

August 2, 2022



Earnings Note

Event

Cost pressures subdued Nestle Nigeria Plc's (the Company) Q2 2022 financial performance. Although revenue grew significantly by 33% YoY to N112.23bn, the sharper increase in operating costs moderated the revenue gains. For context, cost margin expanded by 500 basis points to 67% (Q2 2021: 62%), on the back higher raw materials costs and FX illiquidity. Therefore, gross margin declined to 33% in Q2 2022 from 38% in Q1 2021, despite a 17% YoY absolute growth.

To the management's credit, operating expenses were optimised to protect margins. Operating expense grew by 10% YoY, behind inflation rate. Accordingly, operating expense margin declined 400 basis points to 15% (Q2 2021: 19%).

The cost optimisation effort supported bottomline growth as profit before tax grew by 11% YoY to N15.99bn. Owing to higher effective tax rate (39% in Q2 2022 vs 35% in Q2 2021), net profit grew by just 5% YoY to N9.77bn.

Nestle (N'mn)	Q2 2022	Q2 2021	Q1 2022	Q1 2021
Revenue	112,225	84,182	110,225	87,258
Revenue growth	33%		29%	
Gross profit	36,963	31,692	43,243	34,743
Gross margin	33%	38%	39%	40%
Operating profit	19,779	16,016	26,403	20,314
Operating margin	18%	19%	24%	23%
Net profit	9,771	9,333	17,980	12,400
Net margin	9%	11%	16%	14%
Earnings per share	N12.33	N11.77	N22.68	N15.64

Source: Company Accounts, WSTC Research

Outlook

The company's Q2 2022 performance came slightly below our expectations due to a higher-than-projected production cost. In our view, we opine that the Company is careful about immediately passing on the cost burden to consumers due to the challenging macroeconomic environment in the form of declining purchasing power and increased competition. However, we believe that a persistent increase in cost would inevitably result in a broad-based increase in prices across the industry.

We retain our BUY rating for Nestle. We note that the stock has declined by 19% on a year-to-date basis. However, at the current price, the stock trades at 18.98x to our revised forward earnings per share of N66.49. Based on a blend of the discounted cash flow (DCF), discounted dividend (DDM), enterprise valuation (EV/EBITDA), and residual income (RIM) methodologies, our estimated justified P/E is 24.49x. This implies a fair value of N1,628.24.

Hence, we project a 29% potential price return on the stock. In combination with a projected 5% dividend yield, we estimate a total return on the stock is 34%.

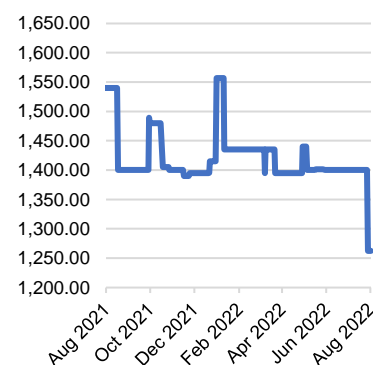
BUY

Fair Value Estimate:
N1,562.02

Price Return: **+29%**

Stock Data

Current price (N)	1,262.30
Shares Outstanding (mn)	793
Market Cap (N'mn)	1,000,570
52-week high (N)	1,556.50
52-week low (N)	1,262.30
Trailing EPS (N)	50.51
Forward EPS (N)	66.49
Forward PE (X)	18.98
Justified PE Multiple (X)	24.49



Stock Data	FY 2020	FY 2021	FY 2022F
P/E	25.52x	24.99x	18.98x
P/BV	34.15x	46.80x	29.38x
PBT Margin	21%	18%	18%
PAT Margin	14%	11%	12%
RoE	105%	158%	190%
Dividend Yield	5%	4%	5%

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H1 2022 Financial performance trend

Income Statement (N'mn)	H1 2022	H1 2021	%
Revenue	222,451	171,440	33%
Cost of Sales	(142,245)	(105,005)	35%
Gross Profit	80,206	66,435	21%
Selling and distribution expenses	(28,353)	(23,492)	21%
Administrative expense	(5,671)	(6,612)	-14%
Operating expenses	(34,024)	(30,105)	13%
Operating profit	46,181	36,330	27%
Finance income	4,521	445	917%
Finance cost	(6,963)	(3,395)	105%
Profit before tax	43,470	33,380	31%
Tax	(15,989)	(11,647)	37%
Profit after tax	27,751	21,733	28%
Balance Sheet (N'mn)	H1 2022	H1 2021	%
Assets			
PPE	101,766	85,894	18%
Inventory	72,679	49,984	45%
Receivables	73,227	28,471	157%
Prepayments & other assets	3,592	2,770	30%
Cash	88,184	88,335	0%
Others	7,281	7,338	-1%
Total Assets	346,729	262,793	32%
Liabilities			
Borrowings	92,934	52,485	77%
Trade payables	170,867	137,777	24%
Others	54,079	49,691	9%
Total Liabilities	317,880	239,954	32%
Net Assets	28,849	22,839	26%

Source: Company Accounts, WSTC Research

Financial Projections

Income statement (NGN mn)	FY 2020	FY 2021	FY 2022F	FY 2023F	FY 2024F	FY 2025F	FY 2026F
Revenue	287,084	351,822	449,413	485,366	524,195	602,825	663,107
EBITDA	72,170	80,375	100,731	128,863	142,894	168,307	168,307
EBIT	64,419	71,966	88,793	115,970	128,970	152,294	152,294
Profit before taxation	60,638	61,875	81,452	107,920	119,661	140,044	140,044
Net profit	39,212	40,037	52,704	69,831	77,428	90,618	90,618
EPS (₦)	49.47	50.51	66.49	88.10	97.68	114.32	114.32
DPS (₦)	60.50	50.50	66.49	88.10	97.68	114.32	114.32
Balance sheet (NGN mn)	FY 2020	FY 2021	FY 2022F	FY 2023F	FY 2024F	FY 2025F	FY 2026F
Cash	58,703	100,518	90,774	91,879	85,062	96,897	105,295
Other current assets	92,798	103,406	144,950	150,788	161,781	184,901	198,900
Non-current assets	94,684	106,314	118,919	132,532	147,234	164,141	182,739
Total assets	246,185	310,239	354,643	375,199	394,077	445,939	486,934
Current liabilities	166,030	195,518	216,703	219,484	230,888	256,436	268,434
Non-current liabilities	50,858	93,342	103,887	104,535	104,411	117,537	127,599
Total liabilities	216,888	288,860	320,589	324,019	335,299	373,972	396,033
Shareholders' equity	29,297	21,378	34,053	51,180	58,777	71,967	90,901
Cash flow statement (NGN mn)	FY 2020	FY 2021	FY 2022F	FY 2023F	FY 2024F	FY 2025F	FY 2026F
Cash from operating activities	97,196	64,436	48,762	86,885	101,050	120,509	138,633
Cash from investing activities	(15,719)	(18,106)	(15,797)	(17,516)	(20,060)	(26,290)	(28,908)
Cash from financing activities	(27,019)	(4,515)	(42,709)	(68,263)	(87,807)	(82,384)	(101,328)
Net increase/ (decrease) in cash	54,459	41,815	(9,744)	1,105	(6,817)	11,835	8,398
Ratio analysis	FY 2020	FY 2021	FY 2022F	FY 2023F	FY 2024F	FY 2025F	FY 2026F
EBITDA margin	25%	23%	22%	27%	27%	28%	30%
Operating margin	22%	20%	20%	24%	25%	25%	28%
ROE	105%	158%	190%	164%	141%	139%	135%
ROA	18%	14%	16%	19%	20%	22%	23%
Dividend payout ratio	122%	100%	100%	100%	100%	100%	100%

Source: Company Accounts, WSTC Research

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Investment Recommendation

WSTC uses a 3-tier recommendation system for stocks under coverage: Buy, Hold, and Sell.

- Buy Rating: estimated fair value is $\geq 15\%$ above current market price.
- Hold Rating: estimated change in price is between -10% and 15% of current market price.
- Sell Rating: estimated change in price is $\leq -10\%$ of current market price.

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