

**BUY**

TP: Rs 28,260 | ▲ 20%

**NESTLE INDIA**

Consumer Staples

26 October 2023

### Analyst meet: Broader footprint lifting volume growth

- Innovation and market penetration-led volume growth remain strategic focus areas; growing emphasis on rural markets
- Creating capacities for future growth with capital investment of Rs 50bn committed over three years
- Primed for consistent and profitable growth; maintain BUY with unchanged TP of Rs 28,260

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**Secular double-digit growth in 9MCY23:** NEST has delivered strong revenue growth of 15% YoY in 9MCY23 led by innovation and market penetration. The company posted high-double-digit growth across its portfolio over Jan-Sep'23, with milk products and nutrition (40% of sales) growing 15% YoY, prepared dishes and cooking aids (32%) up 11%, confectionary (17%) up 21%, and powdered and liquid beverages (11%) rising 19%. To build capacities for future growth, NEST in its analyst meet today said it has committed Rs 50bn toward capex over CY23-CY25.

**Volume slowdown temporary:** NEST has clocked a ~7% volume CAGR for the last five years. Over the last nine months, however, volume growth has slowed to ~2% largely due to higher inflation and price hikes taken in low unit packs, which face added competition from regional players. Per management, the slowdown is a temporary blip and regional competition helps companies redefine strategies.

**Pricing, grammage action taken to counter inflation:** The company has taken price increases or grammage changes for ~50% of its products in the last year to mitigate the impact of high raw material cost inflation. Though key commodities have softened recently, no price hike rollbacks are on the cards. Management also indicated that milk and green coffee costs remain high.

**Robust innovation and premiumisation trends:** NEST has launched 125 products in the last seven years, with 10 more in the pipeline. The company reckons that innovation contributes 6%+ of its domestic sales, which is targeted to rise to 10% in coming years, and that premium product volumes are growing twice as fast as the rest of its portfolio.

**Maintain BUY:** NEST continues to deliver a robust performance supported by consumer engagement, launches, and uptrading to branded products in RURBAN markets. The stock is trading at 62.7x/54.2x CY24E/CY25E EPS. Our target 2Y forward P/E multiple remains at 65x on CY25E EPS for an unchanged TP of Rs 28,260. We retain BUY as we expect NEST to show sustained, profitable growth underpinned by investments in capacity creation, innovation, premiumisation, and direct reach expansion with a rural focus.

### Key changes

Target	Rating
◀ ▶	◀ ▶

Ticker/Price	NEST IN/Rs 23,546
Market cap	US\$ 27.6bn
Free float	37%
3M ADV	US\$ 19.3mn
52wk high/low	Rs 24,745/Rs 17,880
Promoter/FPI/DII	63%/12%/25%

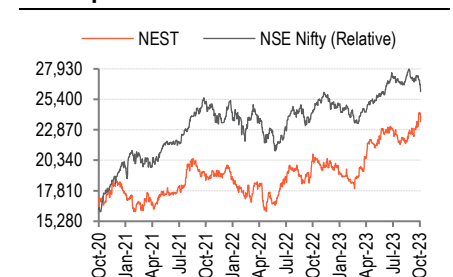
Source: NSE | Price as of 26 Oct 2023

### Key financials

Y/E 31 Dec	CY22A	CY23E	CY24E
Total revenue (Rs mn)	168,969	194,416	221,824
EBITDA (Rs mn)	37,125	46,097	55,879
Adj. net profit (Rs mn)	23,905	29,819	36,218
Adj. EPS (Rs)	247.9	309.3	375.6
Consensus EPS (Rs)	247.9	306.6	350.9
Adj. ROAE (%)	97.2	105.3	103.9
Adj. P/E (x)	95.0	76.1	62.7
EV/EBITDA (x)	61.1	49.2	40.6
Adj. EPS growth (%)	1.5	24.7	21.5

Source: Company, Bloomberg, BOBCAPS Research

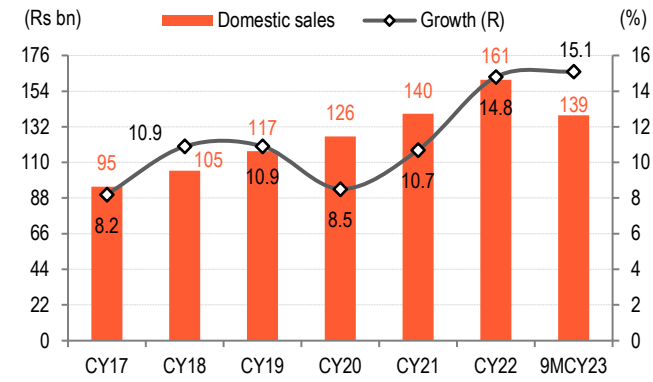
### Stock performance



Source: NSE

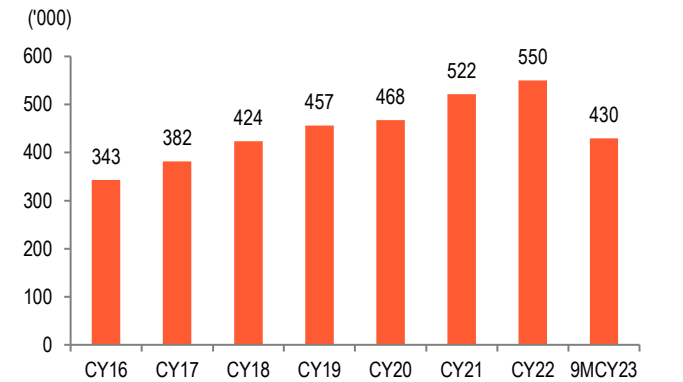


**Fig 1 – Domestic sales and growth YoY**



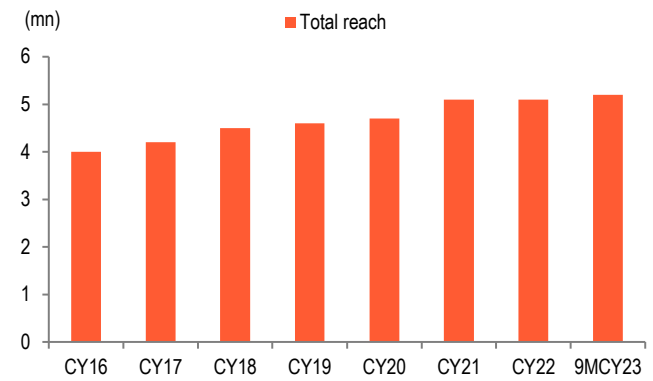
Source: Company, BOBCAPS Research

**Fig 2 – Domestic sales volume**



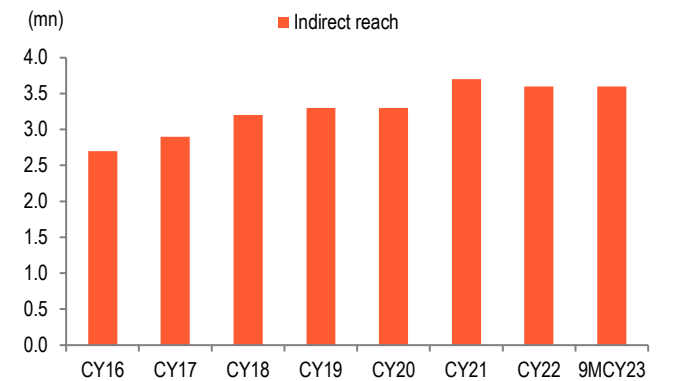
Source: Company, BOBCAPS Research

**Fig 3 – Total reach**



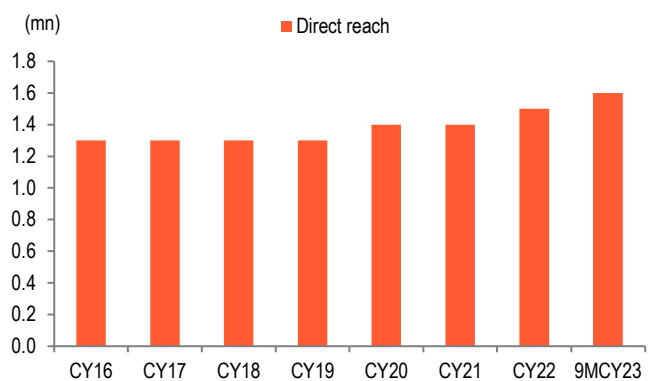
Source: Company, BOBCAPS Research

**Fig 4 – Indirect reach**



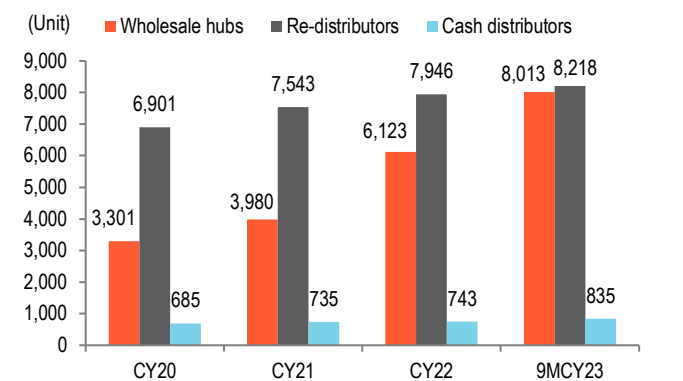
Source: Company, BOBCAPS Research

**Fig 5 – Direct reach**



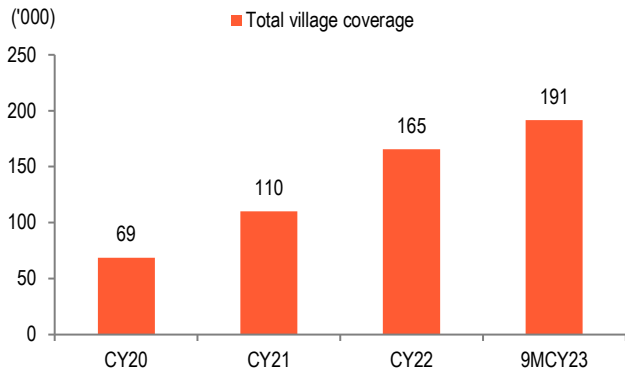
Source: Company, BOBCAPS Research

**Fig 6 – Distribution touchpoints**



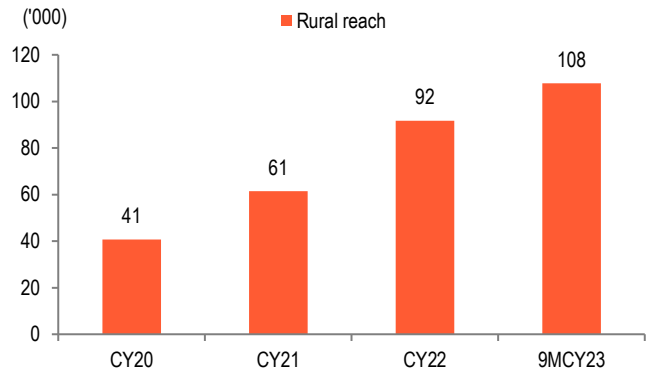
Source: Company, BOBCAPS Research

**Fig 7 – Total village coverage**



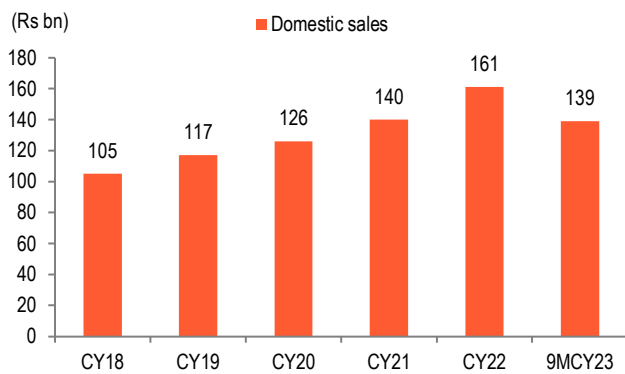
Source: Company, BOBCAPS Research

**Fig 8 – Rural reach in villages with population >2,000**



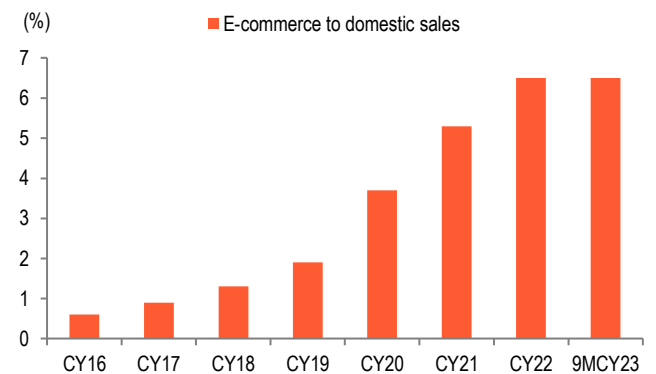
Source: Company, BOBCAPS Research

**Fig 9 – Domestic sales**



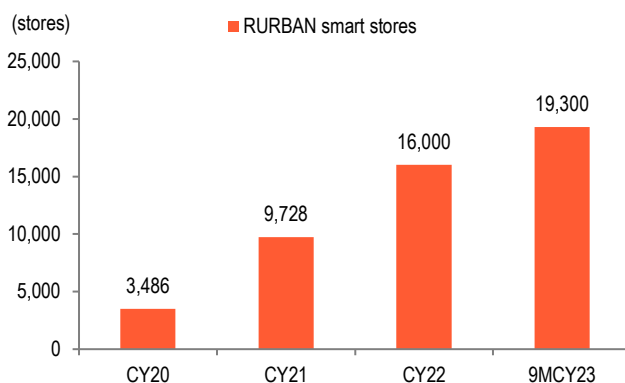
Source: Company, BOBCAPS Research

**Fig 10 – E-commerce-to-domestic sales ratio**



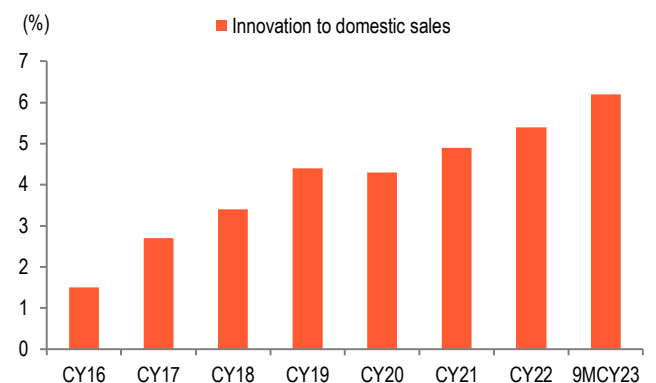
Source: Company, BOBCAPS Research

**Fig 11 – RURBAN smart stores**



Source: Company, BOBCAPS Research

**Fig 12 – Innovation-to-domestic sales ratio**



Source: Company, BOBCAPS Research

## Key analyst meet takeaways

- India's food & beverage market is valued at ~US\$ 800bn, according to NEST, and the packaged food market is pegged at US\$ 100bn, of which the branded packaged segment makes up only US\$ 40bn. Management believes the likely shift from unbranded to branded packaged products provides room for innovation and penetration-led growth, where NEST is likely to be the biggest beneficiary.
- Over the last five years, NEST has registered strong double-digit domestic sales growth, following this up with 15% YoY growth in 9MCY23. Per management, premium product volumes are growing at 2-2.5x the rest of its product portfolio.
- The company has clocked a ~7% volume CAGR for the last five years. Over the last nine months, however, volume growth has slowed to 2% largely due to higher inflation and price hikes taken in low unit packs, which face added competition from regional players. According to management, the recent performance is a temporary blip and regional competition helps companies redefine strategies. NEST believes discretionary portfolio will remain under pressure in the inflationary environment.
- The company has taken price increases or grammage changes for ~50% of its product portfolio in the last year to mitigate the impact of high raw material inflation. Though prices of key commodities have softened recently, management indicated that milk and green coffee costs remain areas of concern and that it does not intend to roll back price hikes for now.
- The e-commerce channel contributed 6.6% of sales and posted 20% YoY growth during 9MCY23 led by quick commerce.
- The company has more than 10,000 distributors and services more than 5.2mn retail outlets in the country. Its direct reach has improved to 1.6mn outlets and indirect reach now stands at 3.6mn outlets.
- NEST has launched 125 products in the last seven years and has 10 more in the pipeline. The company estimates that innovation contributes more than 6% of its domestic sales, which is targeted to rise to 10% in coming years.
- During its analyst meet, NEST shared its 10 mantras for growth: (1) maintaining a consistent balance between growth and profitability, (2) expanding business opportunities with new consumer cohorts, (3) making strong investments in manufacturing and the supply chain, (4) investing in long-term partnerships, (5) expanding and accelerating its rural thrust, (6) embracing the power of analytics and digitisation, (7) accelerating the sustainability journey, (8) focusing on people, (9) using nutrition as a platform for innovation, and (10) enabling a strong impact on communities.
- M&A remains in focus and management indicated that it is looking for a suitable acquisition opportunity.
- The integration of the Purina pet care business is complete and the goal now is to scale up distribution. NEST has global expertise in the pet care business and sees it as a promising category.

- Globally, NEST invests ~US\$ 2bn annually in research & development towards key areas such as new alternate grains, coffee, early life & medical nutrition, and science-based pet nutrition.
- The royalty agreement with parent Nestle SA is up for renewal in Jun'24. The company is yet to take a decision on the revised royalty agreement.

## Valuation methodology

NEST continues to deliver a strong performance in domestic markets supported by high consumer engagement, product launches and uptrading to branded packs in small towns and large villages. In our view, the company is among the best positioned to benefit from the likely shift in demand from unbranded to branded packaged foods. NEST has committed Rs 50bn in capex over CY23-CY25 towards capacity creation for future growth, including a ~Rs 9bn investment in a new Odisha factory. Moreover, it continues to step up innovation and has 10 products in the pipeline for the near future.

The stock is trading at 62.7x/54.2x CY24E/CY25E EPS. Our target two-year forward P/E multiple remains at 65x on CY25E EPS for an unchanged TP of Rs 28,260. We retain BUY as we expect NEST to show sustained, profitable growth underpinned by investments in capacity creation, innovation, premiumisation, and direct reach expansion with a rural focus.

## Key risks

Key downside risks to our estimates are:

- further spikes in food inflation, and
- delayed rural recovery.

## Sector recommendation snapshot

Company	Ticker	Market Cap (US\$ bn)	Price (Rs)	Target (Rs)	Rating
Britannia Industries	BRIT IN	13.2	4,508	5,844	BUY
Dabur India	DABUR IN	11.0	508	669	BUY
Godrej Consumer Products	GCPL IN	12.0	964	1,159	BUY
Hindustan Unilever	HUVR IN	70.8	2,476	3,069	BUY
ITC	ITC IN	65.7	434	523	BUY
Marico	MRCO IN	8.4	537	646	BUY
Nestle India	NEST IN	27.6	23,546	28,260	BUY
Tata Consumer Products	TATACONS IN	10.0	880	994	BUY
Zydus Wellness	ZYWL IN	1.2	1,518	1,556	HOLD

Source: BOBCAPS Research, NSE | Price as of 26 Oct 2023

## Financials

### Income Statement

Y/E 31 Dec (Rs mn)	CY21A	CY22A	CY23E	CY24E	CY25E
<b>Total revenue</b>	<b>147,406</b>	<b>168,969</b>	<b>194,416</b>	<b>221,824</b>	<b>252,190</b>
EBITDA	35,664	37,125	46,097	55,879	63,412
Depreciation	3,910	4,030	5,480	7,177	7,177
EBIT	31,754	33,095	40,617	48,702	56,235
Net interest inc./(exp.)	(2,017)	(1,546)	(1,350)	(1,353)	(1,353)
Other inc./(exp.)	1,202	1,010	1,204	1,331	1,514
Exceptional items	2,365	0	(1,064)	0	0
EBT	28,573	32,560	41,536	48,681	56,397
Income taxes	7,389	8,655	10,652	12,462	14,478
Extraordinary items	0	0	0	0	0
Min. int./Inc. from assoc.	0	0	0	0	0
<b>Reported net profit</b>	<b>21,184</b>	<b>23,905</b>	<b>30,884</b>	<b>36,218</b>	<b>41,919</b>
Adjustments	2,365	0	(1,064)	0	0
<b>Adjusted net profit</b>	<b>23,549</b>	<b>23,905</b>	<b>29,819</b>	<b>36,218</b>	<b>41,919</b>

### Balance Sheet

Y/E 31 Dec (Rs mn)	CY21A	CY22A	CY23E	CY24E	CY25E
Accounts payables	17,482	19,338	23,703	26,221	29,830
Other current liabilities	1,703	2,310	2,310	2,310	2,310
Provisions	34,240	33,659	38,486	43,684	49,445
Debt funds	341	300	300	300	300
Other liabilities	9,112	9,589	9,615	9,643	9,674
Equity capital	964	964	964	964	964
Reserves & surplus	18,500	23,628	28,353	33,895	40,309
Shareholders' fund	19,464	24,592	29,317	34,859	41,273
<b>Total liab. and equities</b>	<b>82,341</b>	<b>89,787</b>	<b>103,731</b>	<b>117,018</b>	<b>132,832</b>
Cash and cash eq.	7,185	9,266	10,761	5,976	6,849
Accounts receivables	1,660	1,919	2,131	2,431	2,764
Inventories	15,927	19,288	21,532	23,820	27,097
Other current assets	1,942	1,963	2,259	2,577	2,930
Investments	7,740	7,775	7,775	7,775	7,775
Net fixed assets	26,530	27,058	34,578	47,401	55,782
CWIP	2,462	3,584	3,584	3,584	3,584
Intangible assets	0	0	0	0	1
Deferred tax assets, net	258	256	256	256	256
Other assets	18,638	18,679	20,855	23,199	25,795
<b>Total assets</b>	<b>82,341</b>	<b>89,787</b>	<b>103,731</b>	<b>117,018</b>	<b>132,832</b>

### Cash Flows

Y/E 31 Dec (Rs mn)	CY21A	CY22A	CY23E	CY24E	CY25E
<b>Cash flow from operations</b>	<b>22,360</b>	<b>27,374</b>	<b>42,950</b>	<b>48,229</b>	<b>55,783</b>
Capital expenditures	(7,348)	(5,499)	(13,000)	(20,000)	(17,000)
Change in investments	(13,523)	1,288	1,475	0	0
Other investing cash flows	1,668	294	(946)	(985)	(1,052)
<b>Cash flow from investing</b>	<b>(19,203)</b>	<b>(3,917)</b>	<b>(12,471)</b>	<b>(20,985)</b>	<b>(18,052)</b>
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	0	0	0	0	0
Interest expenses	(917)	(980)	(1,350)	(1,353)	(1,353)
Dividends paid	(19,283)	(20,247)	(26,158)	(30,677)	(35,505)
Other financing cash flows	0	0	0	0	0
<b>Cash flow from financing</b>	<b>(20,200)</b>	<b>(21,227)</b>	<b>(27,508)</b>	<b>(32,029)</b>	<b>(36,858)</b>
<b>Chg in cash &amp; cash eq.</b>	<b>(17,043)</b>	<b>2,229</b>	<b>2,971</b>	<b>(4,785)</b>	<b>873</b>
<b>Closing cash &amp; cash eq.</b>	<b>7,102</b>	<b>7,791</b>	<b>10,761</b>	<b>5,976</b>	<b>6,849</b>

### Per Share

Y/E 31 Dec (Rs)	CY21A	CY22A	CY23E	CY24E	CY25E
Reported EPS	222.5	247.9	320.3	375.6	434.8
Adjusted EPS	244.2	247.9	309.3	375.6	434.8
Dividend per share	200.0	210.0	271.3	318.2	368.3
Book value per share	201.9	255.1	304.1	361.5	428.1

### Valuations Ratios

Y/E 31 Dec (x)	CY21A	CY22A	CY23E	CY24E	CY25E
EV/Sales	15.4	13.4	11.7	10.2	9.0
EV/EBITDA	63.6	61.1	49.2	40.6	35.8
Adjusted P/E	96.4	95.0	76.1	62.7	54.2
P/BV	116.6	92.3	77.4	65.1	55.0

### DuPont Analysis

Y/E 31 Dec (%)	CY21A	CY22A	CY23E	CY24E	CY25E
Tax burden (Net profit/PBT)	74.1	73.4	74.4	74.4	74.3
Interest burden (PBT/EBIT)	90.0	98.4	102.3	100.0	100.3
EBIT margin (EBIT/Revenue)	21.5	19.6	20.9	22.0	22.3
Asset turnover (Rev./Avg TA)	179.0	188.2	187.4	189.6	189.9
Leverage (Avg TA/Avg Equity)	4.2	3.7	3.5	3.4	3.2
<b>Adjusted ROAE</b>	<b>108.8</b>	<b>97.2</b>	<b>105.3</b>	<b>103.9</b>	<b>101.6</b>

### Ratio Analysis

Y/E 31 Dec	CY21A	CY22A	CY23E	CY24E	CY25E
<b>YoY growth (%)</b>					
Revenue	10.4	14.6	15.1	14.1	13.7
EBITDA	11.4	4.1	24.2	21.2	13.5
Adjusted EPS	13.1	1.5	24.7	21.5	15.7
<b>Profitability &amp; Return ratios (%)</b>					
EBITDA margin	24.2	22.0	23.7	25.2	25.1
EBIT margin	21.5	19.6	20.9	22.0	22.3
Adjusted profit margin	16.0	14.1	15.3	16.3	16.6
Adjusted ROAE	108.8	97.2	105.3	103.9	101.6
ROCE	160.3	133.0	137.1	138.5	135.3
<b>Working capital days (days)</b>					
Receivables	4	4	4	4	4
Inventory	92	91	91	91	91
Payables	101	91	100	100	100
<b>Ratios (x)</b>					
Gross asset turnover	2.3	2.4	5.6	4.7	4.5
Current ratio	1.0	1.1	1.1	1.0	1.0
Net interest coverage ratio	15.7	21.4	30.1	36.0	41.6
<b>Adjusted debt/equity</b>	<b>1.7</b>	<b>1.2</b>	<b>1.0</b>	<b>0.9</b>	<b>0.7</b>

Source: Company, BOBCAPS Research | Note: TA = Total Assets

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**BUY** – Expected return >+15%

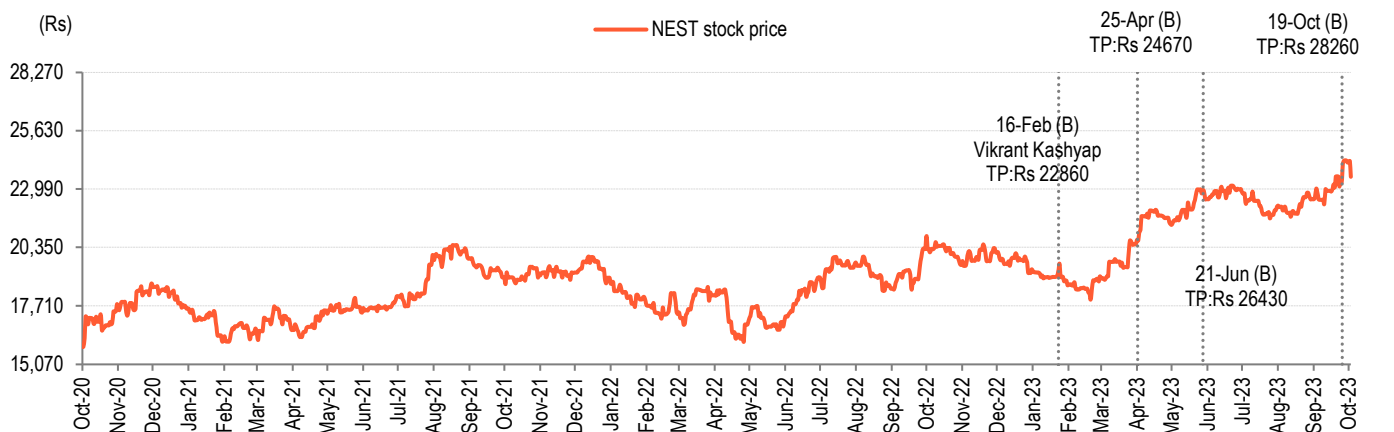
**HOLD** – Expected return from -6% to +15%

**SELL** – Expected return <-6%

**Note:** Recommendation structure changed with effect from 21 June 2021

Our recommendation scale does not factor in short-term stock price volatility related to market fluctuations. Thus, our recommendations may not always be strictly in line with the recommendation scale as shown above.

### Ratings and Target Price (3-year history): NESTLE INDIA (NEST IN)



B – Buy, H – Hold, S – Sell, A – Add, R – Reduce

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