

18 October 2024

India | Equity Research | Q2FY25 results review

Nestle

Consumer Staples & Discretionary

Underwhelming. Reiterate neutral stance.

Nestle's Q2FY25 revenue growth was disappointing; it further de-accelerated to 1% YoY (vs 4% in Q1FY25) due to subdued consumer demand (urban has been witnessing decelerating demand trends over last few quarters). Gross margin was largely flat (despite significant inflation in key inputs) while EBITDA margin declined ~155bps YoY to 22.4% due to operating deleverage. Higher prices of key raw materials (cocoa, coffee etc.), margins are likely to remain under pressure. That said, Nestle appears to have a market share gain opportunity given the relative immunity from cocoa inflation as its key brands KitKat and Munch have lower cocoa content vs competition (~5% vs ~20% in Cadbury). Though we considered upgrading Nestle post stock underperformance of ~20% over last 12 months, we are unable to find any fundamental reasons, as of now. Maintain **HOLD** with revised TP of INR 2,350.

Revenue growth moderates

Nestle's revenue grew 1% YoY (below estimates) in Q2FY25. Domestic revenue grew 1% YoY while exports grew by 3% YoY. It highlighted that (1) beverage business continues to outperform with strong double-digit revenue growth led by premiumisation in coffee and backed by strong performance across NESCAFÉ CLASSIC, NESCAFÉ SUNRISE, and NESCAFÉ GOLD. (2) Prepared dishes and cooking aids also maintained growth momentum through portfolio premiumisation; Milkmaid, Masala-Ae-Magic and Toddler range delivered high double-digit growth while KITKAT grew in high single-digit, (3) Petcare witnessed high single-digit growth led by strong e-commerce. (4) E-commerce is growing in high double-digits (~38%) - contributed 8.3% to domestic sales (highest in last seven quarters) driven by Quick Commerce (QC) and support from other brands. The growth was driven by premiumisation, new user acquisition, festive participation and targeted digital communications. (5) OOH business grew in double-digit.

Nestle launches a new range of products in its CERELAC portfolio with variants of no refined sugar. The expanded range will consist of 21 variants of which 14 are to be with no refined sugar. Management plans to launch 7 of its 14 variants by November-24 and rest by following weeks.

Financial Summary

Y/E March (INR mn)	CY22A	FY24A	FY25E	FY26E
Net Revenue	1,67,895	1,94,671	2,02,791	2,22,756
EBITDA	36,508	46,428	47,055	52,801
EBITDA Margin (%)	21.7	23.8	23.2	23.7
Net Profit	23,905	31,870	32,011	36,268
EPS (INR)	24.8	33.1	33.2	37.6
EPS % Chg YoY	1.5	33.3	0.4	13.3
P/E (x)	95.9	72.0	71.6	63.2
EV/EBITDA (x)	62.5	49.2	48.6	43.2
RoCE (%)	107.2	106.8	85.7	86.3
RoE (%)	108.5	109.9	87.9	89.2

*FY24A are TTM numbers ending Mar'24.

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Market Data

Market Cap (INR)	2,293bn
Market Cap (USD)	27,283mn
Bloomberg Code	NEST IN
Reuters Code	NEST.BO
52-week Range (INR)	2,778 /2,310
Free Float (%)	37.0
ADTV-3M (mn) (USD)	32.5

Price Performance (%)	3m	6m	12m
Absolute	(8.8)	(6.6)	2.0
Relative to Sensex	(9.1)	(17.6)	(20.0)

Earnings Revisions (%)	FY25E	FY26E
Revenue	(2.7)	(2.7)
EBITDA	(5.8)	(6.2)
EPS	(5.8)	(6.3)

Previous Reports

25-07-2024: [Q1FY24 results review](#)

26-04-2024: [Q5FY24 results review](#)

Operating margin decline led by increase in brands investment

Gross margin was largely flattish YoY at 56.4% as elevated raw material inflation continues. Management highlighted: (1) Coffee and cocoa are facing unprecedented inflation; (2) cereals and edible oils are also starting to witness inflationary trends and (3) Milk prices and packaging material are relatively stable.

EBITDA margin contracted by 155bps YoY to 22.4% due to higher investments behind the brands – increase in advertising and marketing investments for the quarter (other expenses were up by 211bps YoY, and 11% YoY on absolute basis). Nestle is likely to continue to invest gross margin benefits behind its brands. EBITDA and recurring PAT declined by 5% YoY and 13% YoY, respectively.

Valuation and risks

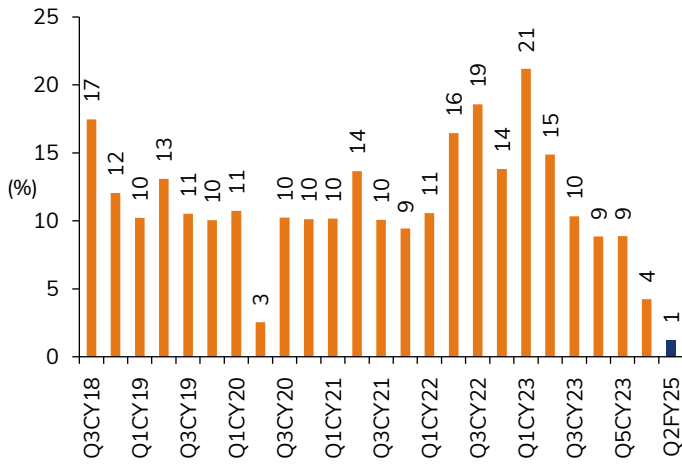
We cut our earnings estimates by 6% for FY25E-26E, modelling revenue / EBITDA / PAT CAGR of 7 / 7 / 7 (%) over FY24-26E. Maintain **HOLD** with a DCF-based revised target price of INR 2,350 (vs INR 2,500). Upside risk: Faster-than-anticipated recovery in demand environment. Downside risk: Higher-than-expected inflation in key raw material prices.

Exhibit 1: Q2FY25 result review

INR mn	Q2FY25	Q2FY24	YoY (%)	Q1FY25	QoQ (%)	1HFY25	1HFY24	YoY (%)
Net domestic revenue	48,831	48,237	1	46,085	6	94,916	92,445	3
Export revenue	1,916	1,858	3	1,845	4	3,761	3,845	(2)
Net Revenues	50,748	50,095	1	47,930	6	98,677	96,290	2
COGS	(22,139)	(21,916)	1	(20,388)	9	(42,528)	(42,966)	(1)
Gross profit	28,608	28,179	2	27,541	4	56,150	53,324	5
Staff cost	(5,017)	(5,176)	(3)	(5,054)	(1)	(10,071)	(9,748)	3
Other opex	(12,207)	(10,989)	11	(11,674)	5	(23,881)	(21,363)	12
Total opex	(17,224)	(16,165)	7	(16,728)	3	(33,951)	(31,112)	9
EBITDA	11,385	12,014	(5)	10,814	5	22,198	22,212	(0)
Other income	361	606	(40)	601	(40)	962	1,236	(22)
Finance Cost	(322)	(314)	3	(317)	2	(639)	(642)	(0)
D&A	(1,216)	(1,112)	9	(1,127)	8	(2,343)	(2,185)	7
PBT	10,208	11,195	(9)	9,971	2	20,178	20,621	(2)
Tax	(3,252)	(3,139)	4	(2,625)	24	(5,877)	(5,549)	6
PAT	6,955	8,055	(14)	7,346	(5)	14,301	15,072	(5)
Impairment of fixed assets	-	(31)		-		-	(31)	
Provision for contingencies	-	(8)	(100)	120	(100)	120	(41)	(393)
Recurring PAT	6,955	8,017	(13)	7,466	(7)	14,421	15,000	(4)
Extraordinary items	2,908	1,064		-		2,908	1,064	
Net profit (reported)	9,864	9,081	9	7,466	32	17,330	16,064	8
EPS	7.2	8.3	(13)	7.7	(7)	15.0	15.6	(4)
Costs as a % of sales								
COGS	43.6	43.7	-13 bps	42.5	108 bps	43.1	44.6	-153 bps
Gross margin (%)	56.4	56.3	12 bps	57.5	-109 bps	56.9	55.4	152 bps
Staff cost	9.9	10.3	-45 bps	10.5	-66 bps	10.2	10.1	8 bps
Other opex	24.1	21.9	211 bps	24.4	-31 bps	24.2	22.2	201 bps
EBITDA margin (%)	22.4	24.0	-155 bps	22.6	-13 bps	22.5	23.1	-58 bps
Income tax rate (%)	31.9	28.0	381 bps	26.3	553 bps	29.1	26.9	221 bps

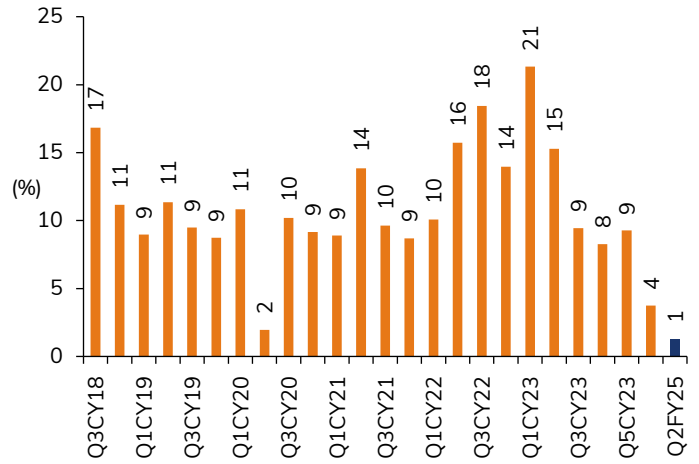
Source: Company data, I-Sec research

Exhibit 2: Domestic revenue growth



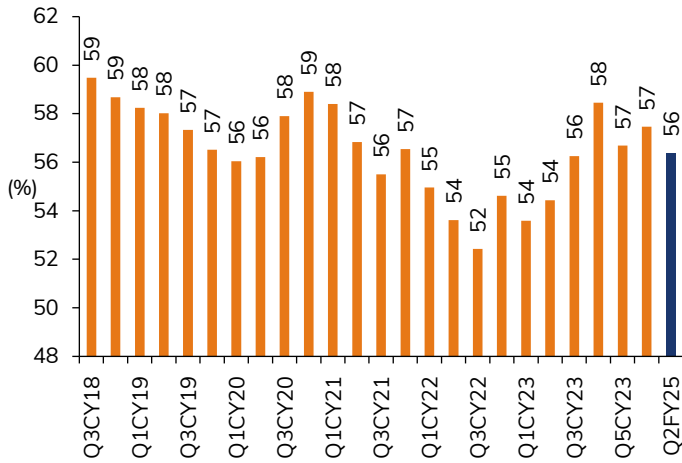
Source: Company data, I-Sec research

Exhibit 3: Revenue growth



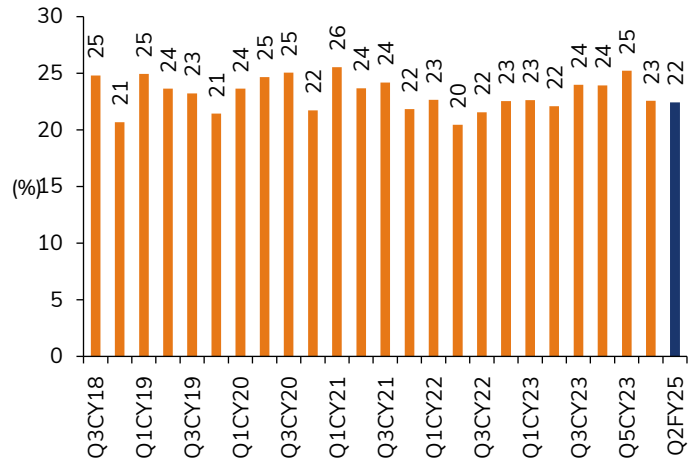
Source: Company data, I-Sec research

Exhibit 4: Gross margin



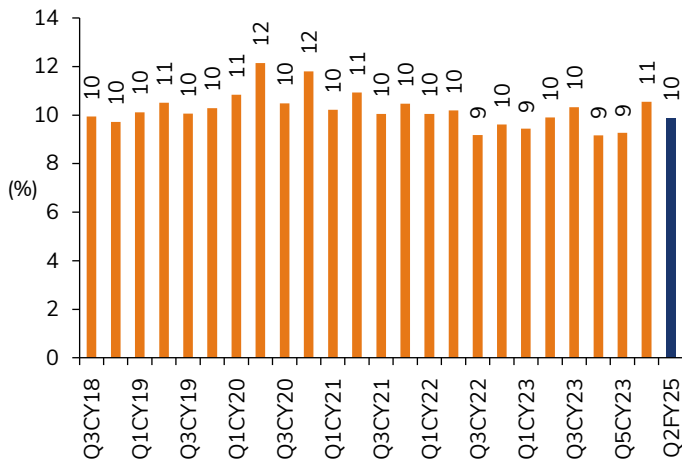
Source: Company data, I-Sec research

Exhibit 5: EBITDA margin



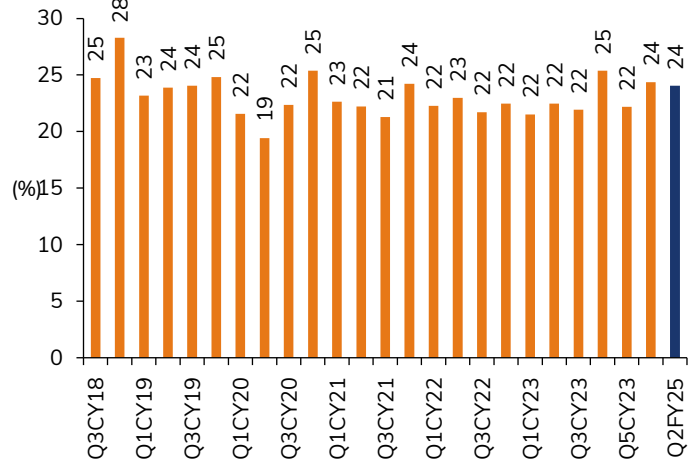
Source: Company data, I-Sec research

Exhibit 6: Employee costs (as a % of sales)



Source: Company data, I-Sec research

Exhibit 7: Other expenses (as a % of sales)



Source: Company data, I-Sec research

Exhibit 8: Shareholding pattern

%	Mar'24	Jun'24	Sep'24
Promoters	62.8	62.8	62.8
Institutional investors	21.1	21.2	21.4
MFs and others	4.4	4.4	5.1
FIs/Banks, Insurance	3.8	4.8	4.3
FIIIs	12.9	12.0	12.0
Others	16.1	16.0	15.8

Source: Bloomberg, I-Sec research

Exhibit 9: Price chart



Source: Bloomberg, I-Sec research

Financial Summary

Exhibit 10: Profit & Loss

(INR mn, year ending March)

	CY22A	FY24A	FY25E	FY26E
Net Sales	1,67,895	1,94,671	2,02,791	2,22,756
Operating Expenses	1,31,387	1,48,243	1,55,737	1,69,955
EBITDA	36,508	46,428	47,055	52,801
EBITDA Margin (%)	21.7	23.8	23.2	23.7
Depreciation & Amortization	4,030	4,361	4,739	5,237
EBIT	32,478	42,067	42,316	47,564
Interest expenditure	1,546	1,133	1,159	1,135
Other Non-operating Income	2,084	2,106	1,896	2,351
Recurring PBT	33,017	43,040	43,052	48,779
Profit / (Loss) from Associates	-	-	-	-
Less: Taxes	8,655	11,022	11,049	12,519
PAT	24,362	32,017	32,003	36,260
Less: Minority Interest	-	-	-	-
Extraordinaries (Net)	-	92	2,908	-
Net Income (Reported)	23,905	31,962	34,919	36,268
Net Income (Adjusted)	23,905	31,870	32,011	36,268

Source Company data, I-Sec research

Exhibit 11: Balance sheet

(INR mn, year ending March)

	CY22A	FY24A	FY25E	FY26E
Total Current Assets	34,902	34,947	36,367	43,788
of which cash & cash eqv.	11,629	8,188	9,249	14,183
Total Current Liabilities & Provisions	28,394	33,188	32,453	35,770
Net Current Assets	6,507	1,759	3,914	8,018
Investments	5,602	4,239	4,239	4,239
Net Fixed Assets	27,058	30,557	31,901	31,564
ROU Assets	-	-	-	-
Capital Work-in-Progress	3,584	17,417	17,417	17,417
Total Intangible Assets	-	-	-	-
Long Term Loans & Advances	15,007	14,025	11,716	12,870
Deferred Tax assets	-	-	-	-
Total Assets	61,137	72,042	73,233	78,154
Liabilities				
Borrowings	300	311	311	311
Deferred Tax Liability	(256)	120	120	120
Provisions	32,052	29,172	24,370	26,769
Other Liabilities	4,450	9,030	9,030	9,030
Equity Share Capital	964	964	964	964
Reserves & Surplus	23,628	32,445	38,438	40,959
Total Net Worth	24,592	33,409	39,402	41,923
Minority Interest	-	-	-	-
Total Liabilities	61,137	72,042	73,233	78,154

Source Company data, I-Sec research

Exhibit 12: Quarterly trend

(INR mn, year ending March)

	Dec-23	Mar-24	Jun-24	Sep-24
Net Sales	45,836	52,544	47,930	50,748
% growth (YOY)	8.9	8.9	4.2	1.2
EBITDA	10,962	13,254	10,814	11,385
Margin %	23.9	25.2	22.6	22.4
Other Income	303	268	391	69
Extraordinaries	(1,073)	101	-	2,908
Adjusted Net Profit	7,629	9,241	7,466	6,955

Source Company data, I-Sec research

Exhibit 13: Cashflow statement

(INR mn, year ending March)

	CY22A	FY24A	FY25E	FY26E
Operating Cashflow	27,374	41,748	36,097	43,206
Working Capital Changes	(302)	(2,489)	(3,588)	2,076
Capital Commitments	(4,949)	(14,045)	(6,084)	(4,901)
Free Cashflow	22,426	27,703	30,013	38,305
Other investing cashflow	1,031	1,670	1,133	1,511
Cashflow from Investing Activities	(3,917)	(12,374)	(4,950)	(3,389)
Issue of Share Capital	-	-	-	-
Interest Cost	(20)	(16)	(1,159)	(1,135)
Inc (Dec) in Borrowings	-	-	-	-
Dividend paid	(20,247)	(30,082)	(28,926)	(33,747)
Others	(960)	(1,251)	-	-
Cash flow from Financing Activities	(21,227)	(31,349)	(30,085)	(34,882)
Chg. in Cash & Bank balance	2,230	(1,976)	1,061	4,934
Closing cash & balance	9,584	7,480	8,849	13,784

Source Company data, I-Sec research

Exhibit 14: Key ratios

(Year ending March)

	CY22A	FY24A	FY25E	FY26E
Per Share Data (INR)				
Reported EPS	24.8	33.1	33.2	37.6
Adjusted EPS (Diluted)	24.8	33.1	33.2	37.6
Cash EPS	29.0	37.6	38.1	43.0
Dividend per share (DPS)	22.0	32.2	30.0	35.0
Book Value per share (BV)	25.5	34.6	40.9	43.5
Dividend Payout (%)	88.7	97.4	90.4	93.0
Growth (%)				
Net Sales	14.5	15.9	4.2	9.8
EBITDA	5.3	27.2	1.4	12.2
EPS (INR)	1.5	33.3	0.4	13.3
Valuation Ratios (x)				
P/E	95.9	72.0	71.6	63.2
P/CEPS	82.1	63.3	62.4	55.3
P/BV	93.3	68.7	58.2	54.7
EV / EBITDA	62.5	49.2	48.6	43.2
P / Sales	13.7	11.8	11.3	10.3
Dividend Yield (%)	0.9	1.4	1.3	1.5
Operating Ratios				
Gross Profit Margins (%)	53.8	56.5	56.7	56.9
EBITDA Margins (%)	21.7	23.8	23.2	23.7
Effective Tax Rate (%)	26.2	25.6	25.7	25.7
Net Profit Margins (%)	14.5	16.4	15.8	16.3
Net Debt / Equity (x)	(0.5)	(0.2)	(0.2)	(0.3)
Net Debt / EBITDA (x)	(0.3)	(0.2)	(0.2)	(0.3)
Fixed Asset Turnover (x)	3.5	3.6	3.4	3.4
Working Capital Days	(13)	(14)	(10)	(11)
Inventory Turnover Days	45	42	40	40
Receivables Days	4	6	6	6
Payables Days	45	45	43	44
Profitability Ratios				
RoCE (%)	107.2	106.8	85.7	86.3
RoE (%)	108.5	109.9	87.9	89.2
RoIC (%)	114.1	112.1	89.5	90.6

Source Company data, I-Sec research

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