



Nestlé (Malaysia) Berhad

(4707 | NESZ MK) Main | Consumer Products & Services | Food & Beverages

Maintain NEUTRAL

1QFY24 Results Preview

Unchanged Target Price: RM127.00

KEY INVESTMENT HIGHLIGHTS

- **1QFY24 earnings preview**
- **Raw material input costs have mostly stabilized, except for cocoa, Arabica, and Robusta**
- **Stronger USD further pressured raw material costs**
- **Potential price adjustments ahead to partially pass on the higher cost**
- **Maintain NEUTRAL with an unchanged TP of RM127.00**

1QFY24 Earnings Preview. Nestle's 1QFY24 results are slated for release on 29 April 2024. We anticipate the core PATAMI for 1QFY24 at RM190.9m-RM214.7m (vs. RM208.4m in 1QFY23; RM199.3m in 4QFY23), excluding unexpected fluctuations in cost structure and one-time items. This projection is grounded on an estimated revenue of RM1.78b-RM2.0b in 1QFY24 (vis-a-vis RM1.82b in 1QFY23; RM1.69b in 4QFY23), assuming both core PATAMI and revenue contribute 24%-27% to our full-year FY24 forecast. No dividend payment is expected during the quarter, as Nestle typically distributes dividends during 2Q-4Q.

We anticipate a slightly higher quarter-on-quarter revenue in 1QFY24, primarily driven by the Chinese New Year Celebration. However, we expect the revenue is expected to be lower than in 1QFY23, largely due to we believe to be a slight shift in consumer preference towards other local brand names. Furthermore, we foresee diminished core earnings on both an annual and quarterly basis, attributable to escalating certain raw material input costs (cocoa, arabica, and robusta prices), as well as increased staff costs and selling and distribution expenses.

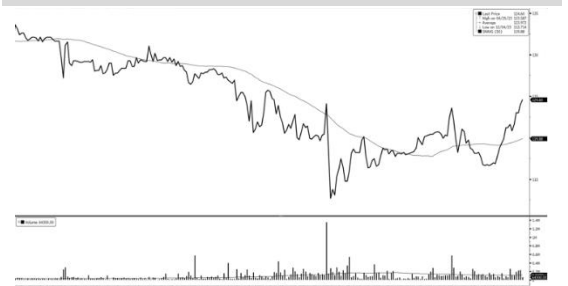
Raw material input costs have mostly stabilized, except for cocoa, Arabica, and Robusta. As of 19 April 2024, the 3-month futures of wheat, raw sugar, CPO, skimmed milk powder, and whole milk powder are trending below their 2-year peak levels. However, we have observed a continuous rising trend in cocoa (+215%yoy), Arabica (+15.2%yoy), and Robusta (+60.8%yoy) futures, mainly due to extreme weather conditions in their major exporting countries, which have lowered production yields and led to shortages. While most input ingredients are normalizing, the excessive hike in selected commodities has eroded the profit margins of certain products, particularly in the "MILO" and "Nescafe" series. Note that the raw material cost accounted for 75%-85% of total cost of sales.

Stronger USD further pressured raw material costs. With the USD strengthening against the RM to USD1.00:RM4.72 in Mar 2024, it creates potential downside risk for raw material costs. Since the group sources most of its raw materials in USD, any strengthening in the USD will cause higher raw material procurement costs. We reckon that the stronger USD could potentially partially offset the benefit of normalizing certain input costs for raw materials.

RETURN STATISTICS

Price @ 22 nd April 2024 (RM)	124.70
Expected share price return (%)	+1.8
Expected dividend yield (%)	+2.6
Expected total return (%)	4.4

SHARE PRICE CHART



Price performance (%)	Absolute	Relative
1 month	5.8	4.7
3 months	5.5	-0.1
12 months	-7.4	-15.5

INVESTMENT STATISTICS

FYE Dec (RM'm)	2024F	2025F	2026F
Revenue	7,416.8	7,890.1	8,490.7
EBITDA	968.4	1,040.2	1,132.2
Profit Before Tax	1,046.4	1,138.1	1,243.3
Core PATAMI	795.2	865.0	944.9
Core EPS (sen)	339.1	368.9	402.9
DPS (sen)	322.2	350.4	382.8
Dividend Yield (%)	2.6	2.8	3.1

KEY STATISTICS

FBM KLCI	1,559.59
Issue shares (m)	234.50
Estimated free float (%)	14.51
Market Capitalisation (RM'm)	29,242.15
52-wk price range	RM111– RM136
3-mth average daily volume (m)	0.12
3-mth average daily value (RM'm)	14.37
Top Shareholders (%)	
Nestle SA	72.61
Employees Provident Fund Board	10.82
BlackRock Inc	1.60

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Potential price adjustments ahead to partially pass on the higher cost. Nestle Malaysia is poised to make slight product prices adjustment in the coming months to partially offset increased costs linked to certain agricultural commodities (including cocoa, Arabica, and Robusta). Based on Nanyang Siang Pau report, Nestle Malaysia will increase prices for "MILO" wholesale packaged (including coffee shops, restaurants, hotels, and clubs) by 10%, effective 1 July 2024. Nanyang Siang Pau also noted that NESCAFE and MAGGI Tomato Sauce will see price increases of 7% and 5%, respectively, effective 1 July 2024.

This move aligns with earlier indications from management regarding certain product margin pressures and plans to gradually adjust prices throughout 2024, as highlighted during the 4QFY23 analyst briefing. Recall that management withheld product price hikes for MILO, NESCAFE, and MAGGI Tomato Sauce in Nov 2023 as an initiative to absorb costs and reduce the burden of rising living costs for consumers. Meanwhile, we also view these initiatives as a positive development to partially pass on the higher costs for certain products and improve the product profit margin. Given that rising cocoa, Arabica, and Robusta prices have increased the raw material costs for these products and deteriorated product margins. While a slight decline in sales volume following the implementation of price adjustments is anticipated, we remain optimistic about demand recovery, buoyed by Nestle's strong brand recognition for MILO and NESCAFE, coupled with the moderate nature of the price increases, which do not entirely pass on the added costs to consumers.

Maintain NEUTRAL with an unchanged TP of RM127.00. We make no changes to our earnings forecast for FY24-26F as we had already factored in the elevated raw material costs and the potential price adjustment in FY24. Our TP is based on DDM valuation with a consistent 3.5% growth rate and a WACC of 6.7%. Looking forward, we acknowledge the trend of Malaysian consumers becoming more cautious in their spending habits, potentially favouring alternatives offering lower prices. Simultaneously, we foresee challenges in the form of increased operating costs stemming from the introduction of higher service taxes and the potential implementation of targeted fuel subsidies, which could further escalate operational expenses. Despite these concerns, we anticipate that Nestle's strong market position is expected to maintain steady product demand. Additionally, the stabilization of key input prices (like sugar, milk, and wheat) may partially mitigate the impact of cocoa, Arabica, and Robusta cost escalations. Hence, we maintain our **NEUTRAL call** on Nestle.


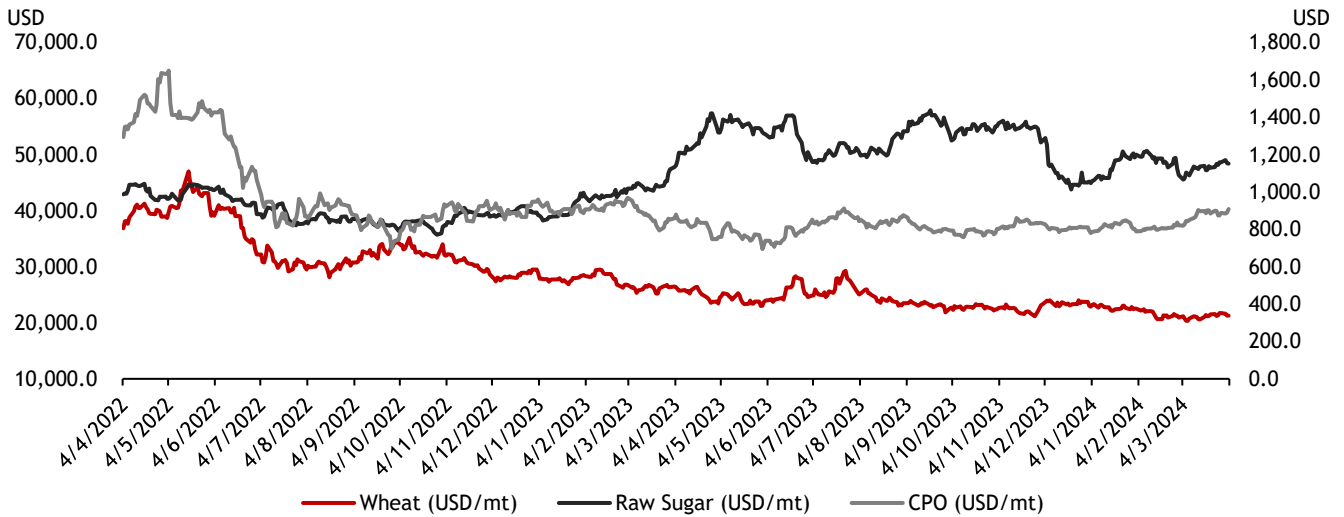
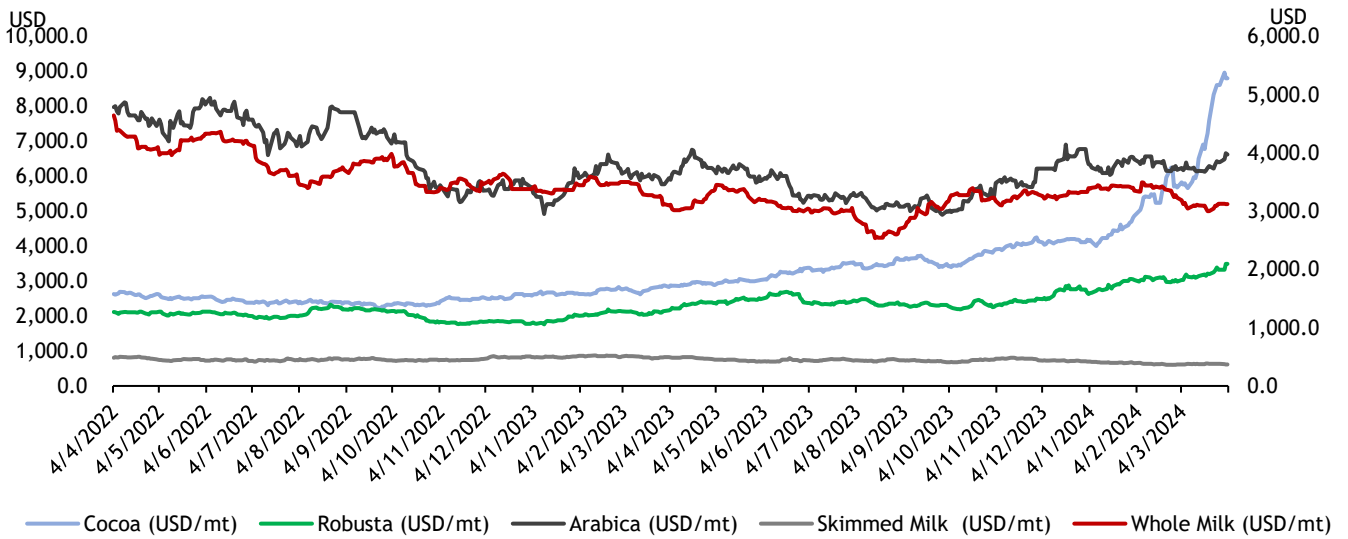
Valuation. Nestle is currently trading at an FY24F P/E ratio of 36.8x, which is below its two-year average P/E ratio of 50.5x. Additionally, it offers a 2.6% dividend yield in FY24F. **Downside risks include** (i) a sharp increase in commodity prices; (ii) higher-than-expected energy costs; (iii) unfavourable USD/MYR exchange rates; and (iv) weaker-than-expected consumer demand due to macro headwinds as well as shifts in consumer preferences. 

TABLE 1: Wheat, Raw Sugar, CPO Futures Price Trend (USD/MT)



Source: MIDFR, Bloomberg

TABLE 2: Cocoa, Arabica, Robusta, Skimmed Milk Powder, Whole Milk Powder Futures Price Trend (USD/MT)



Source: MIDFR, Bloomberg

FINANCIAL SUMMARY

Income Statement (RM'm)	2022A	2023E	2024F	2025F	2026F
Revenue	6,664.1	7,050.9	7,416.8	7,890.1	8,490.7
Cost of Sales	(4,603.3)	(4,819.9)	(4,917.9)	(5,179.4)	(5,518.0)
Gross Profit	2,060.9	2,231.0	2,498.9	2,710.7	2,972.8
Other Income	0.0	0.0	0.0	5.1	0.0
Selling and Distribution expenses	(936.0)	(1,005.2)	(1,083.8)	(1,181.8)	(1,303.5)
General & Administrative	(194.0)	(225.8)	(243.5)	(265.5)	(292.8)
Other operating expenses	(27.9)	(60.7)	(62.9)	(65.9)	(70.2)
EBITDA	1,110.4	1,148.0	968.4	1,040.2	1,132.2
EBIT	902.9	939.3	1,108.8	1,202.6	1,306.2
Profit before tax (PBT)	859.5	879.1	1,046.4	1,138.1	1,243.3
Income tax expense	(239.1)	(219.2)	(251.1)	(273.2)	(298.4)
PATAMI	620.3	659.9	796.2	865.0	944.9
Core PATAMI	632.3	772.8	795.2	865.0	944.9
Core EPS (sen)	269.6	329.5	339.1	368.9	402.9
DPS (sen)	262.0	268.0	322.2	350.4	382.8

Balance Sheet (RM'm)	2022A	2023E	2024F	2025F	2026F
Property, plant and equipment	1,669.3	1,749.5	1,866.2	1,989.3	2,122.8
Intangible assets	62.2	234.4	244.1	257.0	273.8
Total non-current assets	1,954.8	2,263.2	2,394.1	2,535.2	2,691.5
Inventories	1,115.1	831.4	945.7	993.3	1,058.2
ST - Trade and other receivables	445.2	463.0	407.5	432.3	465.2
Cash and cash equivalents	8.2	11.0	11.7	12.5	13.5
Total current assets	1,599.2	1,306.0	1,365.5	1,438.7	1,537.6
Total Assets	3,554.0	3,569.2	3,759.6	3,974.0	4,229.1
Total Equity	626.3	674.9	722.9	812.2	902.3
LT Lease Liabilities	120.0	170.2	185.4	197.3	212.3
LT Loans and borrowings	300.0	300.0	301.5	303.0	304.5
Total non-current liabilities	668.7	756.4	799.7	830.4	868.2
ST Trade and other payables	1,724.9	1,671.6	1,756.4	1,844.7	1,965.3
ST Loans and borrowings	486.9	419.8	421.9	424.0	426.1
Total Current Liabilities	2,259.0	2,137.9	2,237.0	2,331.3	2,458.6
Total Liabilities	2,927.7	2,894.3	3,036.7	3,161.7	3,326.8

Cash Flow (RM'm)	2022A	2023E	2024F	2025F	2026F
Pretax profit	859.5	879.1	1,138.1	1,243.3	1,378.2
Cash flow from operations	511.5	1,267.8	1,231.2	1,304.1	1,438.9
Cash flow from investing	(309.7)	(501.5)	(303.9)	(327.0)	(357.7)
Cash flow from financing	(376.8)	(604.7)	(897.7)	(976.1)	(1,079.9)
Net cash flow	(174.9)	161.6	29.6	1.0	1.3
Net cash/(debt) b/f	(3.8)	(178.7)	(17.1)	12.5	13.5
Net cash/(debt) c/f	(178.7)	(17.1)	12.5	13.5	14.8

Key Metrics	2022A	2023E	2024F	2025F	2026F
Effective tax rate (%)	27.8	24.9	24.0	24.0	24.0
Dividend Yield (%)	2.1	2.1	2.6	2.8	3.1
PER (x)	47.1	44.3	36.8	33.8	30.9
Inventories (Days)	73.7	73.9	70.0	70.0	70.0
Net debt/total equity (x)	1.2	1.1	1.0	0.9	0.8

Profitability Margins	2022A	2023E	2024F	2025F	2026F
Gross Profit Margin (%)	30.9	31.6	33.7	34.4	35.0
EBITDA Margin (%)	16.7	16.3	13.1	13.2	13.3
Core PATAMI Margin (%)	9.5	11.0	10.7	11.0	11.1

Source: Bloomberg, MIDFR

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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.

ESG RECOMMENDATIONS* - source Bursa Malaysia and FTSE Russell

☆☆☆☆	Top 25% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆☆☆	Top 26-50% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆☆	Top 51%- 75% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆	Bottom 25% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell

* ESG Ratings of PLCs in FBM EMAS that have been assessed by FTSE Russell in accordance with FTSE Russell ESG Ratings Methodology