

Focusing on its strengths

We attended Nestlé's recent results briefing, which yielded no major surprises. However, we got some clarity on management's future plans for the business, especially regarding the consolidation of the MILO operations at the Chembong factory in Negeri Sembilan. Management is of the view that consumer sentiment should continue to hold up and new product innovations should continue to spur topline growth, but cautioned on a possible uptick in certain key raw material prices. We retain our SELL call on valuation grounds.

9M18 earnings were solid, driven by strong demand

To recap, 9M18 earnings came in within expectations, primarily driven by strong demand for new product launches and margin improvements on lower raw material prices and realised efficiencies. We understand that new products such as the MAGGI *Pedas Giler* variety saw an overwhelming response from customers, which was also confirmed by our channel checks with certain retailers. The much improved consumer sentiment also provided steady tailwinds, and we concur with management that sentiment should continue to hold up into FY19.

Some updates on the disposal of the chilled dairy business

We also got further clarity on the proposed disposal of Nestlé's chilled dairy business to Lactalis. The rationale for the disposal was two-fold: i) Strategically, Lactalis is better positioned to develop and grow the chilled dairy business in Malaysia, considering its strong portfolio of dairy business globally, and ii) A bulk of the sales proceeds of RM155m allows Nestlé to rationalise the MILO business in an existing factory in Chembong, Negeri Sembilan, which entails the expansion of manufacturing capacity and efficiency gains, to cater to growing demand.

Outlook still looks bright, but foresee an uptick in raw material prices

We believe that the outlook remains strong for Nestlé considering its strong branding in Malaysia and positive consumer sentiment, which translate into a good take-up of its new product offerings. On the flip side, moving forward, management believes that prices of some key raw materials, such as milk powder and certain grains, might increase in the near term, due to the normalisation of supply/demand dynamics globally. However, we believe that this can be mitigated by adequate hedging strategies and efficiency gains in Nestlé's operations.

Maintain SELL on lofty valuations, no significant rerating catalysts

As the briefing did not yield any major surprises, we make no changes to our estimates. We believe the bright prospects have been more than adequately priced in, and thus retain our SELL call with an unchanged DCF-derived TP of RM111.00. Upside risks: less competitive environment in the F&B space; sharp decline in raw material prices.

Earnings & Valuation Summary

FYE 31 Dec	2016	2017	2018E	2019E	2020E
Revenue (RMm)	5063.5	5260.5	5696.9	5909.3	6213.0
EBITDA (RMm)	900.5	974.0	1132.5	1156.8	1232.2
Pretax profit (RMm)	766.5	814.1	953.3	979.2	1050.2
Net profit (RMm)	637.1	645.8	762.7	783.4	840.2
EPS (sen)	271.7	275.4	325.2	334.1	358.3
PER (x)	52.8	52.1	44.1	43	40.1
Core net profit (RMm)	605.6	640.6	762.7	783.4	840.2
Core EPS (sen)	258.3	273.2	325.2	334.1	358.3
Core EPS growth (%)	7.9	1.4	18.1	2.7	7.3
Core PER (x)	55.6	52.5	44.1	43.0	40.1
Net DPS (sen)	270.0	275.0	319.0	328.0	352.0
Dividend Yield (%)	1.9	1.9	2.2	2.3	2.5
EV/EBITDA (x)	37.7	34.9	30.0	29.3	27.5
Chg in EPS (%)			-	-	-
Affin/Consensus (x)			1.06	1.02	1.02

Source: Company, Affin Hwang estimates

Affin Hwang Investment Bank Bhd (14389-U)

Outthink. Outperform.

Company Update

Nestlé (Malaysia)

NESZ MK

Sector: Consumer

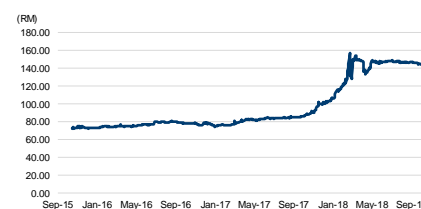
RM143.50 @ 1 November 2018

SELL (maintain)

Downside: 23%

Price Target: RM111.00

Previous Target: RM111.00



Price Performance

	1M	3M	12M
Absolute	-2.0%	-2.6%	63.1%
Rel to KLCI	2.9%	2.1%	66.6%

Stock Data

Issued shares (m)	234.5
Mkt cap (RMm)/(US\$m)	34,650.8/8,052.3
Avg daily vol - 6mth (m)	0.1
52-wk range (RM)	87.04-163
Est free float	15.2%
BV per share (RM)	3.02
P/BV (x)	47.48
Net cash/ (debt) (RMm)	(420.45)
ROE (2018E)	100%
Derivatives	Nil
Shariah Compliant	Yes

Key Shareholders

NESTLE SA	72.6%
EPF	7.6%
SKIM AMANAH SAHAM	2.0%

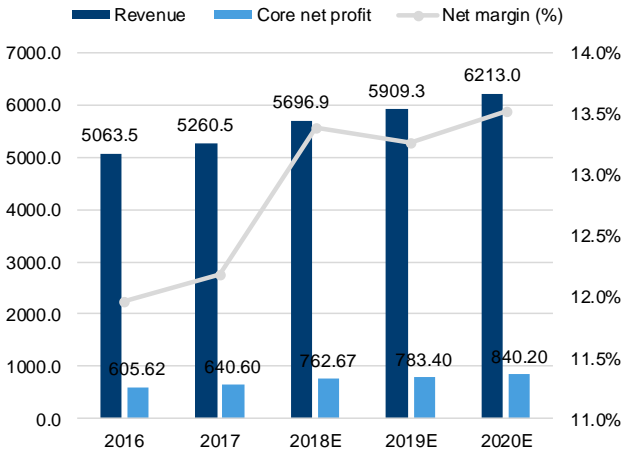
Source: Affin Hwang, Bloomberg

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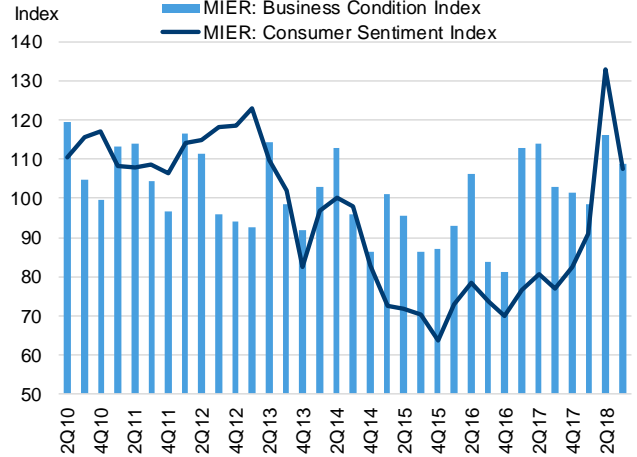
Nestle Focus Charts

Figure 1: Expecting margin improvements in FY18



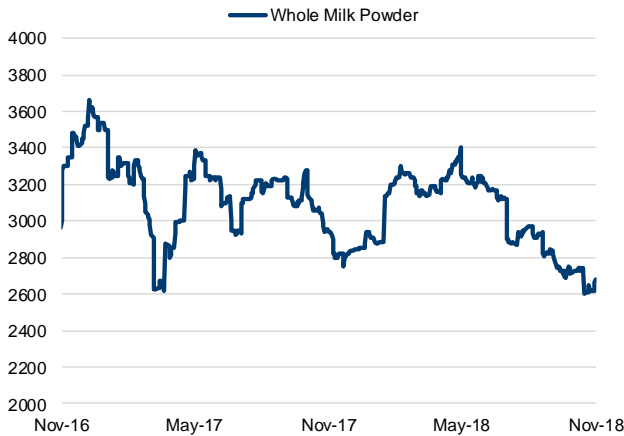
Source: Company, Affin Hwang Forecasts

Figure 2: Consumer sentiments still holding up above 100 pts



Source: MIER

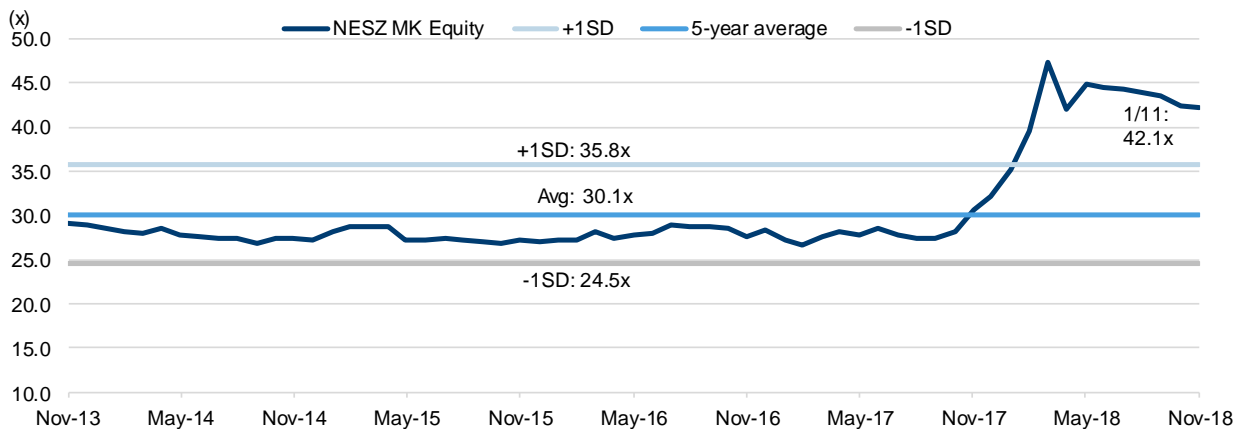
Figure 3: Key raw material prices



Source: Bloomberg



Figure 4: Nestle (Malaysia) PER Chart



Source: Company, Affin Hwang Forecasts

NESTLE - FINANCIAL SUMMARY

Profit & Loss Statement

FYE Dec (RMm)	2016	2017	2018E	2019E	2020E
Total revenue	5,063.5	5,260.5	5,696.9	5,909.3	6,213.0
Operating expenses	(4,163.0)	(4,286.5)	(4,564.4)	(4,752.5)	(4,980.9)
EBITDA	900.5	974.0	1,132.5	1,156.8	1,232.2
Depreciation	(132.8)	(130.9)	(138.3)	(146.0)	(154.2)
Amortisation	(0.4)	(0.4)	0.0	0.0	0.0
EBIT	767.3	842.7	994.2	1,010.8	1,078.0
Net interest income/(expense)	(32.7)	(34.6)	(42.4)	(34.4)	(32.6)
Associates' contribution	0.4	0.8	1.5	2.9	4.8
Others	31.5	5.2	0.0	0.0	0.0
Pretax profit	766.5	814.1	953.3	979.2	1,050.2
Tax	(129.4)	(168.3)	(190.7)	(195.8)	(210.0)
Minority interest	0.0	0.0	0.0	0.0	0.0
Net profit	637.1	645.8	762.7	783.4	840.2

Balance Sheet Statement

FYE Dec (RMm)	2016	2017	2018E	2019E	2020E
Fixed assets	1353.1	1373.7	1413.5	1452.2	1492.3
Other long term assets	111.5	110.2	110.2	110.2	110.2
Total non-current assets	1464.6	1483.9	1523.8	1562.5	1602.5
Cash and equivalents	24.0	12.6	81.2	41.9	78.7
Stocks	455.3	467.3	489.2	513.2	535.3
Debtors	544.3	580.8	629.0	652.5	686.0
Other current assets	6.4	12.3	12.3	12.3	12.3
Total current assets	1030.0	1073.1	1211.7	1219.9	1312.4
Creditors	1392.8	1296.6	1357.3	1423.8	1485.3
Short term borrowings	184.0	305.6	305.6	250.6	250.6
Other current liabilities	0.1	19.8	19.8	19.8	19.8
Total current liabilities	1576.8	1622.1	1682.7	1694.3	1755.7
Long term borrowings	93.1	84.3	84.3	84.3	84.3
Other long term liabilities	177.4	210.7	210.7	210.7	210.7
Total long term liabilities	270.5	295.0	295.0	295.0	295.0
Shareholders' Funds	647.2	639.9	757.8	793.1	864.2

Cash Flow Statement

FYE Dec (RMm)	2016	2017	2018E	2019E	2020E
PBT	766.5	814.1	953.3	979.2	1050.2
Depreciation & amortisation	133.2	131.3	138.3	146.0	154.2
Working capital changes	121.5	(175.4)	(9.4)	19.1	5.8
Cash tax paid	(145.0)	(117.6)	(190.7)	(195.8)	(210.0)
Others	46.7	53.3	42.4	34.4	32.6
Cashflow from operation:	922.8	705.7	933.9	983.0	1032.7
Capex	(123.1)	(164.5)	(178.1)	(184.7)	(194.2)
Disposal/(purchases)	2.7	0.0	0.0	0.0	0.0
Others	4.1	3.7	1.6	1.7	1.9
Cash flow from investing	(119.0)	(160.7)	(176.5)	(183.0)	(192.3)
Debt raised/(repaid)	(204.3)	262.6	0.0	(55.0)	0.0
Equity raised/(repaid)	0.0	0.0	0.0	0.0	0.0
Net interest income/(expense)	(33.8)	(36.0)	(44.0)	(36.2)	(34.5)
Dividends paid	(633.2)	(633.2)	(644.9)	(748.1)	(769.2)
Others	(3.8)	0.0	0.0	0.0	0.0
Cash flow from financing	(875.1)	(406.5)	(688.8)	(839.2)	(803.6)
Free Cash Flow	799.7	541.2	755.8	798.2	838.5

Source: Company, Affin Hwang Estimates

Key Financial Ratios and Margins

FYE Dec (RMm)	2016	2017	2018E	2019E	2020E
Growth					
Revenue (%)	4.7	3.9	8.3	3.7	5.1
EBITDA (%)	1.0	8.2	16.3	2.1	6.5
Core net profit (%)	7.9	1.4	18.1	2.7	7.3
Profitability					
EBITDA margin (%)	17.8	18.5	19.9	19.6	19.8
PBT margin (%)	15.1	15.5	16.7	16.6	16.9
Net profit margin (%)	12.6	12.3	13.4	13.3	13.5
Effective tax rate (%)	16.9	20.7	20.0	20.0	20.0
ROA (%)	25.5	25.3	27.9	28.2	28.8
Core ROE (%)	89.3	99.5	109.1	101.0	101.4
ROCE (%)	77.4	86.2	91.3	88.8	92.6
Dividend payout ratio (%)	99	100	98	98	98
Liquidity					
Current ratio (x)	0.7	0.7	0.7	0.7	0.7
Op. cash flow (RMm)	922.8	705.7	933.9	983.0	1,032.7
Free cashflow (RMm)	799.7	541.2	755.8	798.2	838.5
FCF/share (sen)	3.4	2.3	3.2	3.4	3.6
Asset management					
Debtors turnover (days)	39	40	40	40	40
Stock turnover (days)	54	51	51	51	51
Creditors turnover (days)	166	142	142	142	142
Capital structure					
Core ROA (%)	24.3	25.1	27.9	28.2	28.8
ROCE (%)	77.4	86.2	91.3	88.8	92.6

Quarterly Profit & Loss

FYE 31 Dec (RMm)	3Q17	4Q17	1Q18	2Q18	3Q18
Revenue	1,323.3	1,281.7	1,429.7	1,309.1	1,432.5
Operating expenses	(1,169.9)	(1,106.8)	(1,126.2)	(1,085.5)	(1,234.8)
EBIT	153.3	175.0	303.4	223.6	197.7
Net int income/(expense)	(9.3)	(9.1)	(9.2)	(9.6)	(11.1)
Associates' contribution	0.3	(0.1)	0.6	0.5	0.2
Exceptional items	0.0	0.0	0.0	0.0	0.0
Pretax profit	144.3	165.8	294.8	214.4	186.7
Tax	(25.3)	(32.2)	(63.6)	(48.2)	(49.0)
Minority interest	0.0	0.0	0.0	0.0	0.0
Net profit	119.0	133.5	231.2	166.2	137.7
Core net profit	119.0	133.5	231.2	166.2	137.7
Margins (%)					
EBIT	11.6	13.6	21.2	17.1	13.8
PBT	10.9	12.9	20.6	16.4	13.0
Net profit	9.0	10.4	16.2	12.7	9.6

Equity Rating Structure and Definitions

BUY	Total return is expected to exceed +10% over a 12-month period
HOLD	Total return is expected to be between -5% and +10% over a 12-month period
SELL	Total return is expected to be below -5% over a 12-month period
NOT RATED	Affin Hwang Investment Bank Berhad does not provide research coverage or rating for this company. Report is intended as information only and not as a recommendation

The total expected return is defined as the percentage upside/downside to our target price plus the net dividend yield over the next 12 months.

OVERWEIGHT	Industry, as defined by the analyst's coverage universe, is expected to outperform the KLCI benchmark over the next 12 months
NEUTRAL	Industry, as defined by the analyst's coverage universe, is expected to perform inline with the KLCI benchmark over the next 12 months
UNDERWEIGHT	Industry, as defined by the analyst's coverage universe is expected to under-perform the KLCI benchmark over the next 12 months

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