

26 April 2023

Nestlé (Malaysia)

Sales Normalise, Cost Pressures Stay

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NESTLE's 1QFY23 results met expectations. YoY, the quarterly top line grew 9% but bottom line contracted 4% as it held back from passing on higher input costs to consumers. While we expect top line to stay robust on normalising demand, we remain cautious on margins as input cost is likely to stay elevated, at least in 1HFY23. Also, consumers may switch to cheaper alternatives should the high inflation persists. We maintain our earnings forecasts, TP of RM121.18 and UNDERPERFORM call.

1QFY23 PATAMI met expectations at 28% each of both our full-year forecast and the full-year consensus estimate. No DPS declared as historically NESTLE does not pay 1Q dividend.

YoY, top line grew 9%, with growth of both domestic and export sales moderating to 10% and 4%, (vs. 1QFY22 of 15% and 25%) respectively. Its F&B sales volume grew by 9% to RM1.53b, maintaining its position as the largest top line contributor at 83%. However, EBITDA fell 5% as margin was eroded by 2 pts on account of elevated commodities prices and a weaker MYR, though partially mitigated by reduced Covid-19 related expenses. Despite the absence of Cukai Makmur, PATAMI fell 4%.

QoQ, top line grew 12% on account of festivities and the launch of several new offerings such as Kit Kat Pink Ice Cream, an improved Harvest Gourmet (plant-based burger), Starbucks ready-to-drink products and a new edition of Nescafe classic Kopi Kedah (100% Malaysia home-grown coffee beans). Historically, 1Q has always been a strong quarter for NESTLE. EBITDA improved by 33% on operational efficiency gain.

No change to our cautious stance on the following reasons:

- i. Despite its products being staple food items, it faces difficulty passing on higher input cost, as shown by its recent experience which eroded margins.
- ii. While commodity prices have generally softened; they could potentially rebound due to China's reopening, the lingering supply-chain disruptions and the prolonged Russia-Ukraine war.
- iii. Sustained high inflation may eventually drive consumers to down trade, i.e. opting for cheaper brands or alternatives.

We have reflected such trends in our forecasts. Aside from concerns over the loss of market shares, we believe NESTLE has moral as well as ESG obligations not to excessively raise prices of its staple food products that make up the daily diet of the population.

Post results, we make no changes to our FY23F/FY24F earnings. Consequently, our DCF-derived TP remains at RM121.18 (based on WACC of 4.9% and TG of 2%). There is no adjustment to our TP based on ESG given a 3-star rating as appraised by us (see Page 4). **UNDERPERFORM** reiterated.

Risks to our call include: (i) significant fall in commodities prices, (ii) a stronger MYR resulting in lower cost of imported raw materials, (iii) consumers switching to food products of higher quality as purchasing power rises on easing of inflation, and (iv) a swift end to the Russia-Ukraine conflict.

UNDERPERFORM ↔

Price : **RM136.40**
Target Price : **RM121.18** ↔

Share Price Performance



KLCI	1,421.86
YTD KLCI chg	-4.9%
YTD stock price chg	-2.6%

Stock Information

Shariah Compliant	Yes
Bloomberg Ticker	NESZ MK Equity
Market Cap (RM m)	31,985.8
Shares Outstanding	234.5
52-week range (H)	140.60
52-week range (L)	127.20
3-mth avg daily vol	47,815
Free Float	16%
Beta	0.5

Major Shareholders

Nestlé SA	72.6%
Employees Provident Fund	9.0%
Blackrock	1.9%

Summary Earnings Table

FY Dec (RM m)	2022A	2023F	2024F
Turnover	6,664	6,908	7,105
EBIT	903	1,029	1,040
PBT	859	938	944
Net Profit (NP)	620	711	716
PATAMI	620	711	716
Consensus (NP)	-	711	773
Earnings Revision	-	-	-
Core EPS (sen)	264.5	303.0	305.1
Core EPS growth (%)	8.9	14.5	0.7
NDPS (sen)	262.0	270.0	270.0
BVPS (RM)	2.7	3.0	3.4
Core PER (x)	51.6	45.0	44.7
Price/BV (x)	51.1	45.5	40.7
Net Gearing (x)	1.2	1.1	1.1
Net Div. Yield (%)	1.9	2.0	2.0

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Results Highlights

FYE Dec (RM m)	1Q23	4Q22	QoQ Chg	1Q22	YoY Chg	3M23	3M22	YoY Chg
Turnover	1,842.4	1,648.0	11.8%	1,693.8	8.8%	1,842.4	1,693.8	8.8%
Gross Profit	563.4	508.5	10.8%	575.8	-2.2%	563.4	575.8	-2.2%
EBITDA	327.3	245.2	33.5%	346.0	-5.4%	327.3	346.0	-5.4%
EBIT	277.1	197.2	40.5%	297.8	-7.0%	277.1	297.8	-7.0%
PBT/(LBT)	262.3	183.3	43.1%	288.7	-9.1%	262.3	288.7	-9.1%
Taxation	(65.2)	(50.5)	29.1%	(83.5)	-21.9%	(65.2)	(83.5)	-21.9%
Net Profit	197.1	132.9	48.4%	205.2	-3.9%	197.1	205.2	-3.9%
PATAMI	197.1	132.9	48.4%	205.2	-3.9%	197.1	205.2	-3.9%
Core EPS (sen)	84.1	56.7	48.4%	87.5	-3.9%	84.1	87.5	-3.9%
DPS (sen)	-	122.0	-100.0%	0.0	N.m	-	-	N.m
Gross Margin	30.6%	30.9%		34.0%		30.6%	34.0%	
EBITDA Margins	17.8%	14.9%		20.4%		17.8%	20.4%	
EBIT Margin	15.0%	12.0%		17.6%		15.0%	17.6%	
Pre-Tax Margin	14.2%	11.1%		17.0%		14.2%	17.0%	
Net Profit Margin	10.7%	8.1%		12.1%		10.7%	12.1%	
PATAMI Margin	10.7%	8.1%		12.1%		10.7%	12.1%	
Tax Rate	-24.8%	-27.5%		-28.9%		-24.8%	-28.9%	

Source: Company, Kenanga Research

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Peer Comparison

Name	Rating	Last Price (RM)	Target Price (RM)	Upside (%)	Market Cap (RM'm)	Shariah Compliant	Current FYE	Core EPS (sen)		Core EPS Growth		PER (x) - Core Earnings		PBV (x)	ROE (%)	Net Div. (sen)	Net Div Yld (%)
								1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.
CONSUMER																	
AEON CO. (M) BHD	OP	1.26	1.80	42.86%	1,769.0	Y	12/2023	9.1	10.0	15.2%	9.4%	13.8	12.6	1.0	7.3%	4.0	3.2%
DUTCH LADY MILK INDUSTRIES BHD	MP	26.40	29.78	12.80%	1,689.6	Y	12/2023	139.4	135.3	-64.0%	-2.9%	18.9	19.5	3.8	21.7%	50.0	1.9%
FRASER & NEAVE HOLDINGS BHD	OP	26.88	26.11	-2.86%	9,859.0	Y	09/2023	118.6	129.1	13.5%	8.8%	22.7	20.8	3.1	14.1%	62.5	2.3%
MR D.I.Y.	MP	1.59	1.85	16.35%	14,998.8	Y	12/2023	6.7	7.4	32.4%	11.4%	23.9	21.4	8.6	39.4%	3.5	2.2%
MYNEWS HOLDINGS BHD	UP	0.450	0.410	-8.89%	307.0	N	10/2023	1.0	2.2	-135.8%	127.7%	47.2	20.7	1.4	2.8%	0.0	0.0%
NESTLE (MALAYSIA) BHD	UP	136.50	121.18	-11.22%	32,009.3	Y	12/2023	303.0	305.1	14.6%	0.7%	45.0	44.7	45.5	106.9%	270.0	2.0%
PADINI HOLDINGS BHD	OP	4.03	6.00	48.88%	2,651.4	Y	06/2023	35.8	39.7	53.0%	10.8%	11.2	10.2	2.7	25.3%	10.0	2.5%
POWER ROOT BHD	OP	2.09	2.70	29.19%	891.9	Y	03/2023	13.1	14.3	108.8%	9.5%	16.0	14.6	2.7	18.0%	10.0	4.8%
QL RESOURCES BHD	OP	5.75	6.66	15.83%	13,993.5	Y	03/2023	14.3	17.7	60.3%	23.5%	40.2	32.5	4.4	12.1%	6.0	1.0%
Sector Aggregate					80,489.5					20.1%	9.3%	29.6	27.1	6.4	21.4%		2.2%
TOBACCO PRODUCTS & BREWERIES																	
BRITISH AMERICAN TOBACCO (M) BHD	MP	10.66	12.00	12.57%	3,043.7	N	12/2023	102.1	103.5	11.0%	1.4%	10.4	10.3	7.7	75.4%	99.0	9.3%
CARLSBERG BREWERY MALAYSIA BHD	MP	21.40	23.05	7.71%	6,543.0	N	12/2023	114.6	126.4	13.9%	10.3%	18.7	16.9	25.1	145.0%	100.0	4.7%
HEINEKEN MALAYSIA BHD	MP	27.54	27.70	0.58%	8,319.8	N	12/2023	138.9	147.8	12.3%	6.4%	19.8	18.6	21.1	94.8%	138.9	5.0%
Sector Aggregate					17,906.5					12.5%	6.3%	16.8	15.8	17.9	105.0%		6.3%

Source: Bloomberg, Kenanga Research

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Stock ESG Ratings:

	Criterion	Rating				
GENERAL	Earnings Sustainability & Quality	★	★	★	★	
	Corporate Social Responsibility	★	★	★	★	
	Management/Workforce Diversity	★	★	★		
	Accessibility & Transparency	★	★	☆		
	Corruption-Free Pledge	★	★	★		
	Carbon-Neutral Initiatives	★	★	★		
	OVERALL		★	★	★	
SPECIFIC	Employee Training	★	★	★		
	Energy Efficiency	★	★			
	Food Safety & Quality	★	★	★	★	
	GMO	★	★	★	★	
	Nutrition, Health & Wellness	★	★	★	☆	
	Occupational Health & Safety	★	★	★	☆	
	Renewable Energy	★	★	★	★	
	Sustainable Supply Chain	★	★	★	★	
	Waste Disposal/Pollution Control	★	★	★	★	
	Water Efficiency	★	★	☆		

☆ denotes half-star
 ★ -10% discount to TP
 ★★ -5% discount to TP
 ★★★ TP unchanged
 ★★★★★ +5% premium to TP

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Stock Ratings are defined as follows:**Stock Recommendations**

OUTPERFORM	: A particular stock's Expected Total Return is MORE than 10%
MARKET PERFORM	: A particular stock's Expected Total Return is WITHIN the range of -5% to 10%
UNDERPERFORM	: A particular stock's Expected Total Return is LESS than -5%

Sector Recommendations***

OVERWEIGHT	: A particular sector's Expected Total Return is MORE than 10%
NEUTRAL	: A particular sector's Expected Total Return is WITHIN the range of -5% to 10%
UNDERWEIGHT	: A particular sector's Expected Total Return is LESS than -5%

*****Sector recommendations are defined based on market capitalisation weighted average expected total return for stocks under our coverage.**

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