

RESULT UPDATE

LARGE CAP

Share Data

Reuters code	NEST.BO
Bloomberg code	NEST IN
Market cap. (US\$ mn)	7,360
6M avg. daily turnover (US\$ mn)	3.7
Issued shares (mn)	96
Target price (Rs)	3,806

Performance (%)	1M	3M	12M
Absolute	(5)	(8)	30
Relative	(1)	0	17

Valuation Ratios

Yr to 31 Dec	CY11E	CY12E
EPS (Rs)	104.4	126.9
+/- (%)	20.3	21.5
PER (x)	33.0	27.2
PBV (x)	28.1	20.9
Dividend/Yield (%)	1.7	2.1
EV/Sales (x)	4.5	3.8
EV/EBITDA (x)	21.5	17.6

Major shareholders (%)

Promoters	63
FII's	11
MF's	2
BFSI's	6
Public & Others	18

Financial highlights

(Rs mn)	4QCY09	4CY10	YoY (%)	CY09	CY10	YoY (%)	CY11E	YoY (%)	CY12E	YoY (%)
Net sales	13,518	16,710	23.6	51,294	62,548	21.9	74,315	18.8	87,817	18.2
EBITDA	1,981	3,298	66.4	10,345	12,497	20.8	15,405	23.3	18,930	22.9
EBITDA margin (%)	14.7	19.7	—	20.2	20.0	—	20.7	—	21.6	—
Other income	106	139	31.6	378	427	12.8	396	(7.1)	436	10.0
Interest	(5)	(1)	(79.6)	(14)	(11)	(23.6)	(15)	40.2	(15)	—
Depreciation	(307)	(358)	16.7	(1,113)	(1,278)	14.8	(1,716)	34.3	(2,238)	30.5
PBT before extraordinary items	1,775	3,078	73.4	9,596	11,635	21.2	14,071	20.9	17,112	21.6
Extraordinary items	(204)	(183)	—	(426)	(184)	—	—	—	—	—
Tax (incl. deferred)	(442)	(861)	94.6	(2,620)	(3,265)	24.6	(4,004)	22.6	(4,880)	21.9
PAT	1,129	2,034	80.1	6,550	8,187	25.0	10,067	23.0	12,233	21.5
Adjusted PAT	1,333	2,217	66.3	6,976	8,370	20.0	10,067	20.3	12,233	21.5
Adjusted EPS (Rs)	13.8	23.0	66.3	72.4	86.8	20.0	104.4	20.3	126.9	21.5

Nestle India

Maintain Outperformer

Price: Rs 3,451

BSE Index: 18,212

21 February 2011

4QCY10 Result – Strong performance...Impressive margin expansion...

Nestle India results were in line with our expectations on the topline with the company reporting a 23.6% growth in net sales at Rs 16.7 bn, driven by strong domestic sales growth. A 500 bps improvement in the EBITDA margin at 19.7% (higher employee cost in the base; 130 bps savings in other expenditure; 20 bps improvement in the gross margin) and higher other income led a strong 66% increase in the adjusted net profit; much ahead of expectations.

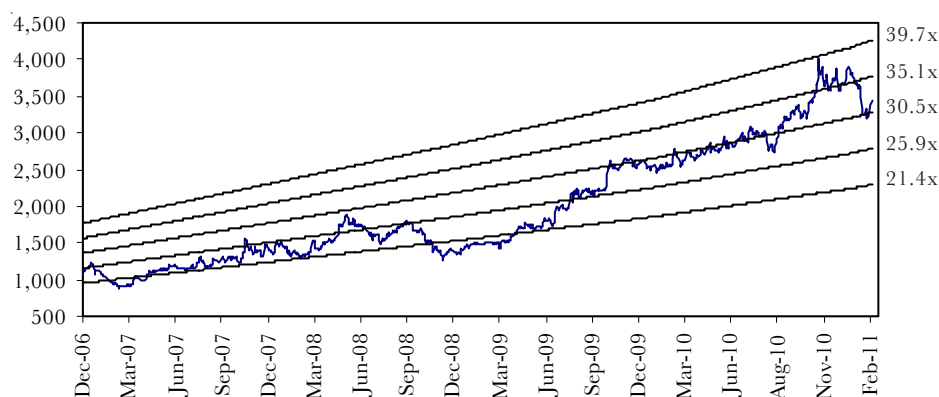
The strong domestic revenue growth continues to impress and is testament of continued robust growth of the categories Nestle operates in as well as the strong positioning of Nestle in these key categories. The improvement in gross margins further strengthens our view on the pricing power and also indicative of the benefits of scale enjoyed by the company, especially with the strong revenue growth. The company has invested ~Rs 5.5 bn in capacity expansion in CY10 and we factor ~Rs 16 bn increase investments in capacity expansion (both greenfield and brownfield) for the next two years, given the company's aggressive capacity expansion plan. Though Nestle could raise debt in the short term (to cover the cash flow to capex lag), we believe strong operating cash flows (~Rs 27.7 bn estimated over the next two years) will be sufficient to cover its capex cost, assuming the current CY10 dividend payout ratios for CY11E and CY12E.

Though dividend payout and return ratios in CY11E and CY12E are likely to be lower than the company's historical average to fund the expansions and capitalise the balance sheet, the huge capacity expansion plan is indicative of the management's confidence on the robust growth outlook for the future for the company. We marginally revise our estimates downwards by 2% to factor higher depreciation and lower other income for CY11 and CY12. We remain positive on Nestle's strong growth outlook and maintain our Outperformer rating on the stock with a revised target price of Rs 3,806 (revised from Rs 3,900).

Highlights

- Net sales growth was driven by a 26.6% domestic sales growth, indicative of an impressive volume growth (estimated in the high teens). Export sales declined by 17%, likely impacted by adverse currency movements as well as capacity constraints.
- A 20 bps YoY and a 150 bps QoQ improvement in the gross margins at 52.4% (highest in the last six quarters) was a positive surprise given the continued inflationary pressure on the company's key inputs of milk, wheat, vegetable oils and coffee.
- A 14% decline in staff costs (due to a one off actuarial adjustment in the base) as well as a 130 bps saving in other expenditure led a 500 bps EBITDA margin expansion at 19.7%, boosting overall profitability.
- For CY10, net sales increased by 21.9% to Rs 62.55 bn with domestic sales increasing by 22.9%. In spite of the significant input cost pressure, the EBITDA margins declined by only 20 bps to 20%, aided by a one off increase in employee costs in CY09. Led by robust sales growth and higher other income, adjusted profit increased by 20% to Rs 8.37 bn for the year.
- As expected, the company has reduced its dividend payout ratio (from ~84% to 67%) for CY10 due fund its huge capex programme. Over the next three years (CY10-13), the company is expected to invest ~Rs 17 bn in brownfield expansion in addition to greenfield projects that are expected to be undertaken. To support the capex programme, the company is seeking shareholder approval to increase borrowing limits to Rs 25 bn and has also received approval of the RBI to raise up to US\$ 450 mn in ECBs. Currently, the company has no debt on the books and a cash balance of Rs 2.55 bn as of 31 December 2010.

PER Band



Source: B&K Research

Income Statement

Yr end 31 Dec (Rs mn)	CY09	CY10	CY11E	CY12E
Net sales	51,294	62,548	74,315	87,817
<i>Growth (%)</i>	<i>18.6</i>	<i>21.9</i>	<i>18.8</i>	<i>18.2</i>
Operating expenses	(40,949)	(50,051)	(58,910)	(68,887)
Operating profit	10,345	12,497	15,405	18,930
EBITDA	10,345	12,497	15,405	18,930
<i>Growth (%)</i>	<i>19.8</i>	<i>20.8</i>	<i>23.3</i>	<i>22.9</i>
Depreciation	(1,113)	(1,278)	(1,716)	(2,238)
Other income	378	427	396	436
EBIT	9,610	11,646	14,086	17,127
Interest paid	(14)	(11)	(15)	(15)
Pre-tax profit	9,596	11,635	14,071	17,112
(before non-recurring)				
Non-recurring items	(426)	(184)	0	0
Pre-tax profit	9,170	11,451	14,071	17,112
(after non-recurring)				
Tax (current + deferred)	(2,620)	(3,265)	(4,004)	(4,880)
Net profit (before Minority Interest, Pref. Dividend, etc.)	6,550	8,187	10,067	12,233
Reported PAT	6,550	8,187	10,067	12,233
Adjusted net profit	6,976	8,370	10,067	12,233
<i>Growth (%)</i>	<i>23.5</i>	<i>20.0</i>	<i>20.3</i>	<i>21.5</i>

Balance Sheet

Yr end 31 Dec (Rs mn)	CY09	CY10	CY11E	CY12E
Cash & marketable securities	1,556	2,553	576	44
Other current assets	7,010	7,907	9,496	11,085
Investments	2,033	1,507	1,500	1,500
Net fixed assets	9,758	13,617	19,519	24,969
Other non-current assets	468	0	468	468
Total assets	20,824	25,584	31,560	38,066
Current liabilities	14,224	16,696	18,927	21,321
Other non-current liabilities	788	333	788	788
Total liabilities	15,012	17,029	19,715	22,109
Share capital	964	964	964	964
Reserves & surplus	4,849	7,591	10,880	14,992
Shareholders' funds	5,813	8,555	11,845	15,956
Total equity & liabilities	20,824	25,584	31,560	38,066
Capital employed	6,601	8,888	12,633	16,744

Cash Flow Statement

Yr end 31 Dec (Rs mn)	CY09	CY10	CY11E	CY12E
Pre-tax profit	9,170	11,451	14,071	17,112
Depreciation	1,113	1,278	1,716	2,238
Change in working capital	1,416	1,550	667	806
Total tax paid	(2,676)	(3,226)	(4,042)	(4,880)
Cash flow from oper. (a)	9,023	11,052	12,411	15,277
Capital expenditure	(2,064)	(5,136)	(7,618)	(7,688)
Change in investments	(1,684)	526	7	0
Others	(185)	(1)	0	(0)
Cash flow from inv. (b)	(3,933)	(4,611)	(7,611)	(7,688)
Free cash flow (a+b)	5,090	6,441	4,800	7,590
Dividend (incl. tax)	(5,471)	(5,471)	(6,768)	(8,122)
Others	1	26	(10)	0
Cash flow from fin. (c)	(5,470)	(5,445)	(6,778)	(8,122)
Net chg in cash (a+b+c)	(380)	997	(1,978)	(532)

Key Ratios

Yr end 31 Dec (%)	CY09	CY10	CY11E	CY12E
Adjusted EPS (Rs)	72.4	86.8	104.4	126.9
Growth	23.5	20.0	20.3	21.5
Book NAV/share (Rs)	60.3	88.7	122.8	165.5
Dividend/share (Rs)	48.5	48.5	60.0	72.0
Dividend payout ratio	78.4	65.4	67.2	66.4
Tax	28.6	28.5	28.5	28.5
EBITDA margin	20.2	20.0	20.7	21.6
EBIT margin	18.7	18.6	19.0	19.5
RoCE	159.0	150.4	130.9	116.6
Net debt/Equity	(26.8)	(29.8)	(4.9)	(0.3)

Valuations

Yr end 31 Dec (x)	CY09	CY10	CY11E	CY12E
PER	47.7	39.7	33.0	27.2
PCE	41.1	34.5	28.2	23.0
Price/Book	57.2	38.9	28.1	20.9
Yield (%)	1.4	1.4	1.7	2.1
EV/Net sales	6.5	5.3	4.5	3.8
EV/EBITDA	32.0	26.5	21.5	17.6

Du Pont Analysis – ROE

Yr end 31 Dec (x)	CY09	CY10	CY11E	CY12E
Net margin (%)	13.6	13.4	13.5	13.9
Asset turnover	2.7	2.7	2.6	2.5
Leverage factor	3.6	3.2	2.8	2.5
Return on equity (%)	132.3	116.5	98.7	88.0

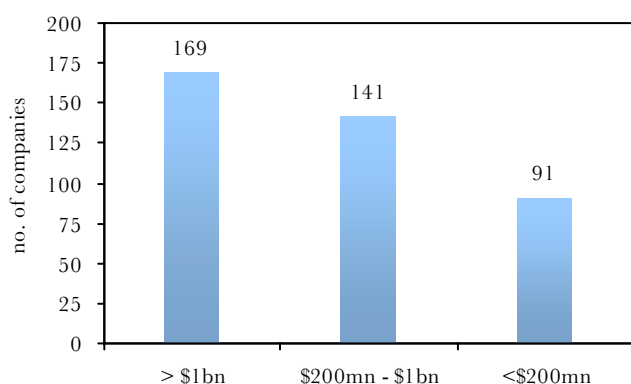
Harit Kapoor
harit.kapoor@bksec.com
+91-22-4031 7130

Ashit Desai
ashit.desai@bksec.com
+91-22-4031 7132

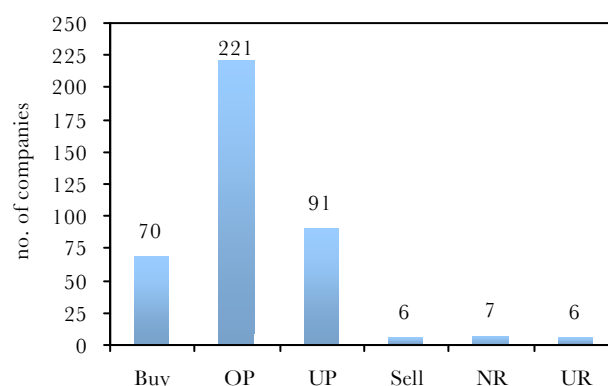
Analyst Declaration: We, Harit Kapoor & Ashit Desai, hereby certify that the views expressed in this report accurately reflect our personal views about the subject securities and issuers. We also certify that no part of our compensation was, is, or will be, directly or indirectly, related to the specific recommendation or view expressed in this report.

B&K Universe Profile

By Market Cap (US\$ mn)



By Recommendation



B&K Securities is the trading name of Batlivala & Karani Securities India Pvt. Ltd.

B&K Investment Ratings:

1. **BUY:** Potential upside of > +25% (absolute returns)
2. **OUTPERFORMER:** 0 to +25%
3. **UNDERPERFORMER:** 0 to -25%
4. **SELL:** Potential downside of < -25% (absolute returns)

All rights reserved. No part of this publication may be reproduced, stored in a retrieval system, or transmitted, in any form or by any means, electronic, mechanical, print, publishing, photocopying, recording or otherwise without the permission of Batlivala & Karani Securities India Pvt. Ltd. Any unauthorized act in relation to all or any part of the material in this publication may call for appropriate statutory proceedings.

The information contained herein is confidential and is intended solely for the addressee(s). Any unauthorized access, use, reproduction, disclosure or dissemination is prohibited. This information does not constitute or form part of and should not be construed as, any offer for sale or subscription of or any invitation to offer to buy or subscribe for any securities. The information and opinions on which this communication is based have been compiled or arrived at from sources believed to be reliable and in good faith, but no representation or warranty, express or implied, is made as to their accuracy, correctness and are subject to change without notice. Batlivala & Karani Securities India P Ltd and/ or its clients may have positions in or options on the securities mentioned in this report or any related investments, may effect transactions or may buy, sell or offer to buy or sell such securities or any related investments. Recipient/s should consider this report only for secondary market investments and as only a single factor in making their investment decision. The information enclosed in the report has not been vetted by the compliance department due to the time sensitivity of the information/document. Some investments discussed in this report have a high level of volatility. High volatility investments may experience sudden and large falls in their value causing losses when the investment is realized. Those losses may equal your original investment. Some investments may not be readily realizable and it may be difficult to sell or realize those investments, similarly it may prove difficult for you to obtain reliable information about the value, risks to which such an investment is exposed. Neither B&K Securities nor any of its affiliates shall assume any legal liability or responsibility for any incorrect, misleading or altered information contained herein.

B & K SECURITIES INDIA PRIVATE LTD.

Equity Research Division: City Ice Bldg., 298, Ground/1st Floor, Perin Nariman Street, Behind RBI, Fort, Mumbai - 400 001, India. Tel.: 91-22-4031 7000, Fax: 91-22-2263 5020/30.
Registered Office: Room No. 3/4, 7 Lyons Range, Kolkata - 700 001. Tel.: 91-33-2243 7902.

B&K Research is also available on Bloomberg <BNKI>, Thomson First Call & Investext.