Stock Update

Result Update

Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Nestle India Ltd

Strong quarter

Consumer Goods	Sharekhan code: NESTLEIND
Reco/View: Buy ↔	CMP: **Rs. 20,663** / Price Target: **Rs. 22,990** ↑

↑ Upgrade ↔ Maintain ↓ Downgrade

3R MATRIX	+	=	-
Right Sector (RS)		✓	
Right Quality (RQ)	✓		
Right Valuation (RV)	✓		

\+ Positive = Neutral – Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↔	

ESG Disclosure Score NEW

ESG RISK RATING 28.28

Updated Mar 08, 2023

Medium Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

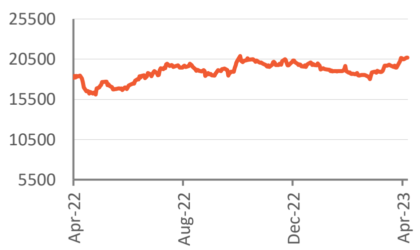
Company details

Market cap:	Rs. 1,99,224 cr
52-week high/low:	Rs. 21,053 / 16,000
NSE volume: (No of shares)	0.6 lakh
BSE code:	500790
NSE code:	NESTLEIND
Free float: (No of shares)	3.6 cr

Shareholding (%)

Promoters	62.8
FII	13.0
DII	9.2
Others	15.1

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	9.4	7.4	1.9	13.7
Relative to Sensex	5.1	7.5	0.9	7.4

Sharekhan Research, Bloomberg

Summary

- Nestle India Limited (Nestle) posted strong performance in Q1CY23 ahead of expectation. Revenues grew by 21.3% y-o-y to Rs. 4,830.5 crore; OPM declined by 55 bps y-o-y to 22.7% and PAT grew by 23.9% y-o-y to Rs. 736.7 crore.
- Domestic volumes recovered sequentially to mid-single digit (4-5% in Q1); excluding Maggi low unit packs, volume growth stood in low double digits. We expect volume growth momentum to sustain in the quarters ahead.
- A surge in milk and green coffee prices will keep pressure on the margins in the near term. Softening of edible oil, packaging material and wheat prices from highs might provide a breather in H2.
- Stock trades at 66.0x, 57.0x and 47.8x its CY2023E, CY2024E and CY2025E EPS, respectively. We maintain a Buy on the stock with a revised PT of Rs. 22,990.

Nestle India Limited (Nestle) registered yet another quarter of strong performance with revenues and PAT growing by 21% and 24%, respectively, in Q1CY2023 well ahead of ours as well as the street's expectation. Revenues grew by 21.3% y-o-y to Rs. 4,830.5 crore (ahead of our expectation of Rs. 4,448.2 crore), driven by a 21% growth in the domestic business, which was largely price-led growth with sales volumes growing by mid-single digit. Domestic sales volume saw sequential improvement. However, excluding Maggi small packs, the volume growth stood in low double-digits during the quarter. Higher raw-material prices led to a 159-bps y-o-y decline in gross margin to 53.8%. OPM decreased by 55 bps y-o-y to 22.7%. The operating profit grew by 18.5% y-o-y to Rs. 1,096 crore. This along with 57% y-o-y growth in other income led to 24% growth in PAT to Rs. 736.7 crore (ahead of our expectation of Rs. 641.6 crore).

Key positives

- All key categories, including milk food, chocolate, beverages, and prepared dishes, registered double-digit growth in Q1CY2023.
- Export sales grew by 25% y-o-y.
- Domestic volume growth recovered to 4-5% vs. negative 1% in Q4.

Key negatives

- Gross margin decreased by 159 bps y-o-y to 53.8% due to raw material inflation.
- Sale of Maggi lower-unit packs moderated due to significant price hike.

Management Commentary

- Nestle delivered broad-based double-digit growth across all its business verticals in Q1CY2023.
- Rural growth was strong, secular and robust, being volume led which is on back of the company's strong efforts to expand its distribution reach in the rural markets. Strong growth in RURBAN was complemented by strong momentum in metro and mega cities.
- The company is witnessing early signs of softening in the commodities such as edible oils, wheat and packaging materials. On the other hand, fresh milk, fuel and green coffee prices have increased and are expected to remain firm in the near term.

Revision in estimates – We have fine-tunned our earnings estimates for CY2023, CY2024 and CY2025 to factor in better than expected operating performance in Q1CY2023.

Our Call

View: Retain Buy with a revised PT of Rs. 22,990 – Nestle's strong positioning in the domestic food market, innovative product portfolio, and improving out-of-home consumption with a thrust on improving penetration in rural markets will help it drive consistent double-digit earnings growth in the long run. The company is supporting its consistent growth agenda by higher investments in capacity enhancement, strong brand support, and better R&D initiatives. The stock is currently trading at 66.0x and 57.0x its CY2023E and CY2024E earnings, respectively. We maintain our Buy rating on the stock with a revised price target (PT) of Rs. 22,990.

Key Risks

Any slowdown in domestic consumption or regulatory hurdles in key food categories or an increase in key input prices would act as a key risk to our earnings estimates.

Valuation (Standalone) Rs cr

Particulars	CY21	CY22	CY23E	CY24E	CY25E
Revenue	14,741	16,897	19,554	21,962	25,019
OPM (%)	24.2	22.0	22.8	23.6	24.7
Adjusted PAT	2,293	2,391	3,019	3,497	4,169
% YoY growth	*10.1*	*4.2*	*26.3*	*15.8*	*19.2*
Adjusted EPS (Rs.)	237.9	247.9	313.1	362.6	432.3
P/E (x)	86.9	83.3	66.0	57.0	47.8
P/B (x)	-	81.0	73.0	64.4	53.2
EV/EBIDTA (x)	55.7	53.5	44.6	38.5	32.2
RoNW (%)	115.7	108.5	116.4	120.1	122.0
RoCE (%)	141.2	129.2	135.5	138.9	142.3

Source: Company; Sharekhan estimates

Revenue and PAT growth over 20% y-o-y; Margins lower y-o-y impacted by milk inflation

Revenues grew by 21.3% y-o-y to Rs. 4,830.5 crore in Q1CY2023, driven by 22% y-o-y growth in the domestic business to Rs. 4,613 crore and 24.9% y-o-y growth in the export business to Rs. 196 crore. Domestic revenue growth was driven by a balance of pricing, volume, and mix led growth during the quarter. As per media reports, volume growth stood at 4-5%, slightly better than our as well as street expectation of 3-4%. However, the management has indicated that the company's volume growth ex-Maggi small packs is higher at low double-digits. Gross margin was down by 160 bps y-o-y to 53.8%, impacted by higher inflation in milk and other commodity prices, while OPM declined by 55 bps y-o-y to 22.7%. Operating profit grew by 18.5% y-o-y to Rs. 1,096 crore. This coupled with higher other income (higher 57% y-o-y to Rs. 33.7 crore) resulted in 23.9% y-o-y growth in the reported PAT to Rs. 736.7 crore.

Double-digit growth across all product groups in last four quarters

All the company's product groups delivered double-digit growth for four quarters in a row.

- Prepared Dishes and Cooking Aids delivered strong growth across all products in its food portfolio aided by market presence, media campaigns and focussed consumer activations.
- Milk Products and Nutrition registered strong double-digit growth led by MILKMAID among others, despite commodity pressures. GERBER Cereals and CEREGROW Grain Selection performed well. Nestle launched ThickenUp Clear, a food and beverage thickener in Q1CY2023. ThickenUp Clear can be used to help patients with swallowing difficulties.
- Confectionery displayed robust growth led by KITKAT and MUNCH supported by focused trade plans, consumer-led campaigns, innovation and strong consumer engagement.
- Beverages delivered another quarter of robust growth and market share gains led by NESCAFÉ Classic, NESCAFÉ Sunrise, and NESCAFÉ GOLD. NESCAFÉ recorded its highest ever market share. NESCAFÉ RTD and out-of-home also delivered strong growth.
- Pet Food continued to build on its momentum and launched a new product within its cat portfolio.

Growth across all channels in Q1CY2023

- The e-Commerce channel delivered strong performance in Q1CY2023 with significant growth in quick commerce.
- The organized trade channel witnessed broad based growth across product groups in retail business fuelled by rapid outlet expansion.
- The Out-of-Home (OOH) channel posted strong performance aided by growth across brands, geographies, and channels.
- Exports registered strong double-digit growth through both mainstream and ethnic channels.

RURBAN continued to deliver

The company accelerated its sustained growth journey in RURBAN areas, where growth was complemented by strong momentum in metro and mega cities. Rural growth was also strong, secular and robust, being volume-led.

Results (Standalone) Rs cr

Particulars	Q1CY23	Q1CY22	Y-o-Y %	Q4CY22	Q-o-Q %
Total Revenue	**4,830.5**	**3,980.7**	**21.3**	**4,256.8**	**13.5**
Raw Material Cost	2,231.5	1,775.7	25.7	1,921.5	16.1
Employee Cost	454.3	396.6	14.5	406.5	11.7
Other Expenses	1,049.3	883.7	18.7	955.4	9.8
Total Operating Cost	3,735.1	3,056.1	22.2	3,283.3	13.8
Operating Profit	**1,095.5**	**924.7**	**18.5**	**973.5**	**12.5**
Other Income	33.7	21.4	57.1	29.6	14.0
PBIDT	1,129.2	946.1	19.4	1,003.0	12.6
Interest & Other Financial Cost	37.0	35.6	4.0	44.8	-17.5
Depreciation	101.7	104.3	-2.5	98.7	3.1
Profit Before Tax	990.5	806.2	22.9	859.5	15.2
Tax Expense	253.8	211.5	20.0	231.0	9.9
Adjusted PAT	**736.7**	**594.7**	**23.9**	**628.5**	**17.2**
Adj. EPS (Rs)	76.4	61.7	23.9	65.2	17.2
			bps		**bps**
GPM (%)	53.8	55.4	-159	54.9	-106
OPM (%)	22.7	23.2	-55	22.9	-19
NPM (%)	15.2	14.9	31	14.8	48
Tax rate (%)	25.6	26.2	-61	26.9	-125

Source: Company; Sharekhan Research

Outlook and Valuation

■ Sector Outlook – Rural recovery key for revival in the volume growth

A recovery in rural demand is key for consumer goods companies to post recovery in volume growth in quarters ahead. A normal monsoon, well spread across the country and government support (especially prior to elections) might help rural demand gradually pick up. In terms of categories, out-of-home, packaged foods and edible oil categories are likely to maintain good momentum in the coming quarters. With mercury expected to rise in most parts of the country, demand for summer products is on the rise as trade channels are building up the inventory prior to the season. On the margin front, stable raw material prices post the recent correction in some of the key inputs (including crude oil & vegetable oils) will help margins consistently improve in the coming quarters. Low penetration in key categories (especially in rural India), lower per capita consumption compared with other countries, a large shift to branded products, and emergence of new channels such as e-commerce/D2C provide several opportunities for achieving sustainable growth in the medium to long run.

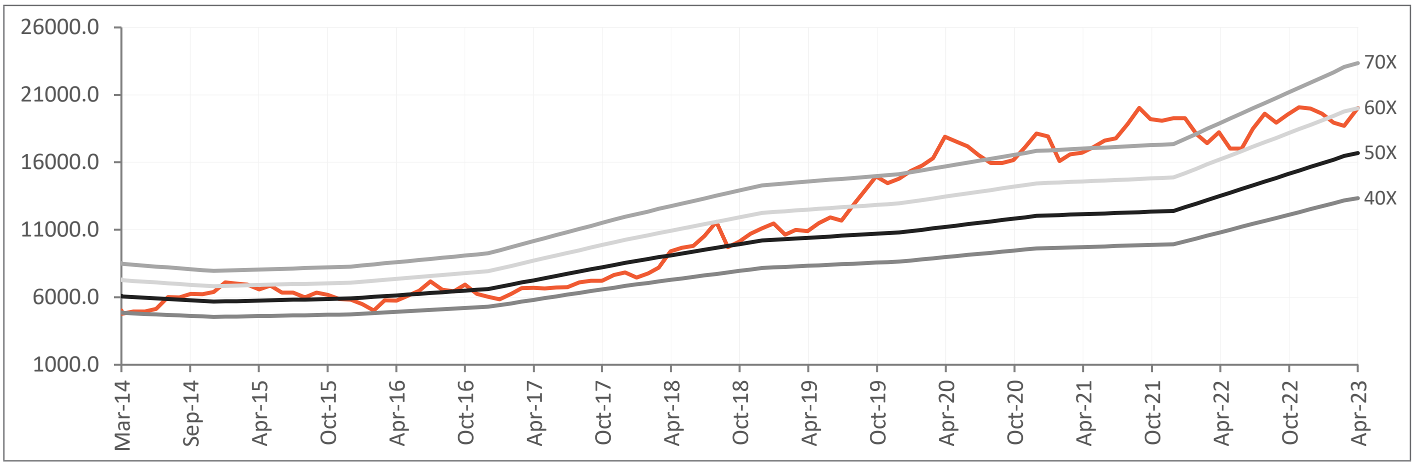
■ Company Outlook – Focusing on achieving consistent growth

Nestle started CY2023 on strong note with revenues and PAT growing in upwards of 20%. Sales volume growth improved to mid-single digit sequentially and is expected to consistently improve in the coming quarters. The company is focusing on consistent growth through innovations (5.4% of domestic revenues), expanding in rural/tier 2 markets, and accelerating footprints through new channels. It has achieved 80% of the target village coverages of 1,20,000 villages. Raw-material inflation stood at high single digit for the company. Nestle will continue to safeguard OPM through 1) better revenue mix, 2) benefits from Project Shark (1.5% of net sales in CY2021), and 3) leveraging on operating efficiencies and cost savings and judicious pricing actions. The change in the pension plan would lead to savings at employee cost level, adding to OPM.

■ Valuation – Retain Buy with revised price target of Rs. 22,990

Nestle's strong positioning in the domestic food market, innovative product portfolio, and improving out-of-home consumption with a thrust on improving penetration in rural markets will help it drive consistent double-digit earnings growth in the long run. The company is supporting its consistent growth agenda by higher investments in capacity enhancement, strong brand support, and better R&D initiatives in the coming years. The stock is currently trading at 66.0x and 57.0x its CY2023E and CY2024E earnings, respectively. We maintain our Buy rating on the stock with a revised price target (PT) of Rs. 22,990.

One-year forward P/E (x) band



Source: Sharekhan Research

Peer Comparison

Particulars	P/E (x)			EV/EBITDA (x)			RoCE (%)		
	FY23	FY24E	FY25E	FY23	FY24E	FY25E	FY23	FY24E	FY25E
HUL	61.2	51.7	44.1	42.7	36.3	31.0	25.9	30.1	33.4
Britannia Industries	54.9	47.9	41.0	39.3	34.5	29.6	36.1	36.8	36.9
Nestle India*	83.3	66.0	57.0	53.5	44.6	38.5	129.2	135.5	138.9

*Source: Company, Sharekhan estimates; *Nestle is a calendar year ending company*

About company

Nestle is the largest food company in India with a turnover of ~Rs. 17,000 crore. The company is present across India with nine manufacturing facilities, four branch offices, one R&D centre, and approximately 8,000 employees. The company manufactures products under international famous brand names such as Nescafé, Maggi, Milkybar, KitKat, Bar-One, Milkmaid, and Nestea; and in recent years, the company has introduced products of daily consumption and use such as Nestle Milk and Nestle Slim Milk. Nestle has a diversified portfolio of brands divided into four segments: Milk Products and Nutrition, Prepared Dishes and Cooking Aids, Confectionery, and Beverages. The brands are broadly segregated on the basis of nutrition, health, comfort, variety, indulgence, and taste. Nestle is the market leader in the categories of 'Instant Noodles' and 'Infant Cereals & Infant Formula'.

Investment theme

Nestle has maintained its leadership position across key categories over the years. The company had faced a setback in CY2015 post the Maggi debacle; however, it bounced back within a short span of time by re-launching the product with the help of innovative media campaigns. Sustained innovation, premiumisation, enhancing of distribution reach, and adoption of the cluster-based distribution approach would be the key growth drivers for the company in the near to medium term. A strong return profile, future growth prospects, and good dividend payout make it a better pick in the FMCG space.

Key Risks

- **Slowdown in demand environment:** Any slowdown in demand, especially in international markets, would affect sales of key categories, resulting in moderation of sales volume growth.
- **Increased competition in highly penetrated categories:** Increased competition in highly penetrated categories such as instant noodles, instant coffee, and infant cereals would act as a threat to revenue growth.
- **Increased input prices:** Any significant increase in the prices of some key raw materials such as milk would affect profitability and earnings growth.

Additional Data

Key management personnel

Suresh Narayanan	Chairman & Managing Director
David McDaniel	Executive Director - Finance and Control and CFO
Pramod Kumar Rai	Company Secretary and Compliance Officer

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Life Insurance Corp of India	2.44
2	Axis Asset Management Co.Ltd	1.49
3	Vanguard Inc	1.49
4	BlackRock Inc	1.45
5	SBI Funds Management	1.26
6	UTI Asset Management Co Ltd	0.69
7	Veritas AMC	0.41
8	Norges Bank	0.31
9	SBI Pension Funds Pvt Ltd	0.31
10	Credit Agricole Group	0.28

Source: Bloomberg

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

Sharekhan

by BNP PARIBAS

Know more about our products and services

For Private Circulation only

Compliance Officer: Ms. Binkle Oza; Tel: 022-61169602; email id: complianceofficer@sharekhan.com;

For any queries or grievances kindly email igc@sharekhan.com or contact: myaccount@sharekhan.com.

Registered Office: Sharekhan Limited, The Ruby, 18th Floor, 29 Senapati Bapat Marg, Dadar (West), Mumbai – 400 028, Maharashtra, INDIA, Tel: 022 - 67502000/ Fax: 022 - 24327343. Sharekhan Ltd.: SEBI Regn. Nos.: BSE / NSE / MSEI (CASH / F&O/ CD) / MCX - Commodity: INZ000171337; DP: NSDL/CDSL-IN-DP-365-2018; PMS: INP000005786; Mutual Fund: ARN 20669; Research Analyst: INH000006183.