

Nestlé (Malaysia) Berhad

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

Maintain NEUTRAL

Margins may be affected to combat Covid-19

Revised Target Price: RM143.90

(Previously RM148.00)

KEY INVESTMENT HIGHLIGHTS

- **1QFY20 earnings missed the mark slightly**
- **Profit for the quarter dropped by 20.8%yoy to RM186.3m due to higher commodity prices as well as higher operating costs incurred during the MCO**
- **We tweak our FY20E/ FY21F earnings by -5.4% and -3.5% to reflect possibly higher operating costs that may become the new norm**
- **Maintain NEUTRAL stance with a revised TP of RM143.90 (previously RM148.00)**

1QFY20 earnings missed the mark slightly. Nestlé's 1QFY20 normalised earnings of RM186.3m were slightly below ours and consensus expectations at 26%. Usually 1Q make up 30% or more of Nestlé's full year earnings historically. No dividend was announced this quarter, which is within expectation.

Profit for the quarter dropped by 20.8%yoy to RM186.3m due to higher commodity prices as well as higher operating costs incurred during the Movement Control Order (MCO). In respond to keeping the workplace safe, the company has purchased personal protective equipment (PPE) and implemented additional safety protocol at sites to protect its employees. It has also granted special allowances to its frontline workers, which also led to the higher expenses incurred during the quarter. These measures have led to compression in operating profit margin by -4.4ppt compared to 1QFY19.

Revenue for the quarter held up well at RM1.43b, marginally down from in the previous year. This was despite the MCO, which has adversely impacted its Out of Home Business as restaurants, coffee shops and eateries close their premises and only allow for takeaway. Sales was however cushioned by the core Food and Beverages business, which remained stable. Supporting the sales were its strong sales execution and effective marketing campaigns that include the Nestlé's Salary for Life Contest. During the period, domestic sales contracted by -3.4% while export sales increased by +8.8%.

We tweak our FY20E/ FY21F earnings by -5.4% and -3.5% to reflect possibly higher operating costs that may become the new norm. We believe that Nestlé will continue to uphold high standards in its production as well as its employees' safety. In view of that, we believe that operating expenses that include PPE and sanitisation routine will continue to be part of its operating expenses in the coming quarters. We also opine that the extended MCO in Malaysia may continue to dampen its Out of Home Business in 2Q although that may be partially cushioned by the upcoming Raya festive season.

RETURN STATISTICS

Price @ 5 th May 2020 (RM)	139.60
Expected share price return (%)	+3.1
Expected dividend yield (%)	+2.0
Expected total return (%)	+5.1

SHARE PRICE CHART




Share price performance (%)	Absolute	Relative
1 month	2.0	-1.5
3 months	2.1	7.7
12 months	-4.1	12.7

KEY STATISTICS

FBM KLCI	1389.55
Syariah compliant	Yes
Issue shares (m)	234.50
Estimated free float (%)	18.70
Market Capitalisation (RM'm)	32736.20
52-wk price range	RM120 - RM149.
Beta vs FBM KLCI (x)	0.51
Monthly velocity (%)	11.02
Monthly volatility (%)	4.23
3-mth average daily volume (m)	0.10
3-mth average daily value (RM'm)	14.07
Top Shareholders (%)	
Nestlé SA	72.61
EPF	7.91
Skim Amanah Saham Bumiputera	1.27

ANALYST

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Maintain NEUTRAL stance with a revised TP of RM143.90 (previously RM148.00). We have lowered our TP in-line with the changes in our earnings forecast. We maintain our DDM-derived valuation as the company is committed in paying out 95% of its net profit as dividend. While Covid-19 may pose a headwind to Nestlé's operations, as it may not be operating at its optimum compared to before due to the more stringent safety measures taken, we are also hopeful for new opportunities. Among others, the company will continue to launch new products in the second half of the year. Management will also speed up its e-commerce strength. All in all, we believe that Nestlé will continue to deliver stable profitability and thrive amid the Covid-19 outbreak. That said, we believe that valuations remain lofty at current level. Hence, our **NEUTRAL** recommendation is maintained. 

INVESTMENT STATISTICS

Financial year ending 31st December (in RM'm, unless otherwise stated)	2018	2019	2020E	2021F	2022F
Revenue	5,519.0	5,518.1	5,452.8	5,561.8	5,673.1
Cost of sales	(3,381.4)	(3,444.6)	(3,435.2)	(3,448.3)	(3,443.5)
Gross profit	2,137.7	2,073.5	2,017.5	2,113.5	2,229.5
PBT	875.9	875.7	845.2	889.9	958.7
PAT	658.9	672.9	659.2	694.1	747.8
Normalised PAT	648.4	672.9	659.2	694.1	747.8
EPS (sen)	274.0	287.0	281.1	296.0	318.9
Normalised EPS (sen)	276.5	287.0	281.1	296.0	318.9
Net Dividend (sen)	280.0	280.0	282.0	296.0	319.0
Gross profit margin (%)	38.7	37.6	37.0	38.0	39.3
PBT margin (%)	15.9	15.9	15.5	16.0	16.9
Normalised PAT margin (%)	11.7	12.2	12.1	12.5	13.2
Normalised EPS growth (%)	2.1	3.8	253.8	5.3	7.7
Dividend yield (%)	2.0	2.0	2.0	2.1	2.2
PER (x)	51.4	49.5	50.5	48.0	44.5

Source: Company, MIDFR

NESTLÉ (MALAYSIA) BERHAD: 1QFY20 Results Summary

FYE 31 st Dec (RMm)	Quarterly results			Cumulative results		
	1QFY20	YoY (%)	QoQ (%)	3MFY20	3MFY19	YoY (%)
Revenue	1,434.5	(1.3)	7.9	1,434.5	1,452.7	(1.3)
Cost of sales	(907.3)	2.7	10.3	(907.3)	(883.6)	2.7
Gross profit	527.2	(7.4)	4.1	527.2	569.1	(7.4)
Other income	-	(100.0)	nm	-	(247.4)	(100.0)
Operating expenses	(273.2)		(16.2)	(273.2)	0.0	
Operating profit	254.0	(21.1)	39.7	254.0	321.8	(21.1)
Finance costs	(8.9)	(12.4)	(12.7)	(8.9)	(10.2)	(12.4)
Finance income	0.7	(12.9)	(13.1)	0.7	0.9	(12.9)
Share of results of associated company	0.4	23.8	(237.0)	0.4	0.3	23.8
PBT	246.3	(21.3)	43.0	246.3	312.8	(21.3)
Taxation	(60.0)	(22.7)	48.6	(60.0)	(77.6)	(22.7)
PAT	186.3	(20.8)	41.4	186.3	235.2	(20.8)
One-off items	-	nm	nm	-	0.0	nm
Normalised PAT	186.3	(20.8)	41.4	186.3	235.2	(20.8)
Basic EPS (sen)	79.5	(20.8)	41.4	79.5	100.3	(20.8)
Normalised EPS (sen)	79.5	(20.8)	41.4	79.5	100.3	(20.8)
	-	<i>+ / (-) ppts</i>				
Gross profit margin (%)	36.8	(2.4)	(1.4)	36.8	39.2	(2.4)
Operating profit margin (%)	17.7	(4.4)	4.0	17.7	22.2	(4.4)
PBT margin (%)	17.2	(4.4)	4.2	17.2	21.5	(4.4)
Normalised PAT margin (%)	13.0	(3.2)	3.1	13.0	16.2	(3.2)
Effective Tax rate (%)	24.3	(0.5)	0.9	24.3	24.8	(0.5)

Source: Company, 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.