

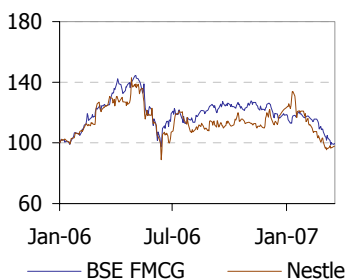
Nestle India

 Relative to sector: **Outperformer**

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Relative Performance



Source: Bloomberg, ENAM Research

Stock data

No. of shares	: 96mn
Market cap	: Rs 86.8bn
52 week high/low	: Rs 1,387/ Rs 800
Avg. daily vol. (6mth)	: 34,800 shares
Bloomberg code	: NEST IN
Reuters code	: NEST.BO

Shareholding (%) Dec-06 QoQ chg

Promoters	: 61.9	0.0
FII's	: 9.1	0.4
MFs / UTI	: 3.8	(0.3)
Banks / FIs	: 5.7	(0.0)
Others	: 19.6	(0.1)

COST PRESSURES OVERSHADOW GROWTH

Nestle India reported net revenues of Rs 7.36bn (↑ 18%), EBIDTA (excluding contingent provisioning) of Rs 1.2bn (↑ 2%) and adj. net profit of Rs 631mn (↓ 16%) in Q4CY06. Gross revenue growth of 11% YoY for CY06 constituted real internal growth (RIG) of ~9% and selling price increase of ~2%. Continuing inflationary cost environment alongside lower than expected price increases, resulted in an EBIDTA margin compression of 263 bps in Q4CY06 (97 bps for CY06). Higher provision for Q4CY06 contingencies, further impacted adj. PAT.

Highlights –Q4CY06

- **Domestic growth a given:** Domestic sales growth (↑ 16% YoY) continues to be encouraging. While Q4CY06 exports grew by 37% YoY due to a lower base effect, full year growth stood at 8% due to continuing decline in coffee exports to Russia and Japan.
- **The tug of war - Inflation vs. pricing power.** Raw material and packing cost were up by 26% YoY in Q4CY06. An overall ~2% price increase in CY06 was less than adequate to offset cost pressure. However we have not ruled out selective price increases by Q2CY07, especially in nutrition and prepared foods segments. The prices of raw materials; coffee, wheat and sugar, have begun to soften in CY07. Expect this dual benefit to translate into better operating margins Q2CY07 onwards.
- **Expect more variants across categories:** In CY06 Nestle introduced a number of new products across categories. It added Indianised variants in its hugely popular Maggi portfolio, and healthier options in the milk products and chocolates categories.

With domestic consumption intact, we expect revenue growth of 12% CAGR YoY and earnings growth of 19% CAGR over the next 3 years. We believe current valuations reflect pessimism about continuing cost inflation and inept pricing power. At CMP (Rs 901), the stock trades at 23x CY07E and 19x CY08E earnings. We upgrade the stock to sector **Outperformer** rating.

Financial summary

Y/E Dec	Sales (Rs.mn)	Adj. PAT (Rs. mn)	Consensus EPS* (Rs.)	EPS (Rs.)	Change YoY (%)	P/E (x)	RoE (%)	RoCE (%)	EV/EBIDTA (x)	DPS (Rs.)
2005	24,750	3,092	-	32.1	22	28.1	91.8	134.8	17.3	25.0
2006	28,161	3,154	-	32.7	2	27.5	84.6	124.2	16.5	25.5
2007E	31,779	3,770	43.2	39.1	20	23.0	91.1	135.5	14.2	30.0
2008E	35,482	4,570	48.4	47.4	21	19.0	97.1	147.2	11.8	35.0

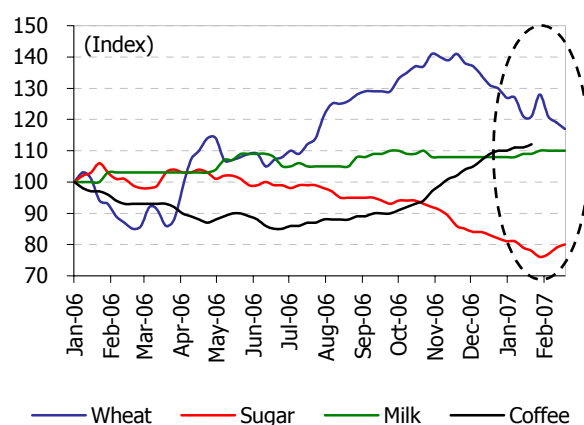
Source: *Consensus broker estimates, Company, ENAM estimates

Results Update

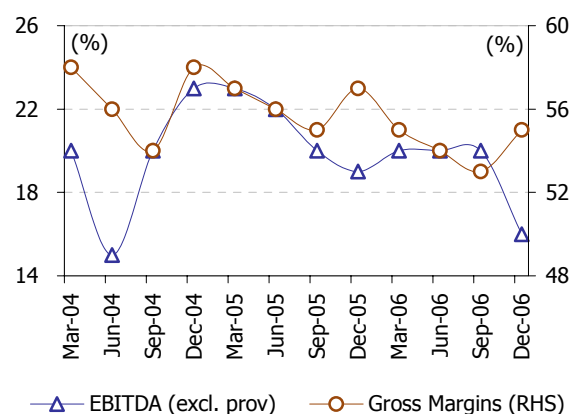
(Rs. mn)	Quarter ended					12 months ended		
	Dec-06	Dec-05	% Chg	Sep-06	% Chg	Dec-07E	Dec-06	% Chg
Net Sales	7,363	6,228	18.2	7,227	1.9	31,779	28,161	12.8
EBIDTA	1,039	1,156	(10.1)	1,383	(24.8)	6,129	5,270	16.3
Other income	73	58	27.0	47	56.3	245	206	18.9
PBIDT	1,112	1,214	(8.4)	1,429	(22.2)	6,374	5,476	16.4
Depreciation	177	154	15.2	168	5.5	663	663	(0.1)
Interest	1	0	250.0	0	250.0	0	4	(100.0)
PBT	934	1,060	(11.9)	1,261	(26.0)	5,711	4,809	18.8
Tax	303	305	(0.7)	431	(29.7)	1,942	1,654	17.4
Adjusted PAT	631	754	(16.4)	830	(24.0)	3,770	3,154	19.5
Extra ordinary income/ (exp.)	(6)	(13)	-	0	-	0	(4)	-
Reported PAT	625	742	(15.8)	830	(24.7)	3,770	3,151	19.6
No. of shares (mn)	97	96	-	96	-	96	96	-
EBITDA margins (%)	14.1	18.6	-	19.1	-	19.3	18.7	-
PBIDT margins (%)	15.1	19.5	-	19.8	-	20.1	19.4	-
EPS - annualized (Rs.)	26.1	31.3	(16.5)	34.4	(24.1)	39.1	32.7	19.5

Source: Company, ENAM Research

Key raw material price trend

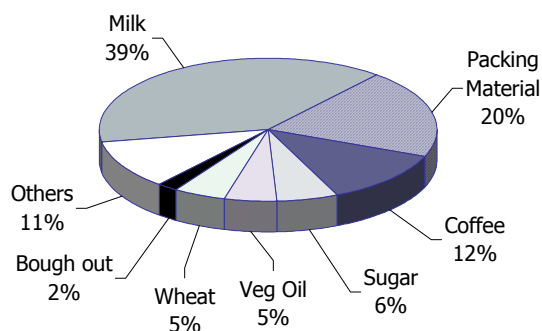


Gross margins & EBITDA trend

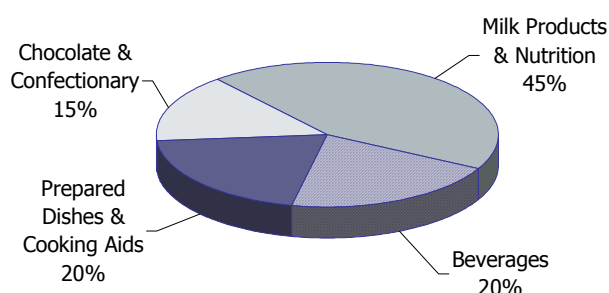


Source: CMIE, Bloomberg, Company

Material cost breakup



Sales mix



Source: Company

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