

## Healthy growth continues despite adverse scenario

Nestlé India (NIL) reported strong revenue growth of 10.8% despite a challenging environment for supply chain & manufacturing. However, we believe 70% of NIL's product portfolio (milk & related products and noodles) would have benefited from the lockdown. The restricted 'out of home' consumption has driven growth in the instant snack. Moreover, consumer preferences have shifted towards packaged foods for increased hygiene consciousness. It is important to note that a 220 bps contraction in gross margins (largely due to elevated milk prices) has not impacted operating margins (down 70 bps) to the same extent. The company was quick to cut the overhead spend. We believe media spend would have been withdrawn in the last eight to 10 days of March 2020. Net profit was up 13.4% due to a cut in corporate tax rate. Other income declined 41% given reduced liquid investment as the company paid a special dividend in August 2019.

## Manufacturing disruption to hit revenue in Q2CY20

Though the company is witnessing higher demand for Maggi (entire prepared dishes segment), manufacturing has still been disrupted in some of its plants. Our channel check suggests usual sales during April as the company was able to supply with existing inventories & usual manufacturing from some of its plants (Moga, Punjab & Goa plants are working at full capacity). However, noodles & coffee supplies are getting depleted in May 2020 with some plants working on reduced capacity mainly due to labour shortage, unavailability of raw material and strict government norms. This is likely to negatively impact sales in the May 2020. We cut our CY20E revenue & earnings estimate by 4.8% & 4.4%, respectively. With the 20% decline in milk prices, ~5% dip in sugar prices & sharp cut in packaging related cost, the company is expected to witness an uptick in gross margins. Further considering the cut in A&P spend, specifically during lockdown period, we expect the company to improve its operating margins by 105 bps in CY20E. We believe consumer preferences would shift towards packaged foods given increasing consciousness about hygiene. This could propel the growth for the milk category, going forward. We expect revenue & earnings CAGR of 10.9% and 14.8%, respectively, in CY19-21E.

## Focus to remain on new product launches

The company was able to achieve strong volume growth of 7-10% in the last two years backed by aggressive new launches (60 + launches in three years). Contribution from new launches increased from ~1.7% to ~3.7% in last three years. We believe NIL would be able to maintain strong volume growth momentum by foraying into new categories within packaged foods and its record of high success ratio (70%) of new launches.

## Valuation & Outlook

In the current unprecedented times where supply chain & manufacturing operations have been hit by lockdowns, NIL is less vulnerable given its presence in packaged foods. With ~80% of revenue contribution from urban India, the company is also least disrupted by liquidity problems of wholesalers. The stock is trading at premium valuation multiples. We maintain our target price of ₹ 18000/share with a **HOLD** recommendation.

### Key Financial Summary

Key Financials	CY17	CY18	CY19	CY20E	CY21E	CAGR (CY19-21E)
Net Sales	9952.5	11216.2	12295.3	13300.0	15115.9	10.9%
EBITDA	2248.3	2759.8	2864.3	3271.3	3755.9	14.5%
EBITDA Margin %	22.6	24.6	23.3	24.6	24.8	
Net Profit	1225.2	1606.9	1969.6	2226.3	2597.7	14.8%
EPS (₹)	127.07	166.66	204.27	230.90	269.42	
P/E	131.5	100.3	81.8	72.4	62.0	
RoNW %	37.5	45.6	101.9	114.1	123.1	
RoCE (%)	34.9	42.9	56.9	59.3	65.9	

Source: Company, ICICI Direct Research



### Particulars

Particulars (₹ crore)	Amount
Market Capitalization	161127
Total Debt (CY19)	53.1
Cash & Investments (CY19)	2,315.5
EV	158,865.1
52 week H/L (₹)	18369 / 10120
Equity capital	96.4
Face value (₹)	10.0

### Key Highlights

- Domestic sales increased 10.8% driven by volume & price mix despite supply chain & manufacturing related disruption during lockdown
- Export sales increased 12.9%
- Gross margins contracted 220 bps due to higher milk prices
- Maintain HOLD recommendation with target price of ₹ 18000/share

### Research Analyst

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Exhibit 1: Variance Analysis

Particulars (₹ crore)	Q1CY20	Q1CY20E	Q1CY19	YoY (%)	Q4CY19	QoQ (%)	Comments
Total Operating Income	3,325.3	3,233.9	3,003.0	10.7	3,149.3	5.6	Net sales grew 10.7% led by strong growth in Maggi brand. Also, our estimate suggests milk product category would have grown at a faster pace
Operating Income	19.5	20.2	20.6	-5.2	18.6	5.1	
Raw Material Expenses	1,453.3	1,366.9	1,245.3	16.7	1,361.4	6.7	Higher milk prices during the quarter resulted in 220 bps dip in gross margins
Employee Expenses	358.4	314.9	303.8	18.0	322.7	11.1	
Other operating Expenses	720.3	793.8	716.2	0.6	787.4	-8.5	
EBITDA	793.3	758.3	737.7	7.5	677.9	17.0	
EBITDA Margin (%)	23.9	23.4	24.6	-71 bps	21.5	233 bps	The company maintained margins largely due to lower overhead spend (our estimate media spend would have been withdrawn in the last eight to 10 days of March)
Depreciation	91.4	76.9	78.0	17.2	79.6	14.8	
Interest	41.0	30.5	31.6	29.6	28.4	44.3	
Other Income	42.9	66.9	73.2	-41.5	44.7	-4.1	Decline in other income due to reduced liquid investment book as company paid special dividend in August 2019
Exceptional Items	0.0	0.0	0.0	NA	0.0	NA	
PBT	703.9	717.8	701.3	0.4	614.6	14.5	
Tax Outgo	178.4	180.9	238.1	-25.0	141.6	26.0	
PAT	525.4	536.9	463.3	13.4	473.0	11.1	Strong earnings growth largely due to cut in corporate tax
Adjusted PAT	525.4	536.9	463.3	13.4	473.0	11.1	

Source: Company, ICICI Direct Research

Exhibit 2: Change in estimates

(₹ Crore)	CY20E			CY21E			Comments
	Old	New	% Change	Old	New	% Change	
Net Sales	13,972.6	13,300.0	-4.8	15,597.7	15,115.9	-3.1	We cut our CY20 estimate due to scaling down of manufacturing operations in initial lockdown period
EBITDA	3289.9	3271.3	-0.6	3774.2	3755.9	-0.5	
EBITDA Margin(%)	23.5	24.6	105 bps	24.2	24.8	65 bps	Higher margins due to sharp decline in milk prices during lockdown & expected lower advertisement spend
PAT	2329.0	2226.3	-4.4	2715.2	2597.7	-4.3	
EPS (₹)	241.5	230.9	-4.4	281.6	269.4	-4.3	

Source: Company, ICICI Direct Research

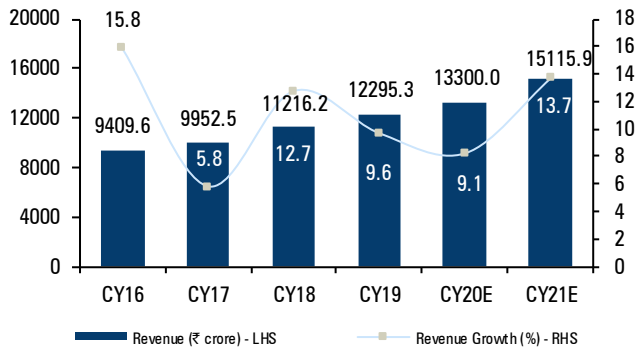
Exhibit 3: Assumptions

	Current					Earlier			Comments
	CY16	CY17	CY18	CY19E	CY20E	CY21E	CY20E	CY21E	
<b>Gross Sales (₹ crore)</b>									
Milk Product and Nutrition	4,635.0	4,819.6	5,187.6	5,610.4	6,183.2	6,945.0	6,241.0	6,880.1	Change in sales estimate due to disruption in manufacturing operations
Beverages	1,286.1	1,387.0	1,522.6	1,662.7	1,679.3	1,868.1	1,831.6	1,980.9	
Prepared dishes	2,317.6	2,707.1	3,105.3	3,484.1	3,832.5	4,500.1	4,198.7	4,843.6	
Chocolate & confectionery	1,170.9	1,221.4	1,400.7	1,558.2	1,604.9	1,802.7	1,701.2	1,893.1	
<b>Volume Growth (%)</b>									
Overall Volume Growth	25.0	10.9	11.1	8.0	7.9	11.4	12.8	9.4	
Milk Product and Nutrition	-2.4	1.6	4.8	5.0	7.0	8.0	8.0	6.0	
Beverages	-0.2	10.6	10.6	5.0	0.0	8.0	8.0	5.0	
Prepared dishes	71.5	19.0	14.5	10.0	10.0	14.0	17.0	12.0	
Chocolate & confectionery	6.7	4.3	14.7	8.0	3.0	8.0	6.0	7.0	

Source: Company, ICICI Direct Research

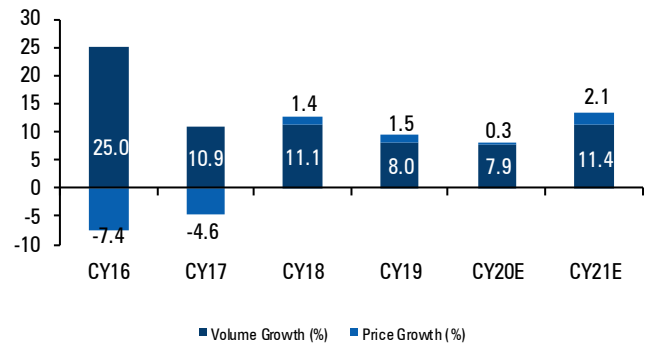
## Key Metrics

Exhibit 4: Revenue growth trend



Source: Company, ICICI Direct Research

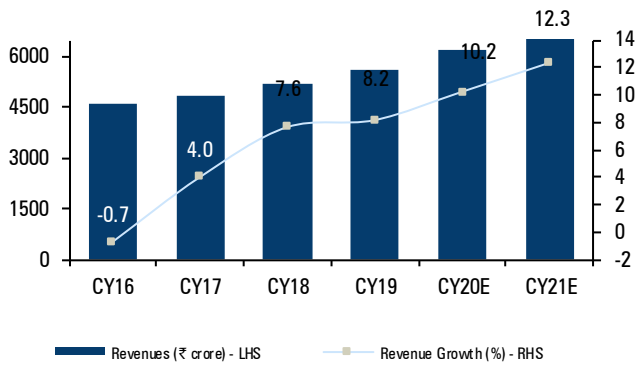
Exhibit 5: Volume growth to drive revenue



Source: Company, ICICI Direct Research

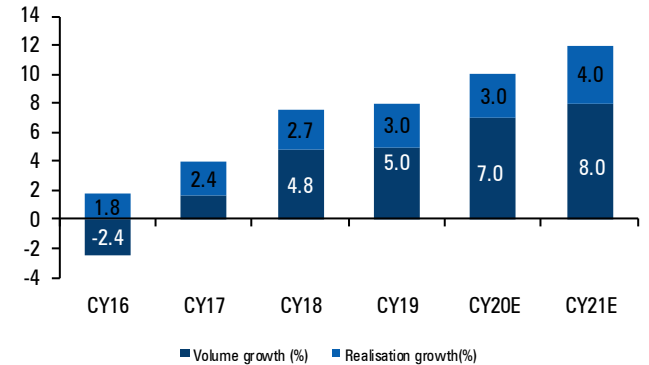
### Milk products & nutrition – Focus on value addition

Exhibit 6: Revenue to grow at 11.3% CAGR over CY19-21E



Source: Company, ICICI Direct Research

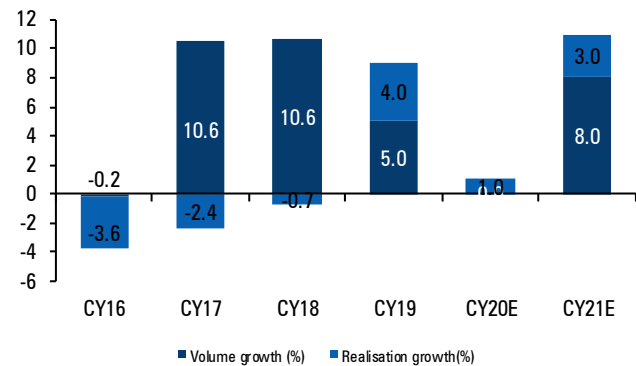
Exhibit 7: Revenue growth to be mix of volume & price growth



Source: Company, ICICI Direct Research

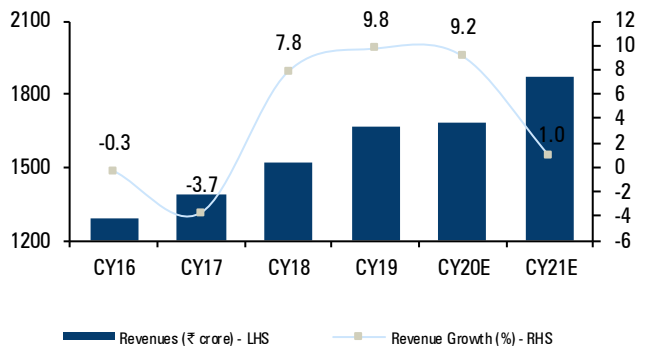
### Beverages – Focus on differentiated products

Exhibit 8: Beverages revenue growth expected at 6% CAGR



Source: Company, ICICI Direct Research

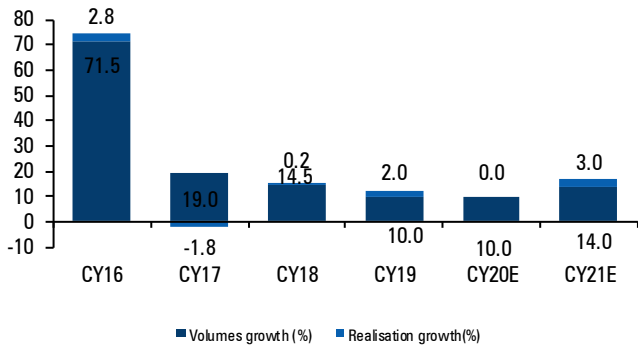
Exhibit 9: Volume growth to be impacted by lockdown



Source: Company, ICICI Direct Research

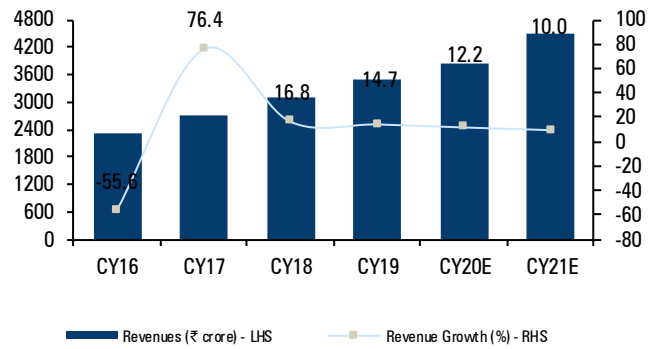
Prepared dishes – Rebuilding, reinvigorating portfolio

Exhibit 10: Maggi sales cross pre-ban level



Source: Company, ICICI Direct Research

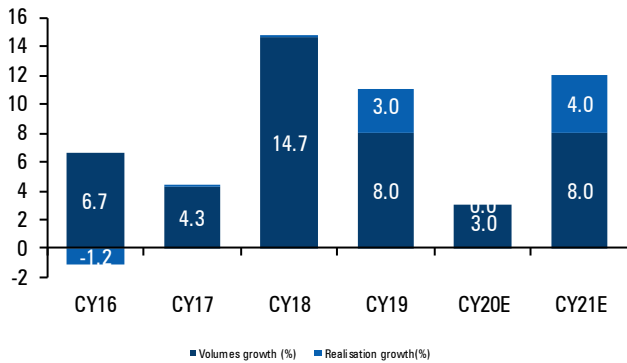
Exhibit 11: Innovation to generate healthy volume growth



Source: Company, ICICI Direct Research

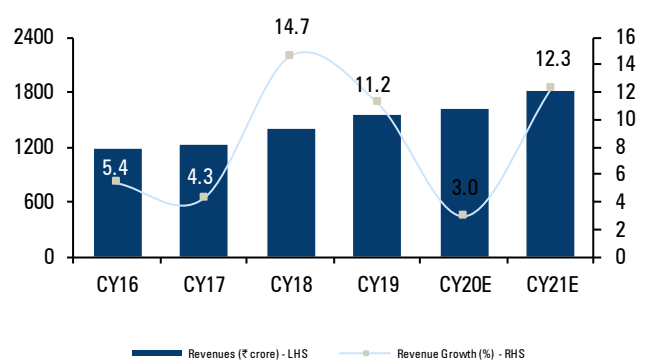
Chocolate & confectionery – Focus on premiumisation

Exhibit 12: Sales to gain traction, going forward



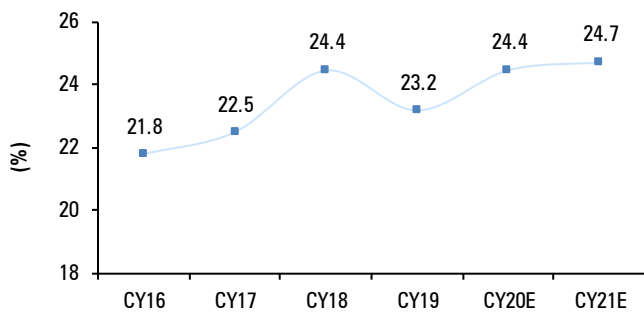
Source: Company, ICICI Direct Research

Exhibit 13: Volume growth to support higher growth



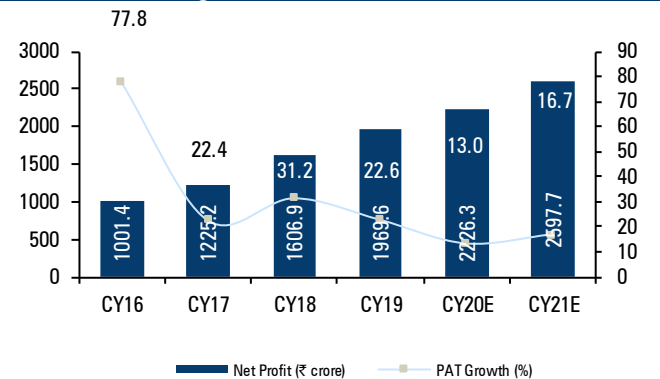
Source: Company, ICICI Direct Research

Exhibit 14: EBITDA margin to remain at elevated levels



Source: Company, ICICI Direct Research

Exhibit 15: PAT to grow at 14.8% CAGR over CY19-21E



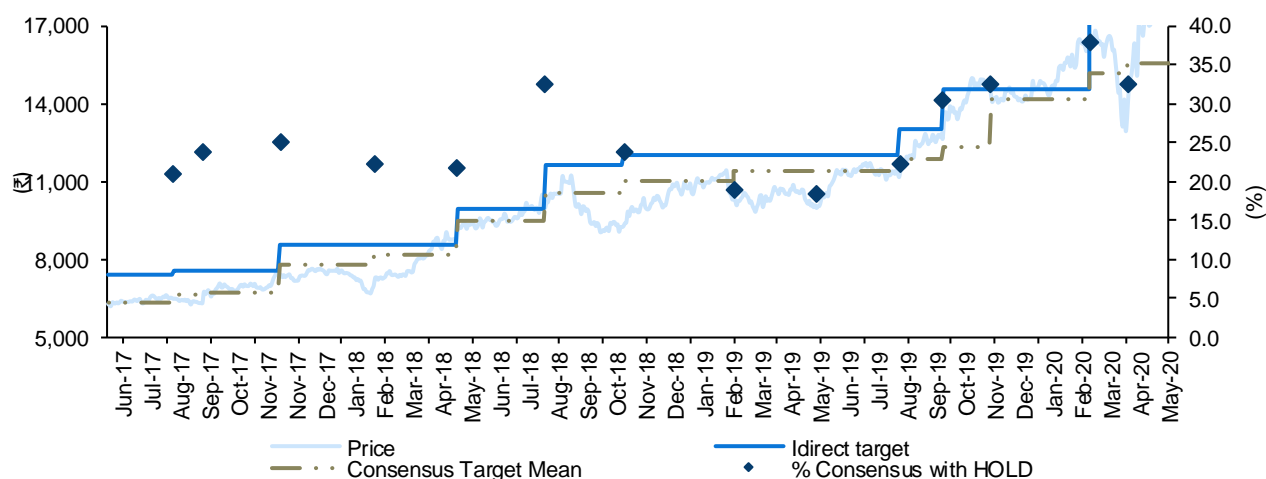
Source: Company, ICICI Direct Research

Exhibit 16: Valuation

	Sales (₹ cr)	Growth (%)	EPS (₹)	Growth (%)	PE (x)	EV/EBITDA (x)	RoNW (%)	RoCE (%)
CY18	11216.2	12.7	166.7	31.2	100.3	57.8	45.6	42.9
CY19	12295.3	9.6	204.3	22.6	81.8	55.8	101.9	56.9
CY20E	13300.0	8.2	230.9	13.0	72.4	48.9	114.1	59.3
CY21E	15115.9	13.7	269.4	16.7	62.0	42.6	123.1	65.9

Source: Company, ICICI Direct Research

Exhibit 17: Recommendation History vs. Consensus



Source: Bloomberg, Company, ICICI Direct Research

Exhibit 18: Top 10 Shareholders

Rank	Investor Name	Filing Date	% O/S	Position (m)	Change (m)
1	Nestle Sa	31-Dec-19	34.3	33.1	0.0
2	Maggi Enterprises Lt	31-Dec-19	28.5	27.5	0.0
3	Life Insurance Corp	31-Dec-19	3.0	2.9	0.1
4	50 Sbi-Etf Nifty	31-Dec-19	1.5	1.5	1.5
5	Sbi Funds Management	31-Mar-20	1.5	1.5	-0.1
6	Axis Asset Managemen	31-Mar-20	1.2	1.2	0.1
7	Arisaig India Fund L	30-Jun-19	1.0	1.0	-0.1
8	Vanguard Group	8-Apr-20	0.9	0.9	0.0
9	Blackrock	21-Apr-20	0.8	0.8	0.0
10	Uti Asset Management	31-Mar-20	0.5	0.5	0.0

Source: Reuters, ICICI Direct Research

Exhibit 19: Shareholding Pattern

(in %)	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20
Promoter	62.8	62.8	62.8	62.8	62.76
FII	12.6	13.0	12.6	12.1	11.81
DII	7.7	7.5	8.5	8.9	9.12
Others	17.0	16.8	16.1	16.3	16.3

Source: Company, ICICI Direct Research

## Financial summary

Exhibit 20: Profit and loss statement				
	₹ crore			
(Year-end December)	CY18	CY19	CY20E	CY21E
<b>Total operating Income</b>	<b>11,292.3</b>	<b>12,368.9</b>	<b>13,381.0</b>	<b>15,205.0</b>
Growth (%)	12.8	9.5	8.2	13.6
Raw Material Expenses	3,823.2	5,223.9	5,720.7	6,445.7
Employee Expenses	1,124.2	1,263.0	1,303.4	1,436.0
Marketing Expenses	1,285.2	0.0	0.0	0.0
Administrative Expenses	1,086.0	63.2	93.1	90.7
Other expenses	1,214.0	2,954.5	2,992.5	3,476.7
Total Operating Expenditure	8,532.5	9,504.6	10,109.7	11,449.1
<b>EBITDA</b>	<b>2,759.8</b>	<b>2,864.3</b>	<b>3,271.3</b>	<b>3,755.9</b>
Growth (%)	22.8	3.8	14.2	14.8
Depreciation	346.8	316.4	334.5	338.8
Interest	112.0	119.8	126.6	143.0
Other Income	258.9	246.9	166.2	198.8
PBT	2,532.6	2,675.0	2,976.3	3,472.9
Others	103.7	0.0	0.0	0.0
Total Tax	822.0	705.4	750.0	875.2
<b>PAT</b>	<b>1,606.9</b>	<b>1,969.6</b>	<b>2,226.3</b>	<b>2,597.7</b>
Growth (%)	31.2	22.6	13.0	16.7
EPS (₹)	166.7	204.3	230.9	269.4

Source: Company, ICICI Direct Research

Exhibit 21: Cash flow statement				
	₹ crore			
(Year-end December)	CY18	CY19	CY20E	CY21E
Profit after Tax	1,606.9	1,969.6	2,226.3	2,597.7
Add: Depreciation	346.8	316.4	334.5	338.8
(Inc)/dec in Current Assets	-646.9	617.8	-551.7	-587.7
Inc/(dec) in CL	362.2	292.6	111.7	267.0
<b>CF from operating activities</b>	<b>1,669.0</b>	<b>3,196.2</b>	<b>2,120.8</b>	<b>2,615.9</b>
(Inc)/dec in LT loans & adv	6.2	-6.8	47.0	0.0
(Inc)/dec in other investments	-148.1	-10.2	-20.0	-20.0
(Inc)/dec in Fixed Assets	-142.2	-180.6	-477.6	-320.0
Others	110.1	401.0	299.6	100.0
<b>CF from investing activities</b>	<b>-162.6</b>	<b>194.8</b>	<b>-70.6</b>	<b>-240.0</b>
Issue/(Buy back) of Equity	0.0	0.0	0.0	0.0
Inc/(dec) in loan funds	0.0	18.0	0.0	0.0
Dividend paid & dividend tax	-1,313.4	-3,957.1	-2,207.5	-2,439.3
Inc/(dec) in Sec. premium	0.0	0.0	0.0	0.0
Others	-40.4	246.0	0.0	0.0
<b>CF from financing activities</b>	<b>-1,353.7</b>	<b>-3,693.0</b>	<b>-2,207.5</b>	<b>-2,439.3</b>
Net Cash flow	152.7	-302.0	-157.3	-63.4
Opening Cash	1,457.4	1,610.1	1,308.1	1,150.7
<b>Closing Cash</b>	<b>1,610.1</b>	<b>1,308.1</b>	<b>1,150.7</b>	<b>1,087.3</b>

Source: Company, ICICI Direct Research

Exhibit 22: Balance sheet				
	₹ crore			
(Year-end December)	CY18	CY19	CY20E	CY21E
<b>Liabilities</b>				
Equity Capital	96.4	96.4	96.4	96.4
Reserve and Surplus	3,577.3	1,835.8	1,854.6	2,013.0
Total Shareholders funds	3,673.8	1,932.3	1,951.0	2,109.4
Total Debt	35.1	53.1	53.1	53.1
Deferred Tax Liability	58.8	18.0	18.0	18.0
Long Term Provisions	2,464.9	2,906.9	3,206.9	3,306.9
<b>Total Liabilities</b>	<b>6,233.1</b>	<b>4,910.7</b>	<b>5,229.0</b>	<b>5,487.4</b>
<b>Assets</b>				
Gross Block	3,485.4	3,785.4	4,085.4	4,385.4
Less: Acc Depreciation	1,084.8	1,401.2	1,735.7	2,074.5
Net Block	2,400.6	2,226.7	2,349.7	2,310.9
Capital WIP	105.2	143.3	163.3	183.3
Total Fixed Assets	2,505.8	2,370.0	2,513.0	2,494.2
LT Loans & Advances	40.1	47.0	0.0	0.0
Inventory	965.6	1,283.1	1,384.7	1,656.5
Debtors	124.6	124.3	127.5	144.9
Loans and Advances	17.9	12.5	145.8	165.7
Current Investments	2,018.9	1,089.3	1,402.9	1,681.4
Cash	1,610.1	1,308.1	1,150.7	1,087.3
Total Current Assets	4,737.0	3,817.2	4,211.6	4,735.8
Creditors	1,240.4	1,494.7	1,457.5	1,656.5
Provisions	157.3	85.5	255.1	248.5
Other Current Liabilities	457.3	567.4	546.6	621.2
Total Current Liabilities	1,855.0	2,147.5	2,259.2	2,526.2
Net Current Assets	2,882.0	1,669.7	1,952.4	2,209.6
<b>Application of Funds</b>	<b>6,233.1</b>	<b>4,910.7</b>	<b>5,229.0</b>	<b>5,487.4</b>

Source: Company, ICICI Direct Research

Exhibit 23: Key ratios				
	₹ crore			
(Year-end December)	CY18	CY19	CY20E	CY21E
<b>Per share data (₹)</b>				
EPS	166.7	204.3	230.9	269.4
Cash EPS	202.6	237.1	265.6	304.6
BV	381.0	200.4	202.3	218.8
DPS	113.0	342.0	190.0	210.0
Cash Per Share	112.5	145.3	180.0	215.2
<b>Operating Ratios (%)</b>				
EBITDA Margin	24.4	23.2	24.4	24.7
PBT / Net Sales	21.7	21.8	22.4	23.0
PAT Margin	14.3	16.0	16.7	17.2
Inventory days	31.4	38.1	38.0	40.0
Debtor days	4.1	3.7	3.5	3.5
Creditor days	40.4	44.4	40.0	40.0
<b>Return Ratios (%)</b>				
RoE	45.6	101.9	114.1	123.1
RoCE	42.9	56.9	59.3	65.9
RoIC	53.4	70.4	75.0	81.0
<b>Valuation Ratios (x)</b>				
P/E	100.3	81.8	72.4	62.0
EV / EBITDA	57.8	55.8	48.9	42.6
EV / Net Sales	14.2	13.0	12.0	10.6
Market Cap / Sales	14.4	13.1	12.1	10.7
Price to Book Value	43.9	83.4	82.6	76.4
<b>Solvency Ratios</b>				
Debt/EBITDA	0.0	0.0	0.0	0.0
Debt / Equity	0.0	0.0	0.0	0.0
Current Ratio	1.7	1.2	1.4	1.4
Quick Ratio	1.2	0.6	0.7	0.8

Source: Company, ICICI Direct Research

**Exhibit 24: ICICI Direct coverage universe (FMCG)**

Sector / Company	CMP	TP	Rating	M Cap	EPS (₹)			P/E (x)			Price/Sales (x)			RoCE (%)			RoE (%)		
	(₹)	(₹)		(₹ Cr)	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E
Colgate (COLPAL)	1,341	1,430	Hold	36,990	28.5	30.6	32.6	47.0	43.8	41.1	8.3	8.0	7.4	70.7	75.5	82.9	52.2	59.7	65.1
Dabur India (DABIND)	446	550	Buy	86,947	8.9	9.9	10.9	50.1	44.9	40.8	9.6	8.8	8.1	30.2	29.9	30.6	25.9	26.7	27.2
Hindustan Unilever (HINLEV)	2,006	2,250	Hold	472,464	31.2	33.5	41.3	64.3	59.8	48.5	12.3	11.8	9.8	82.5	24.4	30.3	85.7	20.2	25.0
ITC Limited (ITC)	167	230	Buy	219,868	11.8	13.2	14.9	14.2	12.7	11.2	4.7	4.3	4.0	29.3	29.6	30.2	22.6	22.7	23.1
Jyothy Lab (JYOLAB)	105	110	Hold	4,113	5.3	3.2	4.4	20.0	32.8	24.1	2.3	2.2	2.0	28.6	18.6	23.9	22.6	14.0	18.5
Marico (MARLIM)	306	300	Hold	36,513	8.1	7.8	9.5	37.9	39.0	32.3	5.0	5.2	4.4	41.0	40.1	46.9	34.5	33.8	40.3
Nestle (NESIND)	16,711	18,000	Hold	161,127	204.3	230.9	269.4	81.8	72.4	62.0	13.1	12.1	10.7	56.9	59.3	65.9	101.9	114.1	123.1
Tata Global Bev (TATGLO)	356	375	Buy	17,986	8.3	9.4	10.7	42.9	37.9	33.2	2.4	1.8	1.6	8.9	8.4	9.3	7.1	6.5	7.1
VST Industries (VSTIND)	2,840	4,000	Buy	4,756	191.8	191.3	210.6	14.8	14.8	13.5	3.9	3.7	3.4	52.5	46.6	47.3	38.0	34.4	34.9
Varun Beverage (VARBEV)	641	580	Reduce	17,662	16.6	9.9	18.1	38.5	64.8	35.4	4.4	3.5	2.5	15.5	11.3	16.3	14.2	8.8	14.2

Source: Company, ICICI Direct Research

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Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



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