256)	(256)
Provisions	32,853	32,052	37,046	41,196
Other Liabilities	4,072	4,450	4,450	4,450
Equity Share Capital	964	964	964	964
Reserves & Surplus	18,500	23,628	29,817	36,624
Total Net Worth	19,464	24,592	30,781	37,589
Minority Interest	-	-	-	-
Total Liabilities	56,470	61,137	72,321	83,279

Source Company data, I-Sec research

Exhibit 12: Quarterly trend

(INR mn, year ending Decemcer)

	Sep-22	Dec-22	Mar-23	Jun-23
Net Sales	45,774	42,333	48,084	46,195
% growth (YOY)	18.6	13.8	21.2	14.9
EBITDA	9,857	9,534	10,878	10,198
Margin %	21.5	22.5	22.6	22.1
Other Income	306	296	337	300
Extraordinaries	-	-	-	-
Adjusted Net Profit	6,615	6,281	7,366	6,890

Source Company data, I-Sec research

Exhibit 13: Cashflow statement

(INR mn, year ending Decemcer)

	CY21A	CY22A	CY23E	CY24E
Operating Cashflow	22,360	27,374	38,471	43,463
Working Capital Changes	(1,717)	(302)	3,852	3,211
Capital Commitments	(20,449)	(4,949)	(7,714)	(8,039)
Free Cashflow	1,911	22,426	30,757	35,424
Other investing cashflow	1,246	1,031	1,574	2,186
Cashflow from Investing Activities	(19,203)	(3,917)	(6,141)	(5,853)
Issue of Share Capital	-	-	-	-
Interest Cost	(11)	(20)	(1,503)	(1,663)
Inc (Dec) in Borrowings	-	-	-	-
Dividend paid	(19,283)	(20,247)	(24,105)	(28,926)
Others	(906)	(960)	-	-
Cash flow from Financing Activities	(20,200)	(21,227)	(25,608)	(30,589)
Chg. in Cash & Bank balance	(17,043)	2,230	6,722	7,021
Closing cash & balance	656	9,584	16,178	23,199

Source Company data, I-Sec research

Exhibit 14: Key ratios

(Year ending Decemcer)

	CY21A	CY22A	CY23E	CY24E
Per Share Data (INR)				
Reported EPS	244.2	247.9	314.2	370.6
Adjusted EPS (Diluted)	244.2	247.9	314.2	370.6
Cash EPS	284.8	289.7	359.8	422.9
Dividend per share (DPS)	200.0	220.0	250.0	300.0
Book Value per share (BV)	201.9	255.0	319.2	389.8
Dividend Payout (%)	81.9	88.7	79.6	80.9
Growth (%)				
Net Sales	10.3	14.5	15.6	11.2
EBITDA	9.9	5.3	23.8	16.4
EPS (INR)	13.1	1.5	26.7	18.0
Valuation Ratios (x)				
P/E	91.4	90.0	71.1	60.2
P/CEPS	78.4	77.1	62.1	52.8
P/BV	110.6	87.5	69.9	57.3
EV / EBITDA	61.9	58.7	47.2	40.5
P / Sales	14.7	12.8	11.1	10.0
Dividend Yield (%)	0.9	1.0	1.1	1.3
Operating Ratios				
Gross Profit Margins (%)	56.7	53.8	54.8	56.6
EBITDA Margins (%)	23.6	21.7	23.3	24.4
Effective Tax Rate (%)	24.1	26.2	26.4	26.5
Net Profit Margins (%)	15.9	14.5	15.7	16.6
Net Debt / Equity (x)	(0.4)	(0.5)	(0.6)	(0.7)
Net Debt / EBITDA (x)	(0.2)	(0.3)	(0.4)	(0.5)
Fixed Asset Turnover (x)	3.6	3.5	3.6	3.5
Working Capital Days	(16)	(13)	(14)	(14)
Inventory Turnover Days	42	45	44	43
Receivables Days	4	4	4	4
Payables Days	46	45	45	45
Profitability Ratios				
RoCE (%)	115.8	107.2	107.2	101.3
RoE (%)	118.8	108.5	109.4	104.5
RoIC (%)	123.1	114.1	113.1	107.6

Source Company data, I-Sec research

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