

Nestle

Interpreting the weak 1QFY25 performance

We carried out detailed channel checks across India to gauge what has gone wrong and led to sub-par 1QFY25 performance, and how the current quarter is shaping up regarding the end consumer demand. We have been able to decipher the following reasons for this weak performance: (a) product formulation change coupled with packaging change in Lactogen in selected geographies has caused inventory correction. Moreover, the increased competitive intensity has majorly weighed on segmental performance; (b) Nestle has stopped the practice of price laddering in the Noodles segment; (c) disproportionate price increases in the coffee segment, which impacted end consumer offtake; and (d) unfavourable weather conditions (extreme heatwaves) leading to reduced Out-of-Home consumption frequency, which affected the Out-of-Home channel's performance. Our checks suggest that July 2024 has not seen any meaningful recovery and as a result, we cut our EPS estimates by 3% for FY25-26 to account for the weak 1HFY25 performance. We revise our target multiple from 70x to 65x to account for near term challenges while maintaining ADD and a TP of INR 2,700 (Sept-26 65x EPS). We will turn high conviction buyers on the stock if the stock were to correct 10% from current levels, as historically the company has shown an ability to bounce back from every debacle and after every mega capacity expansion programme.

- Change in formulation, increased competitive intensity dent performance in infant milk and nutrition segment:** Our channel checks suggest Lactogen performance was impacted to some extent, as the company underwent inventory correction in selected geographies before formulation and packaging change. Interestingly, the brand name has changed from Lactogen to "Lactogen Pro". Further, increased competitive intensity might have led to some market share loss in the infant milk category. Moreover, there was no mention of the infant milk category in the 1QFY25 press release, which further vindicates our stance.
- Price laddering completely/partially avoided in the Noodles segment:** Earlier, there used to be some savings for the end customer, if they opted for a bundle pack instead of a single-serve pack. However, our ground checks suggest that the company has done away with this benefit and there is no advantage to the end customer whether he buys a single-serve pack or a bundle pack, as per unit cost will remain the same; this has impacted the offtake of bulk packs. Higher competitive intensity from Yippee (ITC) in modern trade and e-commerce is further adding to this segment's woes.
- Disproportionate price increase in the coffee segment:** Our ground checks suggest Nestle has taken meaningful price hikes (on a blended basis -20%+) in the coffee segment, owing to unprecedented commodity inflation, which has led to customers downtrading to lower unit packs, which in turn has dented offtake. The price of top-selling SKU (50 grams) has been effectively hiked by 35% in a short span of six months.
- Unfavourable weather conditions (extreme heatwaves)** led to reduced Out-of-Home consumption frequency, which impacted the Out-of-Home channel's performance.

ADD

CMP (as on 06 Sep 2024)	INR 2,503
Target Price	INR 2,700
NIFTY	24,852

KEY STOCK DATA

Bloomberg code	NEST IN
No. of Shares (mn)	964
MCap (INR bn) / (\$ mn)	2,413/28,747
6m avg traded value (INR mn)	2,507
52 Week high / low	INR 2,771/2,177

STOCK PERFORMANCE (%)

	3M	6M	12M
Absolute (%)	1.3	(1.2)	13.8
Relative (%)	(6.9)	(10.8)	(9.5)

SHAREHOLDING PATTERN (%)

	Mar-24	Jun-24
Promoters	62.76	62.76
FIs & Local MFs	9.00	9.22
FPIs	12.10	11.94
Public & Others	16.14	16.07
Pledged Shares	0.00	0.00

Source : BSE

Pledged shares as % of total shares

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Packaging change of Lactogen reflects in short-term growth weakness



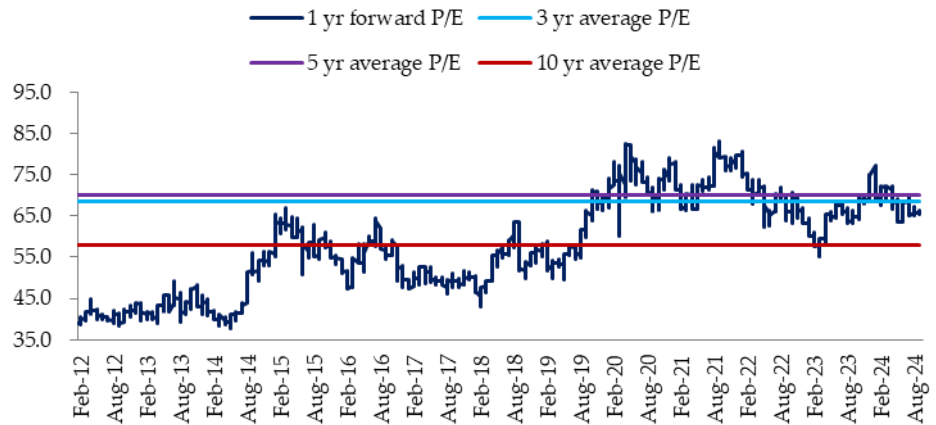
Source: HSIE Research

Margin pressures are expected to continue

Commodity	Units	Base Period (July 2023 – March 2024)	Current Period (July 2024 – March 2025)	Inflation/ (deflation)
Coffee Arabica	USD/lb	173	246	42.2%
Coffee Robusta	USD/mt	2,862	5,012	75.1%
Liquid Milk - Domestic	INR/ltr	49	51	4.3%
SMP - Domestic	EUR/mt	2,457	2,517	2.4%
Wheat	INR/Quintal	2,590	2,795	7.9%
Brent Crude	USD/bbl	84	78	-6.5%
Palm Oil	INR/KG	808	927	14.6%
Cocoa	USD/mt	4,377	6,958	59.0%

Source: HSIE Research

Nestle trading at a 66x, 5% discount to its 5-year average P/E of 70x



Source: Bloomberg, Company, HSIE Research

Standalone P&L

(INR mn)	CY22	FY24	FY25E	FY26E	FY27E
Net Revenues	1,67,895	1,94,671	2,07,963	2,28,248	2,50,559
Growth (%)	14.5	15.9	6.8	9.8	9.8
Material Expenses	77,499	84,770	90,606	98,761	1,07,649
Employee Expense	16,355	18,818	20,421	22,464	24,710
Other Expenses	37,991	44,646	44,646	47,708	52,442
EBITDA	37,126	47,399	53,287	60,412	66,965
EBITDA Growth (%)	4.1	27.7	12.4	13.4	10.8
EBITDA Margin (%)	22.1	24.3	25.6	26.5	26.7
Depreciation	4,030	4,517	4,598	4,689	5,421
EBIT	33,095	42,883	48,689	55,723	61,543
Other Income	1,010	1,143	1,305	1,436	1,579
Interest	1,546	1,133	1,133	1,133	1,133
PBT	32,560	42,892	48,861	56,026	61,990
Tax	8,655	11,022	11,908	13,336	14,807
Profit from minority/associates					
RPAT	23,905	31,870	36,953	42,690	47,183
Adjustment	-	-	-	-	-
Adjusted PAT	23,905	31,870	36,953	42,690	47,183
APAT Growth (%)	12.8	33.3	15.9	15.5	10.5
Adjusted EPS	24.8	33.1	35.2	39.4	43.7
EPS Growth (%)	1.5	33.3	6.34	12.00	11.0

Source: Company, HSIE Research

Standalone Balance Sheet

(INR mn)	CY22	FY24	FY25E	FY26E	FY27E
SOURCES OF FUNDS					
Share Capital - Equity	964	964	964	964	964
Reserves	23,628	32,445	44,208	48,004	52,218
Total Shareholders Funds	24,592	33,409	45,172	48,968	53,182
Minority Interest	-	-	-	-	-
Long Term Debt	2,173	2,814	2,814	2,814	2,814
Short Term Debt	532	631	631	631	631
Total Debt	2,705	3,445	3,445	3,445	3,445
Net Deferred Taxes	(256)	120	120	120	120
Other Non-current Liabilities & Provns	32,225	29,327	25,794	28,295	31,045
TOTAL SOURCES OF FUNDS	59,266	66,301	74,532	80,828	87,793
APPLICATION OF FUNDS					
Net Block	30,437	34,603	40,004	45,315	49,893
CWIP	3,584	17,417	17,417	17,417	17,417
Other Non Current Assets	20,609	18,264	18,264	18,264	18,264
Total Non-current Assets	54,630	70,283	75,685	80,996	85,574
Inventories	19,288	20,894	22,790	25,013	27,459
Debtors	1,919	3,005	2,279	2,501	2,746
Other Current Assets	4,239	3,261	3,261	3,261	3,261
Cash & Equivalents	9,456	7,789	5,532	6,129	8,087
Total Current Assets	34,902	34,947	33,862	36,904	41,552
Creditors	19,338	22,379	19,372	21,261	23,340
Other Current Liabilities & Provns	10,927	16,551	15,644	15,810	15,994
Total Current Liabilities	30,265	38,929	35,016	37,072	39,333
Net Current Assets	4,636	(3,982)	(1,153)	(167)	2,219
TOTAL APPLICATION OF FUNDS	59,266	66,301	74,532	80,828	87,793

Source: Company, HSIE Research

Standalone Cash Flow

(INR mn)	CY22	FY24	FY25E	FY26E	FY27E
Reported PBT	32,560	52,889	45,798	51,293	56,950
Non-operating & EO Items	-	-	-	-	-
Interest Expenses	-	-	-	-	-
Depreciation	4,030	5,378	4,598	4,689	5,421
Working Capital Change	(302)	(2,489)	(8,618)	2,112	2,323
Tax Paid	(8,412)	(12,988)	(11,908)	(13,336)	(14,807)
OPERATING CASH FLOW (a)	27,374	41,748	29,871	44,758	49,887
Capex	(5,499)	(18,827)	(10,000)	(10,000)	(10,000)
Free Cash Flow (FCF)	21,875	22,921	19,871	34,758	39,887
Investments	(1,071)	-	-	-	-
Non-operating Income	2,653	6,453	-	-	-
INVESTING CASH FLOW (b)	(3,917)	(12,374)	(10,000)	(10,000)	(10,000)
Debt Issuance/(Repaid)	-	-	-	-	-
Interest Expenses	(181)	(260)	-	-	-
FCFE	21,694	22,661	19,871	34,758	39,887
Share Capital Issuance	-	-	-	-	-
Dividend	(20,247)	(30,082)	(30,502)	(34,161)	(37,929)
Others	(1,066)	(8)	-	-	-
FINANCING CASH FLOW (c)	(21,227)	(31,349)	(30,502)	(34,161)	(37,929)
NET CASH FLOW (a+b+c)	2,230	(1,976)	(10,630)	597	1,958
EO Items, Others	-	-	-	-	-
Closing Cash & Equivalents	9,964	7,989	(2,642)	(2,045)	(87)

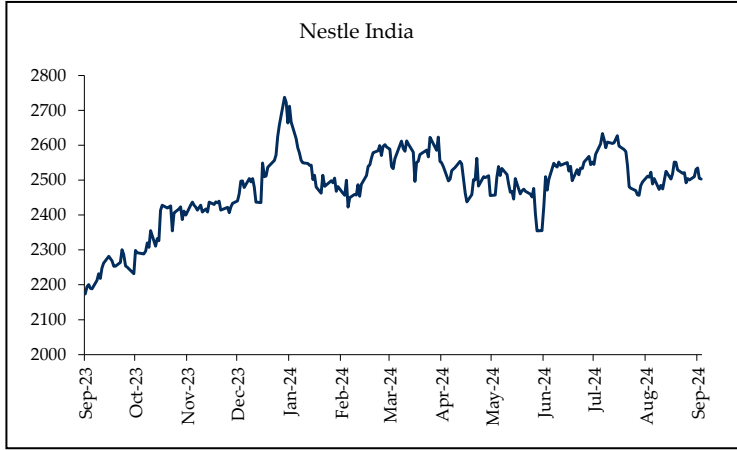
Source: Company, HSIE Research

Ratios

KEY RATIOS	CY22	FY24	FY25E	FY26E	FY27E
PROFITABILITY (%)					
GPM	53.8	56.5	56.4	56.7	57.0
EBITDA Margin	22.1	24.3	25.6	26.5	26.7
EBIT Margin	19.7	22.0	23.4	24.4	24.6
APAT Margin	14.2	16.4	17.8	18.7	18.8
RoE	105.2	109.9	86.3	80.6	82.5
RoIC (or Core RoCE)	50.9	62.5	58.3	57.1	74.4
RoCE	44.6	54.9	54.2	54.3	68.6
EFFICIENCY					
Tax Rate (%)	26.6	25.7	24.4	23.8	23.9
Fixed Asset Turnover (x)	3.4	3.4	3.1	3.0	2.9
Inventory (days)	41.9	39.2	40.0	40.0	40.0
Debtors (days)	4.2	5.6	4.0	4.0	4.0
Other Current Assets (days)	9.2	6.1	5.7	5.2	4.7
Payables (days)	42.0	42.0	34.0	34.0	34.0
Other Current Liab & Provns (days)	23.8	31.0	27.5	25.3	23.3
Cash Conversion Cycle (days)	(10.5)	(22.1)	(11.7)	(10.1)	(8.5)
Net D/E (x)	(0.3)	(0.1)	(0.0)	(0.1)	(0.1)
Interest Coverage (x)	21.4	37.8	43.0	49.2	54.3
PER SHARE DATA (Rs)					
EPS	24.8	33.1	35.2	39.4	43.7
CEPS	29.0	37.7	39.9	44.2	49.3
Dividend	22.0	29.5	31.6	35.4	39.3
Book Value	25.5	34.7	46.9	50.8	55.2
VALUATION					
P/E (x)	101.0	61.5	75.8	71.3	63.6
P/BV (x)	98.2	72.3	53.5	49.3	45.4
EV/EBITDA (x)	64.9	50.9	45.3	39.9	36.0
EV/Revenues (x)	14.3	12.4	11.6	10.6	9.6
OCF/EV (%)	1.1	1.7	1.2	1.9	2.1
FCF/EV (%)	0.9	1.0	0.8	1.4	1.7
FCFE/Mkt Cap (%)	0.9	0.9	0.8	1.4	1.7
Dividend Yield (%)	0.9	1.2	1.3	1.4	1.6

Source: Company, HSIE Research

1 Yr Price Movement



Rating Criteria

- BUY: >+15% return potential
- ADD: +5% to +15% return potential
- REDUCE: -10% to +5% return potential
- SELL: > 10% Downside return potential

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