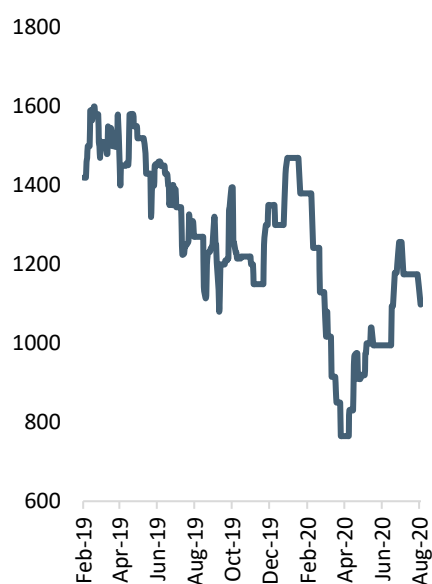




Nestle Nigeria Plc. (NESTLE.NL)

Rating	NEUTRAL
Price	₦1175.00
FVE	₦1239.21
52-week range	₦750- ₦1469.90
Market Cap. (₦bn)	931,371
1-month Avg. Vol	92,809
Curr. PE	22.6x

NESTLE .NL – Share Price Trend



Analyst(s)

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Stock Report

Flattish revenue and elevated cost drag earnings

- Nestle's Q2 2020 result revealed a 20.7% YoY decline in earnings to ₦10.6 billion (EPS: ₦13.41). Aside recording a flat revenue over the period, earnings was dragged further by increased input cost. Meanwhile, Q2 20 EPS missed our expectation by 8% stemming from lower than expected sales. Accordingly, H1 2020 earnings printed at ₦21.8 billion with related EPS at ₦27.53 (-16.8% YoY). The company trades at a current P/E of 22.6x and forward P/E of 19.1x, relative to 3-year historical average of 25.6x. We have cut our FVE to ₦1288.63 (previously: ₦1404.4) which translates to a NEUTRAL rating for the stock.**
- COGS pressure surfaces amidst flattish revenue:** Over the review period, revenue declined marginally by 0.3% YoY stemming largely from lower sales in its beverage segment (-7.1% YoY). Food sales at the other end grew by 4.1% YoY. For us, the growth in the food business shows a recovery from Q1 outturn which is positive for the business. However, increased pricing and shift in consumer preferences to essential products led to the decline in beverage segment. Elsewhere, input cost increased by 14.3% YoY, causing a 751-bps contraction in gross margin to 41.3%. While management attributed this to commodity inflation and covid-related cost, we believe the major pressure stemmed largely from currency devaluation which occurred in March.
- Though operating expense declined with OPEX to sales at 17.5% (Q2 19: 18.7%), the depressed top line left operating margin lower at 23.7% (Q2 19: 30.1%). Further pressure stemmed from low interest rate environment and increased borrowing. As a result, the company reported a net finance expense of ₦382.6 million (vs Q2 19: ₦32.2 million) which in turn translated to PBT of ₦16.4 billion and PAT of ₦10.6 billion (-20.7% YoY).
- Taking a peek at the balance sheet,** the company took up new long-term borrowings totaling ₦5.8 billion, after settling all its long term debt in Q1. Furthermore, mirroring reduced profitability over the review period, retained earnings dipped to ₦31.2 billion (Q1 20: ₦56.2 billion).
- We cut our revenue expectation by 6.2% to ₦283.7 billion as we now expect the flattish trend in revenue to persist, but maintain our view of a contraction in gross margin hinged on the technical devaluation. The impact is a cut in our FVE to ₦1239.21 (previously:

₹1404.4). Relative to the last closing price, it represents a 5.5% upside and translates to a **NEUTRAL** rating.

Summary of Results and Forecasts - ₹'000

ANNUAL

Income Statement (₹'m) *	2018A	2019A	2020F	2021F	2022F
Revenue	266,275	284,035	283,751	307,530	332,132
COGS	-152,354	-155,888	-157,482	-168,219	-181,012
Gross Profit	113,920	128,147	126,269	139,311	151,120
Operating Cost	-53,279	-56,085	-55,899	-59,968	-64,766
Operating Profit	60,641	72,062	70,370	79,343	86,354
Net finance Cost	890	938	686	-183	-1107
PBT	59,751	71,124	69,685	79,526	87,461
Tax	16,743	25,441	24,390	23,858	26,238
PAT	43,008	45,683	45,295	55,668	61,223
Balance Sheet (₹ '000) *					
Fixed Assets	79,600	86,337	80,603	79,695	78,942
Stocks	82,734	107,037	96,774	99,486	98,085
Trade debtors	43,403	66,722	56,750	44,592	48,159
Cash & other bank balances	15,762	6,978	17,976	31,343	24,584
Total Assets	162,334	193,374	177,376	179,181	177,027
Liabilities					
Trade Creditors	60,384	78,400	79,201	84,601	91,035
Non-current Liabilities	19,996	22,281	22,392	22,504	22,619
Total liabilities	101,926	112,114	147,817	142,548	148,109
Shareholders' fund	44,878	50,220	45,558	35,931	32,174
Key Ratios					
Gross Margin	2018E	2019F	2020F	2021E	2022E
	43%	45%	45%	45%	46%
EBIT Margin	23%	25%	25%	26%	26%
PBT Margin	22%	25%	25%	26%	26%
Net Margin	16%	16%	16%	18%	18%
EPS	54.26	57.63	57.14	70.23	77.24
P/E	29.12	25.50	20.56	16.73	15.21
EV/EBITDA	17.54	14.73	11.76	10.39	9.65
ROA	28%	26%	24%	31%	34%

ARM ratings and recommendations

ARM now employs a two-tier rating system which is based on systemic importance of the security under review and the deviation of our target price for the stock from current market price. We characterize systemic importance as a function of a stock's ranking among the group of top 20 stocks by NSE market capitalization over a trailing 6-month period (minimum) to the review date. We adopt a 5-point rating system for this category of stocks and a 3-point rating system for stocks outside this group. The choice of top 20 stocks arises from the consideration that this group of stocks constitutes >75% of overall market capitalization and stocks outside this group are generally less liquid and individually account for <<1% of market capitalization. For stocks in both categories, the basis for ratings subject to target price deviation is outlined below:

TOP 20		NON-TOP 20	
Rating	Deviation	Rating	Deviation
STRONG BUY	>20%	BUY	>20%
OVERWEIGHT	10% — 20 %	NEUTRAL	5% — 20 %
NEUTRAL	0% — 10 %	SELL	<5%
UNDERWEIGHT	-5% — 0%		
SELL	<-5%		

RECOMMENDATION KEY	
Rating	Recommendation
BUY	Accumulate security to a substantial extent constrained only by portfolio diversification considerations
OVERWEIGHT	Accumulate security to an extent moderated by cognizance of its benchmark weight
NEUTRAL	Maintain status quo for security with respect to current holding—i.e. keep if already holding and don't buy otherwise—subject to real portfolio constraints
UNDERWEIGHT	Minimize exposure to security taking cognizance of its index weighting
SELL	Sell-off security completely from portfolio

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