

Accumulate

Despite the magnitude and volatility of the Covid-19 Pandemic, Nestle India (NIL) delivered good sales growth of 8% in 2020. While in-home consumption categories (~85%) demonstrated strong growth; Out-of Home business was muted due to lockdown restrictions. In its Annual Report 2020, NIL reinforced commitment to 5 P's- Purpose, Planet, Partnerships, People and Performance; which helped the company navigate through unprecedented times. The company's continuous efforts to innovate new products and categories and high success rate compared to peers is the most encouraging prospect.

Strengthening distribution reach, enhanced focus on rural

NIL has been rapidly enhancing its distribution reach with a total reach of 4mn outlets in 2016 to 4.7mn outlets in 2020. Direct reach constitutes 30% of total distribution reach.

Rural and semi urban areas have shown greater resilience against the pandemic and performed better compared to metros and Tier I cities. Rural sales constitute 25% of company's topline. NIL plans to aggressively expand its footprint in the fast growing rural markets, with a target to reach 1.2 lakh villages (population of more than 5,000) by 2024. This would be augmented by distribution expansion, targeted products as well as campaigns. With active steps in last few years, the company was able to increase the villages covered from 1,000 in 2017 to 89,000 in 2019. These are serviced through +7K distributors and 2,780 wholesale hubs.

Huge scope for growth in packaged food industry

As per reports, India's packaged goods market is set to double from ~USD35 bn (Rs 2.6tn) currently, to USD70 bn in the next 5-10 years. This would be driven by rise in working age population, nuclearization, digitization and growing e-commerce. By 2030, India is likely to add almost 140 mn households to the middle and high income categories.

NIL is looking to invest Rs 26 bn over the next 3-4 years to augment its existing manufacturing capacities, apart from setting up new plant in Sanand, Gujarat. We believe Nestle is well positioned to cater to the rising demand for packaged food and drive further penetration, which will help it gain market share.

In-home consumption led to strong E-commerce growth

NIL has been rapidly increasing its E-com contribution (to domestic sales) from 0.6% in 2016 to 3.7% in 2020. The channel grew by 111% YoY in 2020. 75% of NIL's products such as Maggi, Kitkat, Maggi sauces, Nescafe Classic grew in double-digit in 2020, riding on strong in-home consumption. Going ahead, we believe E-com channel will continue to gain traction with increase in internet penetration and ease of online shopping.

Strong thrust on innovation

In the last 5 years, NIL had 80 new product launches with 70% success rate and it has 40-50 innovation projects in the pipeline. Over the last four years, contribution of new products to domestic sales has increased from 1.5% to 4.3%. Even during rapidly evolving times, Nestle continued to innovate and renovate and seven out of the eight Nestlé brands held number one position, according to Nielsen data. We believe that increasing pace of new launches and improvement in demand environment, is likely to help Nestle maintain strong growth momentum.

CMP	Rs 16,876
Target / Upside	Rs 17,667 / 5%
BSE Sensex	48,831
NSE Nifty	14,582

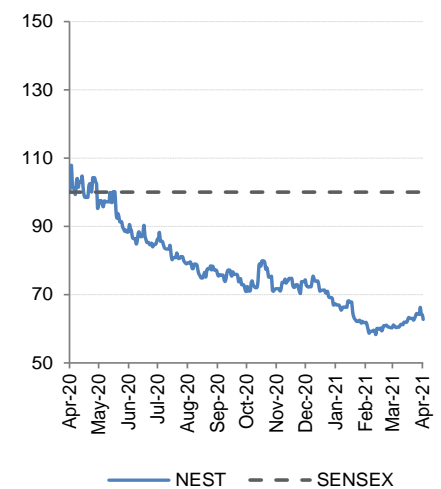
Scrip Details

Equity / FV	Rs 964mn / Rs 10
Market Cap	Rs 1,627bn
	US\$ 22bn
52-week High/Low	Rs18,844/Rs15,100
Avg. Volume (no)	1,20,798
NSE Symbol	NESTLEIND
Bloomberg Code	NEST IN

Shareholding Pattern Dec'20(%)

Promoters	62.8
MF/Banks/FIs	7.8
FII's	12.8
Public / Others	16.7

Company Relative to Sensex



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Annual Report Macro View

The BOD re-appointed Mr. Suresh Narayanan as Managing Director for another term of five consecutive years with effect from 1st August 2020.

Key Management

Mr. David S. McDaniel, Executive Director (Finance & Control) and CFO was appointed as a member of the Committee effective from 1st March 2020, replacing Mr. Shobinder Duggal.

Auditors

M/s B S R & Co. LLP continue to be the statutory auditors of the company since their appointment in May 2017.

Pledged Shares

No pledged shares.

Remuneration

There were 7,747 permanent employees on the rolls of the company in 2020. The median percentage increase in the salaries of employees other than the managerial personnel was 9.0%, while the increase in the remuneration of managerial personnel was 16.8%.

Credit Ratings

CRISIL has assigned AAA credit rating and A1+ credit rating for the company's long term and short-term bank credit facilities respectively. The rating reflects that the company has serviced its financial obligations on time.

Macroeconomic factors

Due to Covid-19 pandemic, Indian economy witnessed significant disruption with sluggish business activity and forced lockdowns impacting consumer demand. People curtailed discretionary spending and focused on essentials and precautionary savings due to the level of uncertainty. Consequently, in 2020, India's economy contracted by 8%. In 2020, the global economy contracted by 3.3%. The IMF projected an impressive 12.5% growth rate for India in 2021 with strong recovery in business activities and ramp up in vaccination drive. However, new lockdown related restrictions amidst rising Covid cases remain a concern.

	Category of Shareholder (%)	CY20	CY19
Key Holders	Promoter Holding	62.76	62.76
	Mutual Funds	3.81	4.13
	Banks/FI	0.02	0.11
	Insurance Companies	3.73	4.52
	Alternate Investment Fund	0.18	0.15
	NBFC	0.01	0.00
	Total DII	7.75	8.91
	FII/FPI	12.84	12.07
	Individuals	13.25	13.03
	Others	3.40	3.23
	Total	100.00	100.00

Source: Company, DART

Financial Analysis

Profit & Loss Analysis

- **Revenue-** Nestle's revenue grew 8% YoY to Rs 133.5bn in CY20. Domestic sales increased 8.5% YoY, led by volume and mix growth of 5.7%. Export sales grew 1.4% YoY (4.8% vol gr.), impacted by lower coffee exports. Demand in Out-of-Home channel was impacted throughout the year due to COVID-19 pandemic. NESCAFÉ, KITKAT, EVERYDAY, MAGGI noodles, MASALA-Ae-MAGIC outperformed and continued to be significant growth drivers.
- **Raw material costs** increased 8.6% YoY to Rs 56.7bn in CY20. Gross margins declined 30bps to 57.5%. Significant inflation in milk and SMP prices was partially mitigated by stable wheat and green coffee prices.
- **Operating expenses** – Employee cost (11.3% of net sales) stood at Rs 15.0 bn in CY20 as compared to Rs 12.6 bn in CY19, increasing 19.3% YoY. Advertising expenses (5.8% of net sales) de-grew 2.5% YoY to Rs 7.6bn.
- **Margins-** EBITDA increased 9.4% YoY to Rs 32.0bn in CY20. EBITDA margin expanded 30bps to 24.0%. While employee cost and RM cost grew 100bps and 30bps YoY, contraction of 60bps and 90bps in advertising and other expenses respectively helped margin performance.
- **Other income** declined significantly by 40.9% YoY to Rs 1.5bn due to lower yields and lower average liquidities.
- **Net Profit** – Net Profit jumped 5.8% YoY to Rs 20.8bn in CY20. Net profit margin stood at 15.7% as compared to 16.0% in CY19. EPS stood at Rs 216 in CY20 from Rs 204 in CY19.

DART View – Nestle posted impressive revenue performance in 2020 fueled by strong demand for packaged food during lockdown. We remain optimistic on Nestle's performance due to its strong supply chain, distribution initiatives, new innovative launches and focused marketing campaigns. However, two thirds of Nestle's business comes from urban. Hence, Out of Home category remains a concern due to new localized lockdowns restricting mobility. Better cost management and improved efficiency should help Nestle mitigate RM inflation and fetch EBITDA margins ~24-25%.

Balance Sheet and Cash Flow Analysis

- During CY20, the paid up **share capital** remained at Rs 964.2bn (96,415,716 shares of FV Rs 10 each). Total reserves stood at Rs 19.2bn in CY20 from Rs 18.2bn in CY19.
- **Dividend:** Over the years, Nestle has been consistent in its dividend distribution. The BOD has recommended a final dividend of Rs 65 per equity share amounting to Rs 6,267 mn for the year 2020 after the balance sheet date. Interim dividend of Rs 135 per share was paid in Nov'20. The total dividend paid in 2020 stands at Rs 18.9bn translating to dividend per share of Rs 196 with dividend payout of 90.7%.
- **Net block:** Net block increased to Rs 28.2bn in CY20 from Rs 24.8 bn in CY19, a growth of 13.4%. This translated to fixed asset turnover of 6.1x from 5.3x in CY19.
- **Capex** increased by 211% YoY, from Rs 1.5bn in CY19 to Rs 4.7bn in CY20. Capex to sales increased from 1.2% to 3.6% during the same period. The company is looking to invest Rs 26 bn over the next 3-4 years to augment its existing manufacturing capacities, as well as towards its new under

construction 'state of the art' factory in Sanand, Gujarat. This will help cater to soaring demand for packaged food.

- **Borrowing** decreased from Rs 531mn in CY19 to Rs 348mn in CY20. **Cash and bank balances** increased by 35.3% to `17.7 bn in CY20 as against Rs 13.1 bn in CY19.
- **Working capital:** Working Capital has been impacted due to coronavirus pandemic. Receivables increased by 32.7%, from Rs 1.2 bn in CY19 to `1,6 bn in CY20. Receivable days remained stable at 5 days. Trade payables grew 1.5% YoY to Rs 15.2 bn. Payable days reduced from 44 to 41 days. Inventory grew by 10.4% YoY Rs 14.1bn. Inventory days remained stable at 39 days while inventory turnover remained stable at 10x in CY20.
- **Return Ratios-** ROE increased from 70.4% in CY19 to 105.8% in CY20. The sharp increase is attributable to payment of special dividend of Rs 180 per share, out of accumulated profits in 2019. This had an impact on retained earnings of 2019 and 2020. Adjusted ROE for 2020 without considering the impact of special dividend is 51.3%.
- **Cash flow from operations** stood at Rs 28.8bn in CY20 from Rs 28.5bn in CY19. We believe that going forward, Nestle will generate cumulative OCF of Rs 64bn over CY21-22E, to suffice its capex and working capital requirement.

Exports

- In 2020, exports registered 4.8% volume growth, driven by categories such as Prepared Dishes and Cooking Aids, Milk Products and Nutrition.
- International markets witnessed growth mainly due to continued focus on MAGGI range extension and channel proliferation.
- Despite Covid-19 led disruptions, NIL recorded highest ever exports of MAGGI noodles and sauces to the United States, Canada, UK, European Union, Australia and New Zealand.
- Categories such as Coffee and Beverages were severely impacted by supply chain disruptions, lower coffee exports to Turkey and drop in Out-of-Home consumption.

Exhibit 1: Segment performance

Segments	Contribution %	Revenue (Rs bn)	Sales YoY %	Commentary
Milk Products & Nutrition	46	61.5	8.8	The segment continued to deliver good performance despite COVID-19 led disruptions and commodity price fluctuation.
Prepared dishes and cooking aids	29	39.1	11.8	To meet the growing demand during Covid, increased its production capacity and launched new varieties under the MAGGI portfolio. Maggi registered strong growth across its brands, strengthening its position as market leader. MAGGI Sauces registered double-digit growth and MAGGI Upma and Poha scaled up in volume and showcased strong presence in the Ready-to-Eat segment.
Powdered & Liquid beverages	11	14.8	(1.7)	Nescafe witnessed strong brand growth and significant market share gains led by focused marketing campaigns, premiumization and higher in-home consumption during lockdown.
Confectionary	13	17.5	6.7	With focus on innovations and new consumption opportunities, the segment demonstrated strong growth and gained market share amidst tough economic environment.

Source: Company, DART

New launches

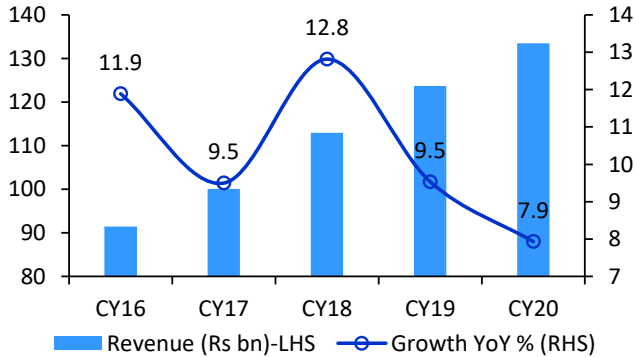
- Taking advantage of consumers experimenting in-home recipes, Maggi noodles launched new flavours such as Yummy Capsica and Chatpata Tomato and renovated Desi Cheesey.
- Nestle also launched MAGGI Atta Spinach noodles for consumers seeking both taste and nutritional benefits.
- The company launched MAGGI Fried Rice Masala and MAGGI Paneer-ae-Magic Shahi Paneer and Kadhai Paneer Masala mix.
- Nestle launched KOKO KRUNCH, a global cereal brand in 2020, and renovated NESPLUS with new packaging.
- Nestle continued to build a strong Toddler portfolio with the launch of LACTOGROW Toddler.
- The company also expanded its offerings in the weight management category by launching OPTIFAST vanilla flavor variant.
- In confectionery category, the company innovations across key brands, such as Nestlé POLO Extra Strong and Nestlé POLO Paan.
- With the objective to premiumize the beverages business portfolio, Roast & Ground (R&G) coffee was developed and launched.

Other Developments during the year

- The company accelerated its digital engagements across key parts of its portfolio and also extended AskNestlé 2.0 to Hindi, an intuitive mobile website, that provides real-time and personalized advice on nutrition.
- NIL activated emerging platforms and newer Route to Market (RTM) by partnering with hyperlocal delivery platforms within a month after lockdown in a few cities for the first time.
- Company's 'Out of Home' business initiated a programme called 'Nayi Shuruat' or 'New Beginnings'. NIL offered financial support in the form of credit period extensions, free goods, machine rental waivers and variable pay protection to its customers and partners.
- During COVID-19, NIL accelerated the invoicing platform and adopted paperless invoicing. Nearly 40% of invoices are managed digitally now.
- During 2020, The company rolled out NESTLÉ SAMMAN' programme for rewarding factory operators. It also launched NESTLÉ SURAKSHA' programme for front-line sales force, who work for distribution partners to cover those who were not covered by Employees' State Insurance, with a COVID-19 insurance protection.

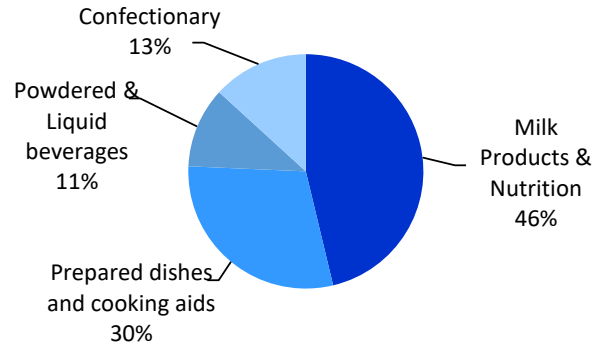
Financial Metrics and Charts

Exhibit 2: Net sales trend



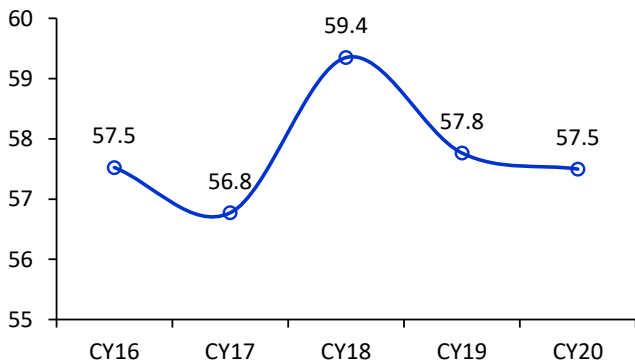
Source: Company, DART

Exhibit 3: Revenue contribution CY20



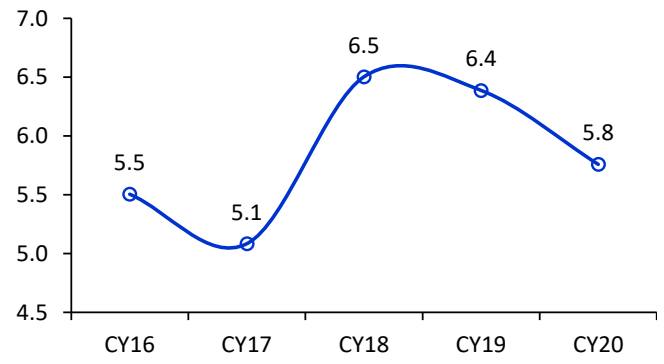
Source: Company, DART

Exhibit 4: Gross margin trend



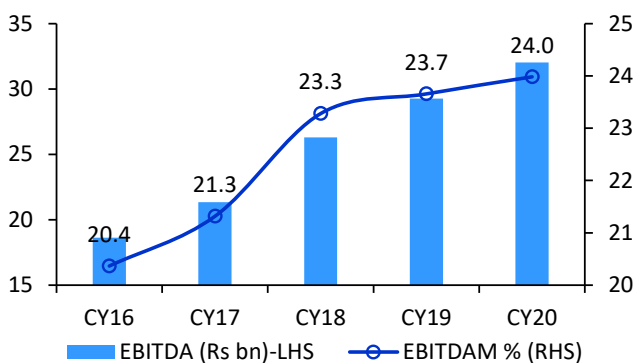
Source: Company, DART

Exhibit 5: Trend Advertising spends



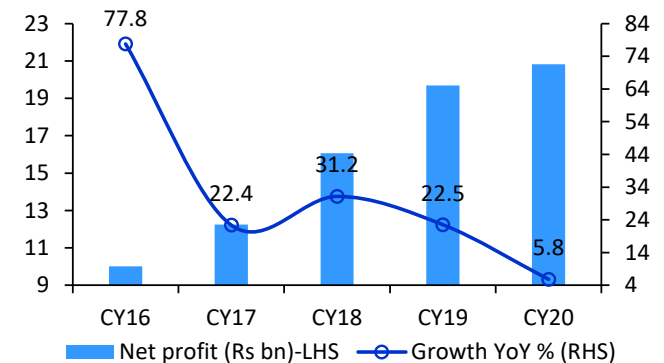
Source: Company, DART

Exhibit 6: EBITDA and EBITDA margin



Source: Company, DART

Exhibit 7: Net profit trend



Source: Company, DART

Profit and Loss Account

(Rs Mn)	CY19A	CY20A	CY21E	CY22E
Revenue	1,23,689	1,33,500	1,49,562	1,64,785
Total Expense	94,430	1,01,485	1,12,081	1,23,338
COGS	52,239	56,739	62,300	68,841
Employees Cost	12,582	15,010	16,811	18,155
Other expenses	29,609	29,737	32,971	36,342
EBIDTA	29,259	32,015	37,480	41,446
Depreciation	3,702	3,704	3,969	4,033
EBIT	25,557	28,311	33,511	37,413
Interest	1,291	1,642	1,806	1,987
Other Income	2,469	1,459	1,677	1,929
Exc. / E.O. items	0	0	0	0
EBT	26,735	28,128	33,383	37,356
Tax	7,050	7,304	8,402	9,402
RPAT	19,684	20,824	24,980	27,953
Minority Interest	0	0	0	0
Profit/Loss share of associates	0	0	0	0
APAT	19,684	20,824	24,980	27,953

Balance Sheet

(Rs Mn)	CY19A	CY20A	CY21E	CY22E
Sources of Funds				
Equity Capital	964	964	964	964
Minority Interest	0	0	0	0
Reserves & Surplus	18,225	19,229	24,929	33,603
Net Worth	19,189	20,193	25,894	34,567
Total Debt	531	348	348	348
Net Deferred Tax Liability	134	0	0	0
Total Capital Employed	19,854	20,542	26,242	34,915

Applications of Funds

Net Block	23,414	21,794	19,825	19,792
CWIP	1,433	6,385	9,385	12,385
Investments	7,436	7,408	7,408	7,408
Current Assets, Loans & Advances	38,641	42,314	47,846	58,618
Inventories	12,831	14,164	15,502	17,080
Receivables	1,243	1,649	1,632	1,798
Cash and Bank Balances	13,081	17,699	21,910	30,938
Loans and Advances	594	597	597	597
Other Current Assets	818	975	975	975
Less: Current Liabilities & Provisions	51,070	57,359	58,222	63,288
Payables	14,947	15,166	14,278	15,732
Other Current Liabilities	36,123	42,194	43,943	47,556
	<i>sub total</i>			
Net Current Assets	(12,429)	(15,045)	(10,376)	(4,670)
Total Assets	19,854	20,542	26,242	34,915

E – Estimates

Important Ratios

Particulars	CY19A	CY20A	CY21E	CY22E
(A) Margins (%)				
Gross Profit Margin	57.8	57.5	58.3	58.2
EBIDTA Margin	23.7	24.0	25.1	25.2
EBIT Margin	20.7	21.2	22.4	22.7
Tax rate	26.4	26.0	25.2	25.2
Net Profit Margin	15.9	15.6	16.7	17.0
(B) As Percentage of Net Sales (%)				
COGS	42.2	42.5	41.7	41.8
Employee	10.2	11.2	11.2	11.0
Other	23.9	22.3	22.0	22.1
(C) Measure of Financial Status				
Gross Debt / Equity	0.0	0.0	0.0	0.0
Interest Coverage	19.8	17.2	18.6	18.8
Inventory days	38	39	38	38
Debtors days	4	5	4	4
Average Cost of Debt	292.5	373.3	518.7	570.5
Payable days	44	41	35	35
Working Capital days	(37)	(41)	(25)	(10)
FA T/O	5.3	6.1	7.5	8.3
(D) Measures of Investment				
AEPS (Rs)	204.2	216.0	259.1	289.9
CEPS (Rs)	242.5	254.4	300.2	331.7
DPS (Rs)	368.8	196.0	200.0	200.0
Dividend Payout (%)	180.7	90.7	77.2	69.0
BVPS (Rs)	199.0	209.4	268.6	358.5
RoANW (%)	70.4	105.8	108.4	92.5
RoACE (%)	72.9	111.2	114.5	97.9
RoAIC (%)	180.3	588.8	934.1	900.5
(E) Valuation Ratios				
CMP (Rs)	16876	16876	16876	16876
P/E	82.7	78.1	65.1	58.2
Mcap (Rs Mn)	16,27,155	16,27,155	16,27,155	16,27,155
MCap/ Sales	13.2	12.2	10.9	9.9
EV	16,04,531	16,02,575	15,98,364	15,89,336
EV/Sales	13.0	12.0	10.7	9.6
EV/EBITDA	54.8	50.1	42.6	38.3
P/BV	84.8	80.6	62.8	47.1
Dividend Yield (%)	2.2	1.2	1.2	1.2
(F) Growth Rate (%)				
Revenue	9.5	7.9	12.0	10.2
EBITDA	11.3	9.4	17.1	10.6
EBIT	12.0	10.8	18.4	11.6
PBT	10.1	5.2	18.7	11.9
APAT	22.5	5.8	20.0	11.9
EPS	22.5	5.8	20.0	11.9
Cash Flow				
(Rs Mn)	CY19A	CY20A	CY21E	CY22E
CFO	28,449	28,815	28,491	35,308
CFI	5,584	(4,163)	(5,000)	(7,000)
CFF	(35,417)	(19,109)	(19,280)	(19,280)
FCFF	24,959	21,779	23,491	28,308
Opening Cash	16,101	13,081	17,699	21,910
Closing Cash	13,081	17,699	21,910	30,938

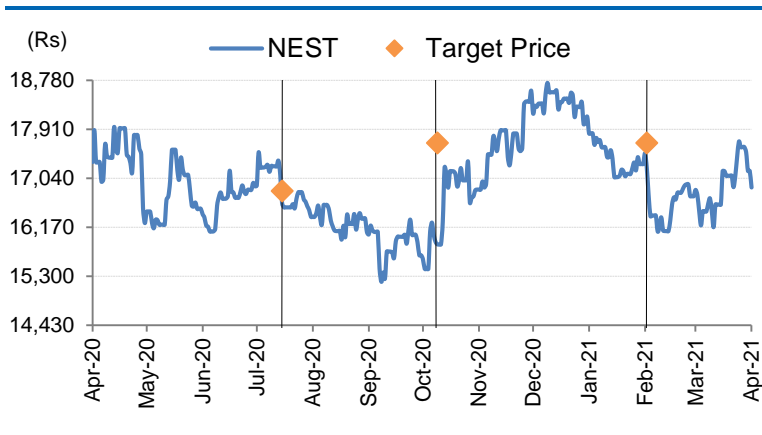
E – Estimates

DART RATING MATRIX

Total Return Expectation (12 Months)

Buy	> 20%
Accumulate	10 to 20%
Reduce	0 to 10%
Sell	< 0%

Rating and Target Price History



Month	Rating	TP (Rs.)	Price (Rs.)
Jul-20	Reduce	16,813	16,598
Oct-20	Accumulate	17,667	15,865
Feb-21	Accumulate	17,667	17,217

*Price as on recommendation date

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