

26 April 2018 | 1QFY18 Briefing Note

## Nestlé (Malaysia) Berhad

*Profit margin expected to pick up in the coming quarters*

### INVESTMENT HIGHLIGHTS

- **Gross profit is expected to improve in coming quarters as benefit from lower commodities price kicks-in**
- **Nevertheless, earnings growth will be partially mitigated by higher A&P expenses and higher effective tax rate**
- **Better earnings prospect in FY18 have been priced into the current valuation**
- **Maintain NEUTRAL stance with a revised TP of RM132.32**

**Gross profit is expected to improve in coming quarters.** To recall Nestlé recorded a marginal earnings growth of +0.2%yoy to RM231.2m for 1QFY18. This is within management's expectation as the group is yet to benefit from a lower cost of sales as agricultural commodity prices have been stabilising and Ringgit has strengthen against the USD. In the coming quarters, gross profit is expected to improve as higher value inventories had been cleared off.

**Earnings will be impacted by higher A&P expenses and taxes.** While we expect future earnings to improve, its growth is expected to be partially mitigated by: (i) higher projected advertising and promotional (A&P) expenses in FY18 compared to FY17 to take advantage of the improving consumer sentiment and; (ii) higher effective tax rate of 22-23% as the Halal tax incentives had been fully claimed.

**Impact to earnings.** We are maintaining our earnings forecast post-analyst briefing.

**Maintain NEUTRAL stance with a revised TP of RM132.32.** Nestlé's valuation is currently stretched with a forward PER of 47x in comparison to the average three-year PER of 28x before the inclusion to both KLCI and MSCI Malaysia indices. We believe that the expectation of better earnings prospect in FY18 have been priced into the current valuation. We are maintaining our **NEUTRAL** call on Nestlé with a revised target price of **RM132.32** per share (previously RM116.50 per share) as we roll forward our valuation base year to FY19. Our target price is based on dividend discount model with the assumption that required return on equity is of 5.00% and sustainable dividend growth rate of 2.4%.

**Maintain NEUTRAL**

**Revised Target Price (TP): RM132.32**  
*(Previously RM116.50)*

RETURN STATS	
Price (25 April 2018)	RM139.10
Target Price	RM132.32
Expected Share Price Return	-4.9%
Expected Dividend Yield	+2.3%
<b>Expected Total Return</b>	<b>-2.6%</b>

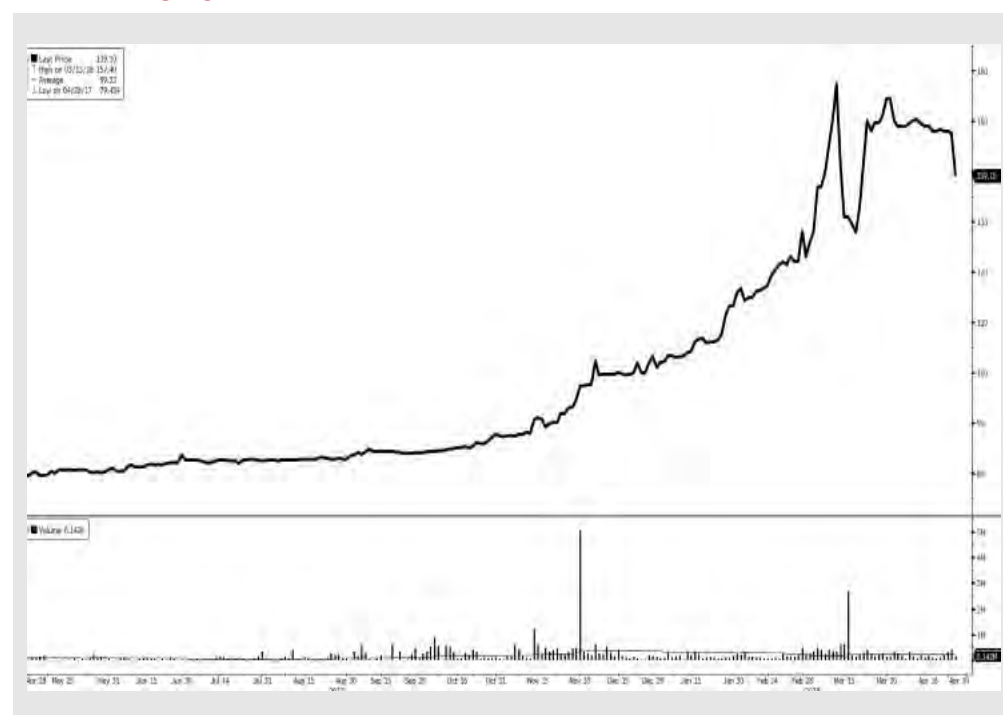
STOCK INFO	
KLCI	1,851.93
Bursa / Bloomberg	4707/ NESZ MK
Board / Sector	Main/Consumer
Syariah Compliant	Yes
Issued shares (mil)	234.5
Market cap. (RM'm)	34,618.95
Price over NA	43.15x
52-wk price Range	RM81.0-RM163.0
Beta (against KLCI)	0.58
3-mth Avg Daily Vol	0.25m
3-mth Avg Daily Value	RM34.0m
Major Shareholders (%)	
NESTLE SA	72.61
EPF	6.95
PNB & Associated Funds	2.72

## INVESTMENT STATISTICS

FYE Dec (RMm)	2015	2016	2017	2018F	2019F
Revenue	4,838.0	5,063.5	5,260.5	5,534.7	5,811.4
Cost of sales	(2,972.5)	(3,066.1)	(3,330.1)	(3,376.1)	(3,559.5)
Gross profit	1,865.5	1,997.5	1,930.3	2,158.5	2,251.9
PBT	727.7	766.5	814.1	885.5	941.4
<b>PAT</b>	<b>590.7</b>	<b>637.1</b>	<b>645.8</b>	<b>694.2</b>	<b>734.6</b>
EPS (sen)	251.9	271.7	275.4	296.1	313.2
Net Dividend (sen)	260.0	270.0	275.0	295.0	315.0
<b>Gross profit margin (%)</b>	<b>38.6</b>	<b>39.4</b>	<b>36.7</b>	<b>39.0</b>	<b>38.8</b>
PBT margin (%)	15.0	15.1	15.5	16.0	16.2
<b>PAT margin (%)</b>	<b>12.2</b>	<b>12.6</b>	<b>12.3</b>	<b>12.5</b>	<b>12.6</b>
<b>EPS Growth (%)</b>	<b>7.3</b>	<b>7.9</b>	<b>1.4</b>	<b>7.5</b>	<b>5.8</b>
<b>Dividend yield (%)</b>	<b>1.9</b>	<b>1.9</b>	<b>2.0</b>	<b>2.1</b>	<b>2.3</b>
<b>PER (x)</b>	<b>55.2</b>	<b>51.2</b>	<b>50.5</b>	<b>47.0</b>	<b>44.4</b>

Source: Company, MIDFR

## DAILY PRICE CHART



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## MIDF AMANAH INVESTMENT BANK : GUIDE TO RECOMMENDATIONS

### STOCK RECOMMENDATIONS

BUY	Total return is expected to be >10% over the next 12 months.
TRADING BUY	Stock price is expected to <i>rise</i> by >10% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -10% and +10% over the next 12 months.
SELL	Total return is expected to be <10% over the next 12 months.
TRADING SELL	Stock price is expected to <i>fall</i> by >10% within 3-months after a Trading Sell rating has been assigned due to negative newsflow.

### SECTOR RECOMMENDATIONS

POSITIVE	The sector is expected to outperform the overall market over the next 12 months.
NEUTRAL	The sector is to perform in line with the overall market over the next 12 months.
NEGATIVE	The sector is expected to underperform the overall market over the next 12 months.