REDUCE

Nestlé India

Growth slump a concern; downgrade to REDUCE

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Consumer Goods ▸ Result Update ▸ **October 17, 2024**

TARGET PRICE (Rs): 2,400

We downgrade Nestlé India to REDUCE from Add with a 14.3% cut in TP to Rs2,400 amid sustained topline pressures; our target valuation multiple reduces to 60x (~10% discount to last 5Y avg. fwd. P/E of 67x). Q2 result was weaker than street and our expectations, wherein sales growth was 1% (5% below expectations) and adjusted earnings declined 9% (14% below expectations). EBITDA margin saw 150bps YoY contraction amid surge in A&P spends; gross margin remained steady at 56%. Amid inflationary stress, Nestlé India's core categories saw demand pressure. Factoring in muted topline show in 1H, we lower revenue expectations by 3% over FY25-27. We cut our earnings 8% for FY25E and ~3% over FY26-27E. The recent stock correction has priced in near-term pressure, reflecting in 1Y fwd P/E at 62x near -1 SD (5Y avg).

Nestlé India: Financial Snapshot (Standalone)

Y/E Mar (Rs mn)	CY22	FY24	FY25E	FY26E	FY27E
Revenue	168,970	243,939	202,482	223,930	247,235
EBITDA	37,583	58,490	48,064	54,892	61,633
Adj. PAT	24,362	39,577	31,842	36,834	40,820
Adj. EPS (Rs)	25.3	32.8	33.0	38.2	42.3
EBITDA margin (%)	22.2	24.0	23.7	24.5	24.9
EBITDA growth (%)	5.3	24.5	2.7	14.2	12.3
Adj. EPS growth (%)	3.3	30.0	0.6	15.7	10.8
RoE (%)	107.2	109.2	82.3	84.6	96.4
RoIC (%)	67.5	88.6	86.2	85.9	107.7
P/E (x)	94.1	72.4	72.0	62.3	56.2
EV/EBITDA (x)	60.7	39.1	47.5	41.7	36.9
P/B (x)	93.3	85.8	52.2	53.1	55.2
FCFF yield (%)	0.9	2.7	1.1	1.4	2.6

Source: Company, Emkay Research

Demand slump concerning; Q2 revenue grew 1% with 1.5% decline in volume

Contrary to expectation of sequential performance improvement, Nestle India reported growth moderation to 1%, which implies volume decline of 1.5% in Q2FY25. Inflation pressure (in all major commodities – Milk, Cocoa, Coffee, and Palm oil) led to steady price hikes in the portfolio, which has started affecting sales growth. As per the management commentary, revenue pressure seems to be high for formula milk and instant noodles. New launches in the last eight years have sales contribution of 7%, it has eight innovation in the pipeline. The company has launched a new variant in noodles (Chatpata Besan) and will be launching Cerelac variants with no refined sugar (7 in Nov-24); among the 21 variants, 14 will be with no refined sugar. The company continues to leverage opportunity in the e-commerce channel (grew 38% YoY), where share of revenue expanded to 8.3% of domestic sales in Q2FY25 from 7.5% in Q1.

High A&P spends caused 150bps compression in EBITDA margin

Gross margin at 56.4%, expanded by 10bps YoY, but contracted by 110bps QoQ. Management noted inflationary stress from cocoa and coffee, and noted concern on elevated edible oil prices. Milk and packaging prices are likely to be stable ahead. We see any further inflation to be detrimental to its growth, given >20% cumulative price hikes in the last couple of years. EBITDA margin contracted by 150bps YoY, affected primarily by higher A&P spends in the business. EBITDA declined 5% YoY, while other income reduced 79% YoY amid lower liquidity, leading to earnings falling 8% YoY.

Recent correction factors near-term stress, valuation elevated on its strengths

Nestlé India's elevated valuations has been a factor of execution prowess, price power, strong parentage, and healthy return profile. We see that the recent correction is factoring in business pressures, its 1Y fwd P/E at 62x is at -1 SD 5Y historical average. We cut Sep-25E TP from Rs2,800 to Rs2,400, as we lower earnings by 3% and multiple to 60x (from 67x). We downgrade stock to REDUCE as we see the stock as fairly valued.

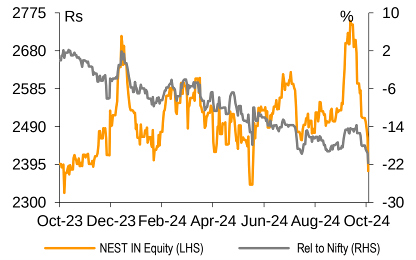
Target Price – 12M	Sep-25
Change in TP (%)	**(14.3)**
Current Reco.	REDUCE
Previous Reco.	ADD
Upside/(Downside) (%)	0.9
CMP (17-Oct-24) (Rs)	2,378.7

Stock Data	NEST
52-week High (Rs)	2,778
52-week Low (Rs)	2,310
Shares outstanding (mn)	964.2
Market-cap (Rs bn)	2,293
Market-cap (USD mn)	27,281
Net-debt, FY25E (Rs mn)	-8,998
ADTV-3M (mn shares)	1
ADTV-3M (Rs mn)	2,733.1
ADTV-3M (USD mn)	32.5
Free float (%)	37.2
Nifty-50	24,750
INR/USD	84.1
Shareholding, Jun-24	
Promoters (%)	62.8
FPIs/MFs (%)	11.9/9.2

Price Performance

(%)	1M	3M	12M
Absolute	(6.6)	(8.8)	2.0
Rel. to Nifty	(4.1)	(9.3)	(18.4)

1-Year share price trend (Rs)



Nitin Gupta
nitin.gupta@emkayglobal.com
+91 22 6612 1257

Pinky Mahato
pinky.mahato@emkayglobal.com
+91 22 6612 1306

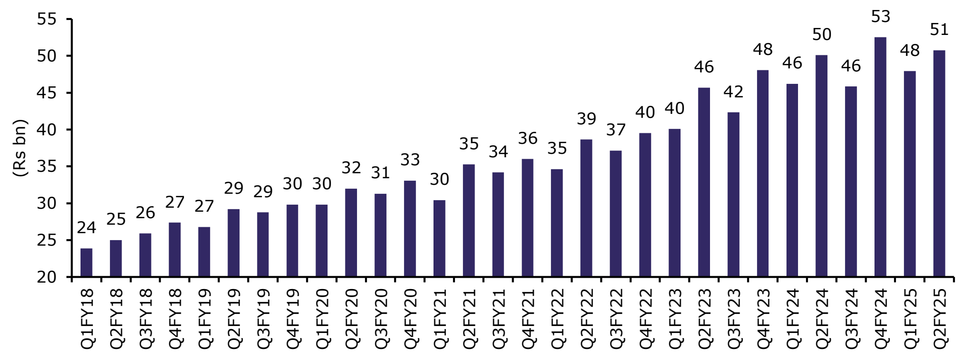
Quarterly performance

Exhibit 1: Q2FY25 Quarterly performance

(Rs mn)	2QFY25	2QFY24	YoY (%)	1QFY25	QoQ (%)	2QFY25E	Var (%)
Total income	**51,040**	**50,368**	**1.3**	**48,140**	**6.0**	**53,716**	**(5.0)**
Cost of goods	22,139	21,916	1.0	20,388	8.6	22,964	(3.6)
Employee expenses	5,017	5,176	(3.1)	5,054	(0.7)	5,500	(8.8)
Other expenses	12,207	10,989	11.1	11,674	4.6	12,088	1.0
EBITDA	**11,677**	**12,287**	**(5.0)**	**11,023**	**5.9**	**13,165**	**(11.3)**
EBITDAM (%)	22.9	24.4	-150bps	22.9	0bps	24.5	-160bps
Depreciation	1,216	1,112	9.4	1,127	7.9	1,200	1.3
EBIT	**10,461**	**11,176**	**(6.4)**	**9,896**	**5.7**	**11,965**	**(12.6)**
EBITM (%)	20.5	22.2	-170bps	20.6	-10bps	22.3	-180bps
Interest cost	322	314	2.7	317	1.7	300	7.4
Other income	69	333	(79.4)	391	(82.5)	375	(81.7)
PBT	**10,208**	**11,195**	**(8.8)**	**9,971**	**2.4**	**12,040**	**(15.2)**
Tax	3,252	3,139	3.6	2,625	23.9	3,070	5.9
Tax rate (%)	31.9	28.0	380bps	26.3	550bps	25.5	640bps
Non-recurring items	2,908	1,026	183.5	120	2323.5	(150)	(2038.8)
PAT	**9,864**	**9,081**	**9**	**7,466**	**32.1**	**8,820**	**11.8**
Adj Profit	**7,882**	**8,343**	**(5.5)**	**7,378**	**6.8**	**8,931**	**(11.7)**
NPM (%)	15.4	16.6	-110bps	15.3	10bps	16.6	-120bps
EPS (Rs)	8.0	8.6	(7.7)	7.7	4.1	9.3	-14.0

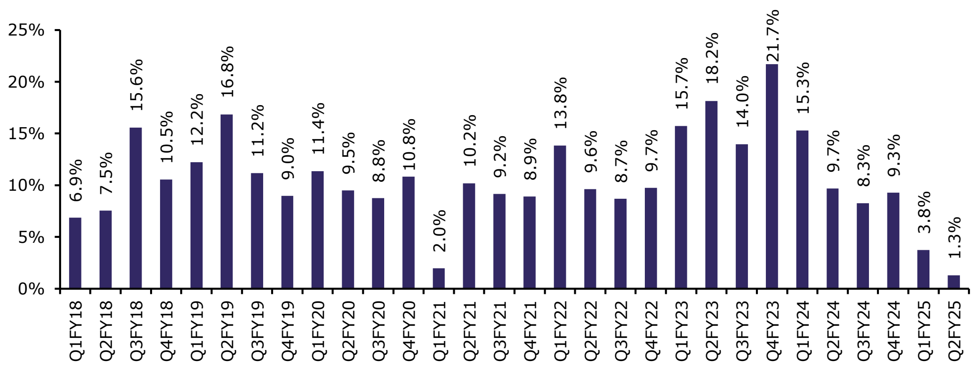
Source: Company, Emkay Research

Exhibit 2: Nestlé revenue



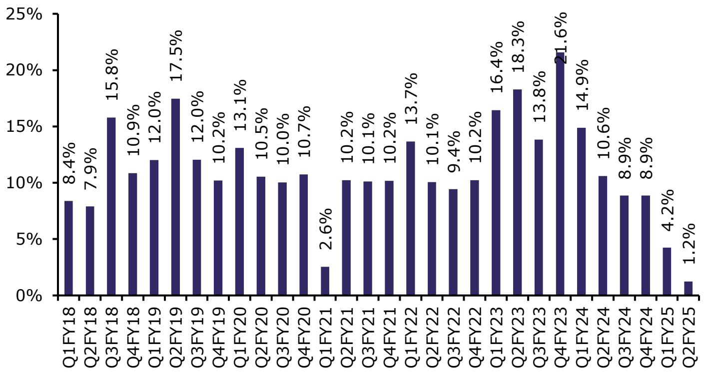
Source: Company, Emkay Research

Exhibit 3: Nestlé revenue growth (YoY)



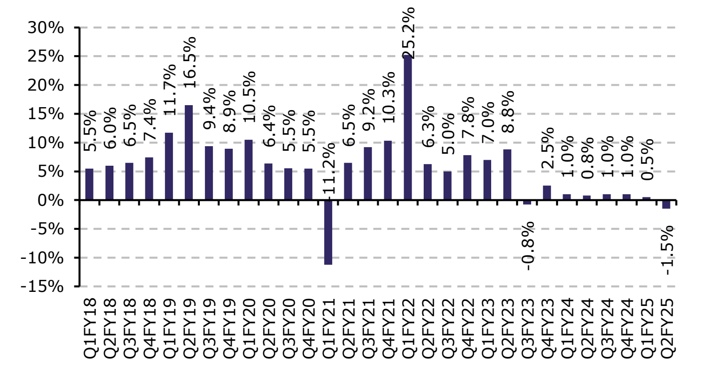
Source: Company, Emkay Research

Exhibit 4: Domestic revenue growth



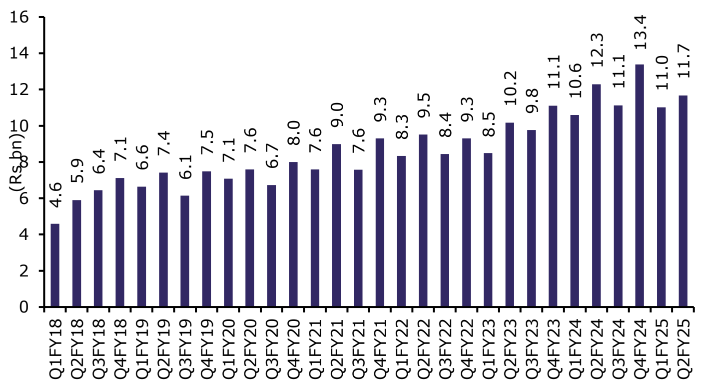
Source: Company, Emkay Research

Exhibit 5: Domestic volume growth



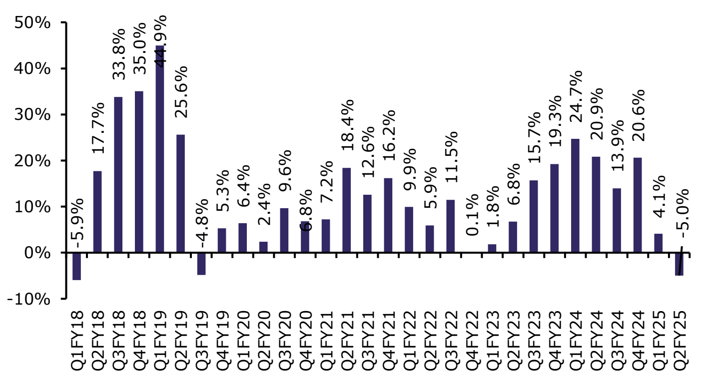
Source: Company, Emkay Research

Exhibit 6: Nestlé EBITDA



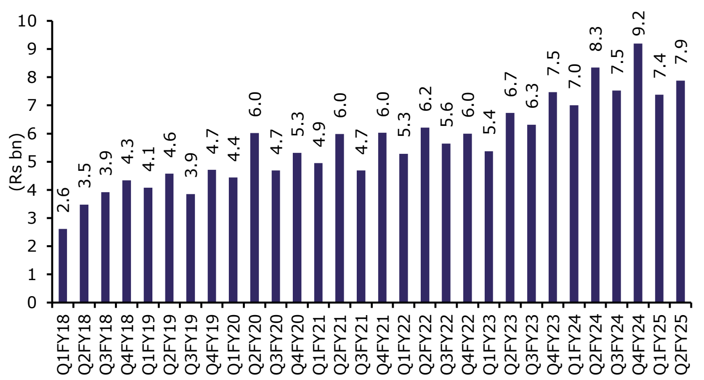
Source: Company, Emkay Research

Exhibit 7: Nestlé EBITDA growth



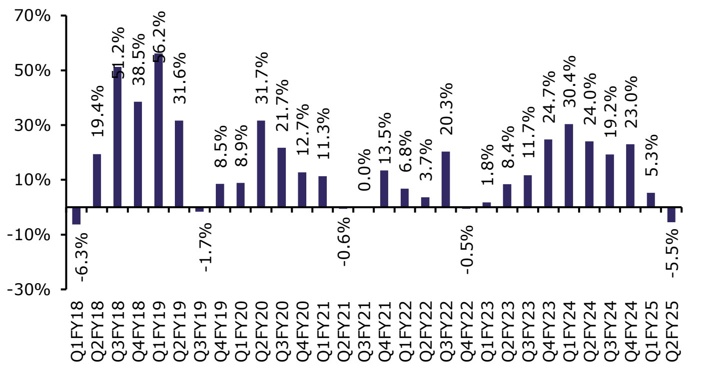
Source: Company, Emkay Research

Exhibit 8: Adjusted PAT



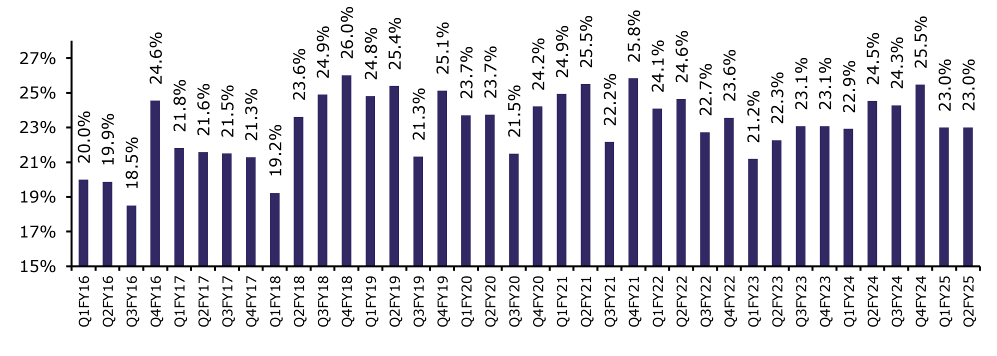
Source: Company, Emkay Research

Exhibit 9: Adjusted PAT growth



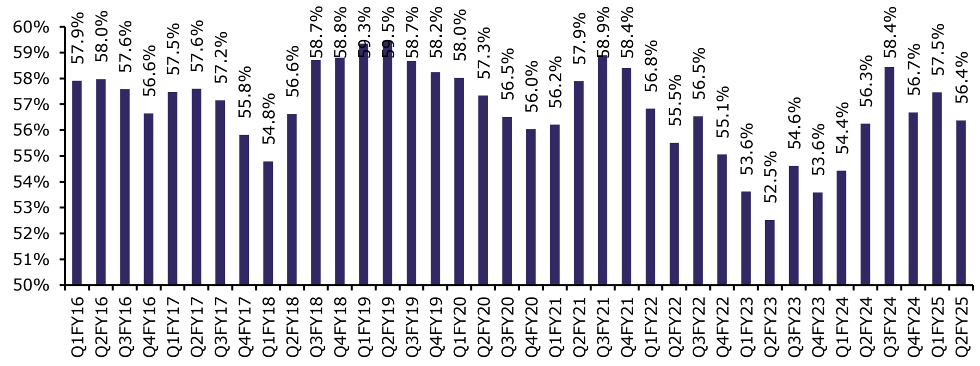
Source: Company, Emkay Research

Exhibit 10: EBITDA margin



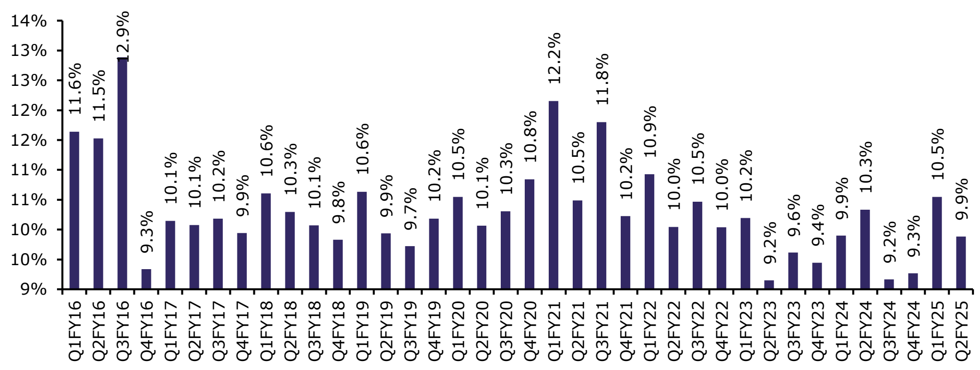
Source: Company, Emkay Research

Exhibit 11: Gross margin



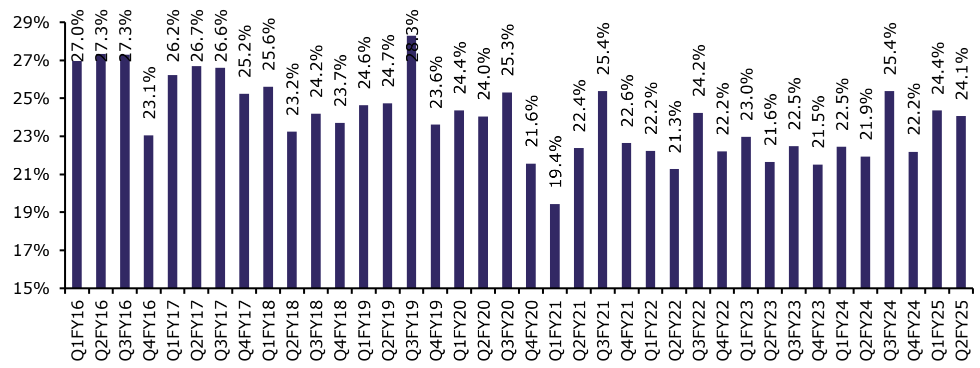
Source: Company, Emkay Research

Exhibit 12: Staff costs



Source: Company, Emkay Research

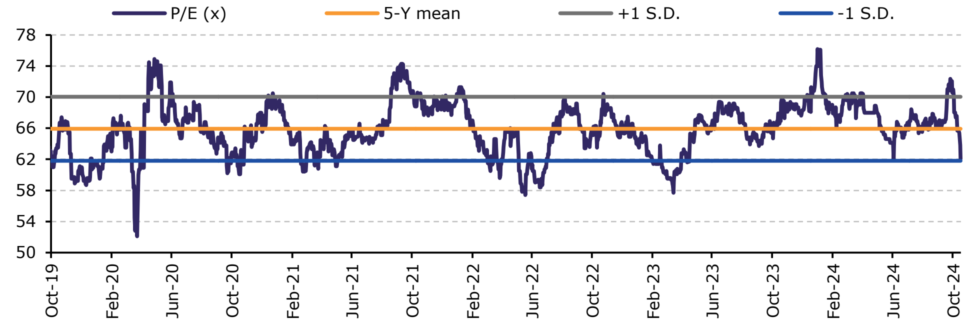
Exhibit 13: Other expenses as a % of sales



Source: Company, Emkay Research

Valuations

Exhibit 14: Nestlé India's one-year forward P/E (on consensus)



Source: Bloomberg, Emkay Research

Exhibit 15: Key assumptions

	CY20	CY21	CY22	FY24E	FY25E	FY26E	FY27E
Income statement							
Total income growth	8.1%	10.1%	14.7%	15.7%	3.6%	10.6%	10.4%
Volume growth	2.6%	10.5%	5.6%	2.7%	-1.1%	7.3%	7.4%
Gross margin	57.5%	57.0%	54.1%	56.1%	56.8%	57.3%	57.3%
Royalty	4.9%	4.9%	4.9%	4.9%	4.9%	4.9%	4.9%
Advertisement	5.7%	5.2%	4.1%	5.3%	5.5%	5.5%	5.5%
EBITDA margin	24.1%	24.3%	22.2%	24.0%	23.7%	24.5%	24.9%
Tax rate	25.8%	23.9%	26.2%	25.5%	25.7%	25.5%	25.5%
Adj PAT growth	5.1%	12.5%	3.3%	30.0%	0.6%	15.7%	10.8%
EPS (Rs)	21.7	24.4	25.3	41.0	33.0	38.2	42.3
Balance Sheet							
ROE	106.1%	114.9%	107.2%	109.2%	82.3%	84.6%	96.4%
ROCE	140.9%	152.3%	145.6%	145.0%	110.7%	112.3%	129.3%
Inventory days (no. of)	39	39	42	39	32	32	32
Receivable days (no. of)	5	4	4	6	4	4	3
Payable days (no. of)	41	43	42	42	32	32	34

Source: Company, Emkay Research

Exhibit 16: Changes to our estimates

(Rs mn)	New estimates			Old estimates			Changes to estimate		
	FY25E	FY26E	FY27E	FY25E	FY26E	FY27E	FY25E	FY26E	FY27E
Net sales	201,280	222,659	245,903	207,689	229,832	253,616	-3%	-3%	-3%
Growth	3.8%	10.6%	10.4%	7.1%	10.7%	10.3%			
EBITDA	48,064	54,892	61,633	51,196	56,879	63,572	-6%	-3%	-3%
Growth	2.7%	14.2%	12.3%	9.4%	11.1%	11.8%			
EBITDA margin	23.9%	24.7%	25.1%	24.7%	24.7%	25.1%			
Adj PAT	31,842	36,834	40,820	34,712	38,030	41,936	-8%	-3%	-3%
Growth	0.6%	15.7%	10.8%	9.6%	9.6%	10.3%			
EPS (Rs)	33.0	38.2	42.3	36.0	39.4	43.6	-8%	-3%	-3%

Source: Emkay Research

Exhibit 17: Emkay estimates vs consensus estimates

(Rs mn)	Emkay estimates			Consensus estimates			Emkay vs Consensus estimates		
	FY25E	FY26E	FY27E	FY25E	FY26E	FY27E	FY25E	FY26E	FY27E
Revenue	201,280	222,659	245,903	211,807	235,550	257,163	-5%	-5%	-4%
Growth	3.8%	10.6%	10.4%	9.2%	11.2%	9.2%			
EBITDA	48,064	54,892	61,633	51,448	58,295	64,623	-7%	-6%	-5%
Growth	2.7%	14.2%	12.3%	10.0%	13.3%	10.9%			
EBITDA margin	23.7%	24.5%	24.9%	24.3%	24.7%	25.1%			
Adj PAT	31,842	36,834	40,820	34,366	39,294	44,111	-7%	-6%	-7%
Growth	0.6%	15.7%	10.8%	8.5%	14.3%	12.3%			
EPS (Rs)	33.0	38.2	42.3	35.7	40.5	45.5	-7%	-6%	-7%

Source: Bloomberg, Emkay Research

Nestlé India: Standalone Financials and Valuations

Profit & Loss

Y/E Mar (Rs mn)	CY22	FY24	FY25E	FY26E	FY27E
Revenue	**168,970**	**243,939**	**202,482**	**223,930**	**247,235**
Revenue growth (%)	14.9	15.5	3.8	10.6	10.4
EBITDA	**37,583**	**58,490**	**48,064**	**54,892**	**61,633**
EBITDA growth (%)	5.3	24.5	2.7	14.2	12.3
Depreciation & Amortization	4,030	5,378	4,920	5,641	6,484
EBIT	**33,553**	**53,113**	**43,144**	**49,251**	**55,148**
EBIT growth (%)	5.6	26.6	1.5	14.2	12.0
Other operating income	1,074	1,184	1,202	1,271	1,332
Other income	1,010	1,480	962	1,191	644
Financial expense	1,546	1,455	1,250	1,000	1,000
PBT	**33,017**	**53,137**	**42,856**	**49,442**	**54,792**
Extraordinary items	0	0	0	0	0
Taxes	8,655	13,560	11,014	12,608	13,972
Minority interest	0	0	0	0	0
Income from JV/Associates	0	0	0	0	0
Reported PAT	**23,905**	**39,328**	**34,870**	**36,834**	**40,820**
PAT growth (%)	11.5	31.6	10.8	5.6	10.8
Adjusted PAT	**24,362**	**39,577**	**31,842**	**36,834**	**40,820**
Diluted EPS (Rs)	**25.3**	**32.8**	**33.0**	**38.2**	**42.3**
Diluted EPS growth (%)	3.3	30.0	0.6	15.7	10.8
DPS (Rs)	**19.6**	**16.0**	**21.8**	**31.2**	**25.3**
Dividend payout (%)	**79.1**	**49.0**	**60.2**	**81.7**	**59.6**
EBITDA margin (%)	22.2	24.0	23.7	24.5	24.9
EBIT margin (%)	19.9	21.8	21.3	22.0	22.3
Effective tax rate (%)	26.2	25.5	25.7	25.5	25.5
NOPLAT (pre-IndAS)	**24,758**	**39,559**	**32,056**	**36,692**	**41,085**
Shares outstanding (mn)	964.2	964.2	964.2	964.2	964.2

Source: Company, Emkay Research

Balance Sheet

Y/E Mar (Rs mn)	CY22	FY24	FY25E	FY26E	FY27E
Share capital	964	964	964	964	964
Reserves & Surplus	23,628	32,445	42,969	42,199	40,594
Net worth	**24,592**	**33,409**	**43,933**	**43,163**	**41,559**
Minority interests	0	0	0	0	0
Deferred tax liability (net)	(256)	0	0	0	0
Total debt	**33,104**	**31,245**	**28,224**	**28,724**	**29,224**
Total liabilities & equity	**57,440**	**64,654**	**72,157**	**71,888**	**70,783**
Net tangible fixed assets	30,437	34,603	39,708	46,623	51,673
Net intangible assets	0	0	0	0	0
Net ROU assets	0	0	0	0	0
Capital WIP	3,584	17,417	19,392	18,835	17,301
Goodwill	0	0	0	0	0
Investments [JV/Associates]	5,602	4,239	4,239	4,239	4,339
Cash & equivalents	**11,629**	**8,188**	**8,998**	**2,911**	**18,723**
Current assets (ex-cash)	38,280	40,783	37,722	40,768	25,832
Current Liab. & Prov.	32,091	40,576	37,902	41,489	47,086
NWC (ex-cash)	**6,188**	**207**	**(179)**	**(721)**	**(21,254)**
Total assets	**57,440**	**64,654**	**72,157**	**71,888**	**70,783**
Net debt	(11,629)	(8,188)	(8,998)	(2,911)	(18,723)
Capital employed	24,336	33,409	43,933	43,163	41,559
Invested capital	**36,625**	**34,810**	**39,528**	**45,902**	**30,420**
BVPS (Rs)	25.5	27.7	45.6	44.8	43.1
Net Debt/Equity (x)	(0.5)	(0.2)	(0.2)	(0.1)	(0.5)
Net Debt/EBITDA (x)	(0.3)	(0.1)	(0.2)	(0.1)	(0.3)
Interest coverage (x)	0.0	0.0	0.0	0.0	0.0
RoCE (%)	**153.9**	**151.3**	**114.1**	**115.8**	**131.7**

Source: Company, Emkay Research

Cash flows

Y/E Mar (Rs mn)	CY22	FY24	FY25E	FY26E	FY27E
PBT	33,017	53,137	42,856	49,442	54,792
Others (non-cash items)	327	277	0	0	0
Taxes paid	(8,412)	(12,988)	(11,014)	(12,608)	(13,972)
Change in NWC	(302)	(2,489)	(2,623)	1,042	21,033
Operating cash flow	**27,374**	**41,748**	**37,455**	**43,326**	**68,693**
Capital expenditure	(6,478)	18,870	(12,000)	(12,000)	(10,000)
Acquisition of business	0	0	0	0	0
Interest & dividend income	1,018	1,673	962	1,191	644
Investing cash flow	**(4,046)**	**(12,374)**	**(10,638)**	**(10,809)**	**(11,956)**
Equity raised/(repaid)	0	0	0	0	0
Debt raised/(repaid)	0	(1,000)	(11)	0	0
Payment of lease liabilities	0	0	0	0	0
Interest paid	(181)	(260)	(1,250)	(1,000)	(1,000)
Dividend paid (incl tax)	(20,980)	(30,082)	(24,346)	(37,604)	(42,425)
Others	(67)	300	0	0	0
Financing cash flow	**(21,227)**	**(31,041)**	**(25,607)**	**(38,604)**	**(43,425)**
Net chg in Cash	2,101	(1,667)	1,209	(6,087)	13,312
OCF	27,374	41,748	37,455	43,326	68,693
Adj. OCF (w/o NWC chg.)	27,676	44,237	39,944	42,284	47,661
FCFF	20,897	60,618	25,455	31,326	58,693
FCFE	20,369	60,836	25,167	31,517	58,337
OCF/EBITDA (%)	72.8	71.4	77.9	78.9	111.5
FCFE/PAT (%)	83.6	153.7	79.0	85.6	142.9
FCFF/NOPLAT (%)	**84.4**	**153.2**	**79.4**	**85.4**	**142.9**

Source: Company, Emkay Research

Valuations and key Ratios

Y/E Mar	CY22	FY24	FY25E	FY26E	FY27E
P/E (x)	94.1	72.4	72.0	62.3	56.2
P/CE(x)	80.8	63.8	62.4	54.0	48.5
P/B (x)	93.3	85.8	52.2	53.1	55.2
EV/Sales (x)	13.6	9.4	11.4	10.3	9.3
EV/EBITDA (x)	60.7	39.1	47.5	41.7	36.9
EV/EBIT(x)	68.0	53.8	53.0	46.5	41.2
EV/IC (x)	62.3	65.7	57.8	49.9	74.8
FCFF yield (%)	0.9	2.7	1.1	1.4	2.6
FCFE yield (%)	0.9	2.7	1.1	1.4	2.5
Dividend yield (%)	0.8	0.7	0.9	1.3	1.1
DuPont-RoE split					
Net profit margin (%)	14.4	16.2	15.7	16.4	16.5
Total asset turnover (x)	7.5	6.8	5.2	5.1	5.8
Assets/Equity (x)	1.0	1.0	1.0	1.0	1.0
RoE (%)	**107.2**	**109.2**	**82.3**	**84.6**	**96.4**
DuPont-RoIC					
NOPLAT margin (%)	14.7	16.2	15.8	16.4	16.6
IC turnover (x)	4.6	6.8	5.4	5.2	6.5
RoIC (%)	**67.5**	**88.6**	**86.2**	**85.9**	**107.7**
Operating metrics					
Core NWC days	(18.7)	(14.3)	(16.5)	(13.4)	(14.6)
Total NWC days	**13.4**	**0.4**	**(0.3)**	**(1.2)**	**(31.4)**
Fixed asset turnover	3.2	3.3	2.9	2.8	2.7
Opex-to-revenue (%)	31.9	32.1	33.1	32.8	32.4

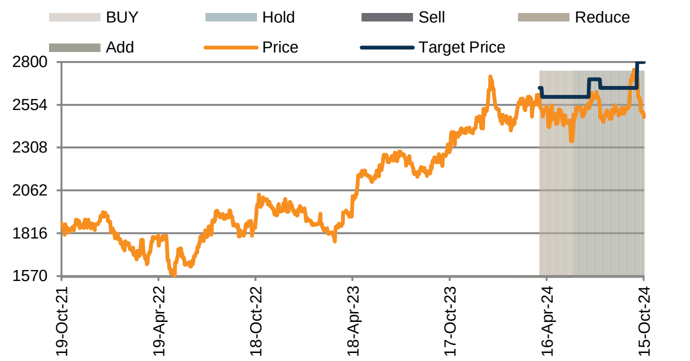
Source: Company, Emkay Research

RECOMMENDATION HISTORY - DETAILS

Date	Closing Price (INR)	TP (INR)	Rating	Analyst
02-Oct-24	2,707	2,800	Add	Nitin Gupta
24-Sep-24	2,696	2,650	Add	Nitin Gupta
25-Jul-24	2,481	2,650	Add	Nitin Gupta
04-Jul-24	2,534	2,700	Add	Nitin Gupta
26-Jun-24	2,523	2,600	Add	Nitin Gupta
04-Jun-24	2,417	2,600	Add	Nitin Gupta
13-May-24	2,505	2,600	Reduce	Nitin Gupta
08-May-24	2,528	2,600	Reduce	Nitin Gupta
25-Apr-24	2,552	2,600	Reduce	Nitin Gupta
15-Apr-24	2,543	2,600	Reduce	Nitin Gupta
07-Apr-24	2,527	2,600	Reduce	Nitin Gupta
02-Apr-24	2,612	2,650	Reduce	Nitin Gupta

Source: Company, Emkay Research

RECOMMENDATION HISTORY - TREND



Source: Company, Bloomberg, Emkay Research

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ADD	5-15% upside
REDUCE	5% upside to 15% downside
SELL	<15% downside

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CIN - L67120MH1995PLC084899

7th Floor, The Ruby, Senapati Bapat Marg, Dadar - West, Mumbai - 400028. India
Tel: +91 22 66121212 Fax: +91 22 66121299 Web: www.emkayglobal.com

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