

16 August 2018 | Briefing Note

## Nestlé (Malaysia) Berhad

Maintain **NEUTRAL**

*Stable earnings growth*

*Unchanged Target Price (TP): RM132.32*

### INVESTMENT HIGHLIGHTS

- **Delay in sales recognition due to warehouse relocation**
- **Positive spill-over effect to be seen in 3QFY18**
- **Reimplementation of SST in 4Q18 expected to impede the quarterly earnings growth**
- **Maintain NEUTRAL stance with an unchanged target price of RM132.32**

**Delay in sales recognition due to warehouse relocation.** To recall, Nestlé's 1HFY18 revenue grew by a modest +3.1%yoy to RM2.7b which is lower than the +4.0% to +5.0%yoy growth for the past three financial years. This was mainly due to the delay in sales completion attributable to the relocation to a new National Distribution Centre (NDC) near Westport. Based on management guidance, we estimated RM21.5m to RM23.7m worth of 2QFY18 sales was delayed and set to be completed and recognised in 3QFY18.

**Expect a strong 3QFY18, but a weaker 4QFY18 sales growth.** As a consequence of a strong consumer sentiment and pre-SST spending, we expect that sales growth to reach at least +10.0%yoy growth. For the record, 95.0% of Nestlé's product assortment was charged the standard tax rate of 6.0% under GST. Thereafter, we expect that the sales growth will be subdued due to the temporary transition in spending as a result of the reimplementation of SST. All in, we forecast a 2HFY18 to continue to growth, albeit slower pace.

**Operating profit margin will remain stable.** We gathered from management that the group has hedged its raw material requirement until the end of the financial year. Hence, we expect that the current gross profit margin of approximately 38.5% to be sustained in 2HFY18. In addition, the impact of the proposed policy by the new government to increase minimal wages on staff costs is expected to be minimal as most of Nestlé's workforce is being paid higher than the current minimum wages.


**Impact to earnings.** We are keeping our earnings estimates unchanged at this juncture.

Price (15 <sup>th</sup> August 2018)	RM146.10
Target Price	RM132.32
Expected Share Price Return	-9.4%
Expected Dividend Yield	+2.2%
<b>Expected Total Return</b>	<b>-7.2%</b>

### STOCK INFO

KLCI	1785.94
Bursa / Bloomberg	4707/ NESZ MK
Board / Sector	Main/Consumer
Syariah Compliant	Yes
Issued shares (mil)	234.5
Market cap. (RM'm)	34260.45
Price over NA	53.10x
52-wk price Range	RM84-RM163.0
Beta (against KLCI)	0.53
3-mth Avg Daily Vol	0.13m
3-mth Avg Daily Value	RM20.6m
Major Shareholders (%)	
NESTLE SA	72.61
EPF	6.84
PNB & Associated Funds	2.04

**Maintain NEUTRAL stance with an unchanged TP of RM132.32.** We expect strong sales growth in the 3QFY18 driven by the: (i) the relocation of warehouse; and (ii) strong tax-holiday spending fuelled by positive consumer sentiment. Thereafter, we anticipate sales growth to be subdued in the 4QFY18 due to the temporary transition in spending after the end of tax-holiday period. Nevertheless, over a longer term horizon, we believe that the earnings growth to remain stable as: (i) prices of its products will not be significantly different under the new SST; (ii) continuous improvement in its market share; and (iii) stabilising prices of agricultural commodities such as sugar, cocoa and coffee beans.

Valuation wise, Nestlé's forward PER is currently stretched with a forward PER of 45.5x in comparison to the average three-year PER of 28x before the inclusion to both FBM 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 an unchanged target price of **RM132.32** per share. Our target price is based on dividend discount model with 5.00% required return on equity and sustainable dividend growth rate of 2.4%. 

## 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	275.0	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>1.2</b>	<b>7.7</b>	<b>5.8</b>
<b>Dividend yield (%)</b>	<b>1.8</b>	<b>1.8</b>	<b>1.9</b>	<b>2.0</b>	<b>2.2</b>
<b>PER (x)</b>	<b>58.0</b>	<b>53.8</b>	<b>53.1</b>	<b>49.3</b>	<b>46.6</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.