

November 14, 2022



Earnings Note

Event

Nestle Nigeria Plc recently released its Q3 2022 financial performance with revenue increasing by 23% to N111.02bn, although slower than previous quarters (Q2 2022: +33%, Q1 2022: +26%). The growth in Q3 2022 was driven by a 27% year-on-year growth in its Food segment, and a 17% year-on-year revenue growth in its Beverage segment respectively. We believe price increases across the Company's product drove the growth in these segments.

Despite price increases, gross margin lowered by 600 basis points to 33%. For context, cost of sales rose by 34% year-on-year to N73.94bn in Q3 2022 from N55.29bn in Q3 2021. We believe that the ongoing global supply chain disruptions and global inflationary pressures negatively impacted raw materials costs. The inability to fully pass on the costs to the consumers resulted in the gross margin decline.

In addition to the higher raw material costs, the Company's operating expenses increased by 22% year-on-year, resulting from higher marketing and distribution expenses. In our view, the increased marketing spend was due to the need to invest behind brands amid competitive pressures. Also, higher energy costs (i.e., diesel) impacted the cost of distribution for the Company. Due to the double-faced pressures that came from cost of sales and operating expense, operating profit declined by 6% YoY to N18.70bn.

However, the bottomline recorded a growth, as profit after tax stood at N12.41bn – a 5% year-on-year growth. This was driven by a lower effective tax rate (15% in Q3 2022 versus 35% in Q3 2021). In line with its dividend policy, the Company declared 25 kobo as interim dividend. The qualification date for the interim dividend is November 18, 2022; while the payment date is slated for December 5, 2022.

Quarterly Trend

N'mn	Q3 2022	Q3 2021	Q2 2022	Q2 2021	Q1 2022	Q1 2021
Revenue	111,021	90,151	112,225	84,182	110,225	87,258
Revenue Growth	23%		33%		29%	
Gross profit	37,080	34,857	36,963	31,692	43,243	34,743
Gross margin	33%	39%	33%	38%	39%	40%
Operating profit	18,696	19,793	19,779	16,016	26,403	20,314
Operating margin	17%	22%	18%	19%	24%	23%
Net profit	12,401	11,853	9,771	9,333	17,980	12,400
Net margin	11%	13%	9%	11%	16%	14%
Earnings Per Share	N15.65	N14.95	N12.33	N11.77	N22.68	N15.64

Source: Company Accounts, WSTC Research

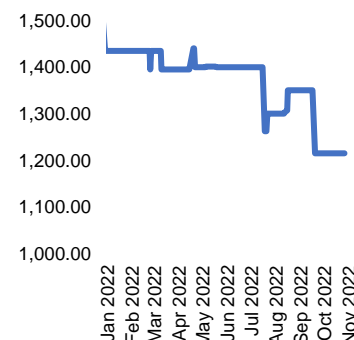
BUY

Fair Value Estimate:
N1,568.87

Total Return: **+34%**

Stock Data

Current price (N)	1,215.00
Shares Outstanding (mn)	793
Market Cap (N'mn)	963,077
52-week high (N)	1,556.50
52-week low (N)	1,215.00
Trailing EPS (N)	50.51
Forward EPS (N)	57.30
Forward PE (X)	21.20
Justified PE Multiple (X)	27.38



Stock Data	FY 2020	FY 2021	FY 2022F
P/E	24.56x	24.05x	21.21x
P/BV	32.87x	45.05x	35.98x
PBT Margin	21%	18%	16%
PAT Margin	14%	11%	10%
RoE	105%	158%	189%
Dividend Yield	5%	4%	5%

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9M 2022 Financial Performance

Income Statement (N'mn)	9M 2022	9M 2021	Growth (%)
Revenue	333,472	261,591	27%
Cost of sales	(216,187)	(160,300)	35%
Gross profit	117,285	101,291	16%
Marketing expense	(43,380)	(35,616)	22%
Admin expense	(9,028)	(9,554)	-6%
Operating expense	(52,408)	(45,169)	16%
Operating profit	64,877	56,122	16%
Finance income	2,579	1,198	115%
Finance cost	(9,070)	(5,735)	58%
Profit before tax	58,386	51,584	13%
Income tax	(18,233)	(18,000)	1%
Profit after tax	40,152	33,584	20%
Balance Sheet (N'mn)	9M 2022	9M 2021	Growth (%)
Assets			
PPE	105,475	89,371	18%
Inventory	77,584	55,389	40%
Receivables	73,676	35,570	107%
Prepayments	4,059	1,462	178%
Cash	107,136	116,607	-8%
Others	7,506	7,235	4%
Total Assets	375,435	305,635	23%
Liabilities			
Borrowings	105,458	71,722	47%
Payables	170,076	140,425	21%
Others	58,629	58,768	0%
Total Liabilities	334,163	270,915	23%
Net Assets	41,272	34,720	19%

Source: Company Accounts, WSTC Research

Outlook

In the near term, we expect profit margins to remain under pressure due to high operating costs. The global supply chain disruptions are likely to persist into Q4 2022 and in the near term. Also, higher energy prices and domestic inflationary pressures are two downsides that are expected to hurt margins in the near term. We expect the domestic inflationary pressures to negatively affect the company in two forms – (i) erosion of purchasing power which weakens consumer disposable income (ii) high business running costs.

In view of our expectations, we revised our forecasts to reflect the current realities of a more challenging macroeconomic environment. Therefore, we reviewed our earnings per share forecast for FY 2022 downwards to N57.30 (previous: N66.49).

By implication, our fair value for the stock is lower by 4% to N1,568.24. However, we recommend a BUY for the stock. Due to a general market selloff, the stock declined to a 52-week low of N1,215.00. Based on the fundamentals of the company (market leadership, essential products, pricing power to an extent, relatively strong management, and strong cash flows), we believe that the stock is undervalued.

Financial Projections

Income statement (NGN mn)	FY 2021	FY 2022F	FY 2023F	FY 2024F	FY 2025F	FY 2026F	FY 2027F	FY 2028F
Revenue	351,822	449,322	485,267	524,089	602,702	662,972	729,269	765,733
EBITDA	80,375	93,124	112,278	135,201	159,459	159,459	191,051	210,156
EBIT	71,966	81,189	99,388	121,279	143,449	143,449	173,440	190,784
Profit before taxation	61,875	70,190	91,483	112,947	132,430	132,430	160,433	176,351
Net profit	40,037	45,417	59,195	73,084	85,691	85,691	103,811	114,110
EPS (N)	50.51	57.30	74.68	92.20	108.11	108.11	130.97	143.96
DPS (N)	50.50	57.30	74.68	92.20	108.11	108.11	130.97	143.96
Balance sheet (NGN mn)	FY 2021	FY 2022F	FY 2023F	FY 2024F	FY 2025F	FY 2026F	FY 2027F	FY 2028F
Cash	100,518	91,843	86,512	91,284	107,624	120,927	130,675	129,283
Other current assets	103,406	157,232	166,316	175,611	200,803	216,382	238,015	249,914
Non-current assets	106,314	114,598	123,545	133,207	144,319	156,541	169,986	184,104
Total assets	310,239	363,673	376,372	400,102	452,745	493,850	538,677	563,300
Current liabilities	195,518	224,052	231,311	237,781	264,171	276,694	299,712	312,352
Non-current liabilities	93,342	112,855	104,517	107,887	121,534	131,997	143,505	149,835
Total liabilities	288,860	336,907	335,828	345,669	385,705	408,690	443,217	462,188
Shareholders' equity	21,378	26,766	40,544	54,433	67,040	85,160	95,459	101,113
Cash flow statement (NGN mn)	FY 2021	FY 2022F	FY 2023F	FY 2024F	FY 2025F	FY 2026F	FY 2027F	FY 2028F
Cash from operating activities	64,436	39,524	77,643	92,265	113,143	130,856	148,678	155,759
Cash from investing activities	(18,106)	(17,187)	(12,849)	(15,019)	(20,492)	(22,531)	(24,925)	(25,916)
Cash from financing activities	(4,515)	(31,012)	(70,125)	(72,474)	(76,311)	(95,022)	(114,004)	(131,236)
Net increase/ (decrease) in cash	41,815	(8,675)	(5,331)	4,772	16,340	13,303	9,748	(1,393)
Ratio analysis	FY 2021	FY 2022F	FY 2023F	FY 2024F	FY 2025F	FY 2026F	FY 2027F	FY 2028F
EBITDA margin	23%	21%	23%	26%	26%	29%	29%	29%
Operating margin	20%	18%	20%	23%	24%	26%	26%	26%
ROE	158%	189%	176%	154%	141%	136%	126%	122%
ROA	14%	13%	16%	19%	20%	22%	22%	22%
Dividend payout ratio	100%	100%	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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