

FX Devaluation Undermines Positive Operating Performance

Food Segment Anchors Topline Performance

In its H1:2023 financial scorecard, **NESTLE** recorded a 17.68% improvement in topline to NGN261.77bn from NGN222.45bn in H1:2022. Higher revenue from the domestic market (+18.74%YoY), supported the firm's performance, as export sales continued to decline for the fourth consecutive quarter (since Q3:2022). Given that export sales to the Ghanaian market (which typically contributes c.80% to its export sales) was a major reason for the export sales decline witnessed in 2022, we do not rule out the possibility of that still being the case with the H1:2023 financial result as the country's current economic situation. Also, we consider the possibility of a gradual reduction in production for export as logistics conditions remain challenging. The H1:2023 performance was also supported by an upward revision of the prices on products in the food segment (which typically makes up c.61% of total revenue) like Maggi and Golden Morn. Sales volumes (on its seasoning and infant nutrition products) also increased in the period, pushing the segment's revenue higher by +25.54%YoY to NGN166.27bn (from NGN132.45bn in H1:2023). Riding on the introduction of the new 3-in 1 Milo product, the Beverage segment recorded marginal growth of 6.11%YoY to NGN95.50bn (from NGN90.00bn). Lastly, we highlight that the Q2:2023 standalone topline performance of NGN133.80bn represents the firm's record high in a single quarter.

While heightened competition, weakening consumer purchasing power and a challenging business environment are major headwinds to volume growth in the domestic market, we expect that the essential nature of the company's product, brand loyalty it enjoys and price reviews on products to sustain topline performance in the domestic market. Export sales should however sustain its downward trend in the near term till economic condition improve with export partner countries (like Ghana, Ivory coast and Burkina Faso). We have thus modelled a 21.15%YoY growth in 2023FY revenue to NGN541.30bn (vs. NGN351.82bn in 2022FY).

Margins Buckle Under Significant Devaluation Losses

NESTLE's production cost expanded by 8.57% YoY to NGN154.43bn, slower than growth in revenue. As a result, its cost to sales ratio improved to 59.00% (from 63.94% in H1:2022). Operating expenses also expanded by 36.79%YoY on the back of higher advertising (+76.63%YoY), personnel (+10.23% YoY) and delivery expenses (+18.00% YoY). Nevertheless, operating margin improved to 23.22% (from 20.22% in H1:2023) on account of higher revenue performance. We note the significant surge in finance cost to NGN137.73bn owing to the increased exchange rate losses (+5722.85% YoY) as the firm's interest-bearing liabilities (owed in USD to its related parties) were revalued upwards due to the devaluation of the Naira to NGN860.00/USD (from NGN461.32/USD). The interest coverage ratio also contracted significantly to 4.36x in H1:2023 (from 9.55x recorded in H1:2022). This resulted in a loss after tax of **NGN49.98bn** (from a profit after tax of NGN27.75bn in H1:2023). **While we remain optimistic about the firm's revenue performance and prospects in the long run, we expect NESTLE to end 2023FY in a loss position of NGN36.25bn due to the impact of the exchange rate revaluation loss on its finance cost.**

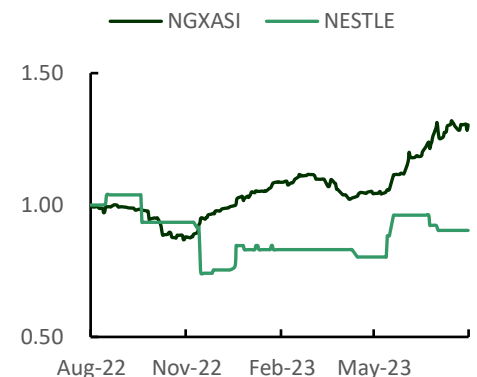
Dividend Payout Policy to Adjust Marginally

Due to its robust dividend payout policy – where a significant portion of its earnings are paid out as dividends (average of c.104% over the past 5 years) – **NESTLE's** retained earnings could hardly withstand the significant loss recorded in H1:2023. This wiped out its retained earnings and plunged its shareholders' equity in the negative region. Given its attraction as a dividend-paying stock (interim and final), we expect a marginal shift in this policy for 2023FY and 2024FY.

Recommendation

We project a 2023FY expected EBITDA of NGN139.62 and a target EV/EBITDA of 9.49x. This yields a target price of NGN1,324.52 and an implied upside potential of 12.73% based on the closing price on August 10th, 2023. Hence, we rate the ticker a **BUY**.

Company	NESTLE
Valuation	
Trailing EPS	486.14
BVPS	-61.36
P/E	-32.38x
P/BV	-19.15x
Target EV/EBITDA	9.49x
Dec-2023 Exp. EBITDA	139.62
Dec 2023 Target price	1,324.52
Current Price	1,175.00
Up/Downside Potential	+12.73%
Ratings	BUY
Key metrics	
ROE	-102.75%
ROA	-10.85%
Net margin	-19.09%
Asset Turnover	0.57
Leverage	-9.47
Yr Hi	1,250.00
Yr Lo	1,043.80
YTD return	+6.82%
Beta	0.61
Adjusted Beta	0.74
Shares outstanding	0.79bn
Market cap [NGN]	931.37bn
Financial year end	December
Most Recent Period (MRP)	H1:2023



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Chart 1: Sensitivity Analysis

Sensitivity Analysis of Dec-2023 Target Price to key model inputs							Min	1,246.24
							Max	1,405.19
EPS								
	1,324.52	135.43	137.52	139.62	141.71	143.80		
Target PE	9.20x	1,246.24	1,265.52	1,284.79	1,304.06	1,323.33		
	9.34x	1,265.52	1,285.08	1,304.65	1,324.22	1,343.79		
	9.49x	1,284.79	1,304.65	1,324.52	1,344.39	1,364.26		
	9.63x	1,304.06	1,324.22	1,344.39	1,364.56	1,384.72		
	9.77x	1,323.33	1,343.79	1,364.26	1,384.72	1,405.19		

Financial Highlights and Forecasts (NGN billion)

Profit & Loss Account	H1:2022A	H1:2023A	2023F	2024F	2025F	2026F	2027F
Revenue	222.45	261.77	541.31	617.15	665.24	717.26	773.54
Cost of sales	142.25	154.43	336.60	383.58	414.09	447.28	483.38
Gross profit	80.21	107.33	315.37	359.41	386.82	416.25	447.91
Other income	34.02	46.54	105.85	121.01	130.43	140.64	151.67
Operating expense	46.18	60.79	98.85	112.56	120.72	129.35	138.49
Operating profit	6.96	137.73	154.30	56.45	51.21	54.31	44.82
Finance cost	43.74	(69.12)	-53.31	58.44	72.28	77.97	96.76
PBT	27.75	(49.98)	-36.25	39.74	49.15	53.02	65.80
PBT	222.45	261.77	541.31	617.15	665.24	717.26	773.54

Balance Sheet	2022A	H1:2023A	2022F	2023F	2024F	2025F	2026F
Property, Plant and Equipment	116.74	123.67	132.17	151.39	172.10	194.49	217.92
Total Debt	155.43	299.84	293.47	395.69	485.02	523.58	460.02
Total Assets	415.04	460.61	488.03	692.95	840.99	940.14	944.97
Total Equity	30.29	-48.64	-34.86	0.92	34.22	67.42	105.48
Total Current Liabilities	218.40	240.52	263.00	338.58	376.49	408.11	426.15
Non-Current Liabilities	166.35	268.73	259.90	353.45	430.28	464.61	413.33
Total Liabilities	384.75	509.25	522.89	692.04	806.77	872.72	839.49

Financial Ratios	2022A	H1:2023A	2022F	2023F	2024F	2025F	2026F
Gross Margin	56.49%	36.06%	58.26%	58.24%	58.15%	58.03%	57.90%
Operating Margin	19.45%	20.76%	18.26%	18.24%	18.15%	18.03%	17.90%
Net Margin	10.97%	12.48%	-6.70%	6.44%	7.39%	7.39%	8.51%
Return on Asset	11.80%	-10.85%	-7.43%	5.74%	5.84%	5.64%	6.96%
Return on Equity	161.74%	-	-	326.94%	143.65%	78.64%	62.38%
Return on Invested Capital	85.04%	-	-	310.53%	169.60%	126.45%	42.46%
Asset Turnover	1.08x	0.57x	1.11x	0.89x	0.79x	0.76x	0.82x
Financial Leverage	13.70x	-9.47x	-14.00x	754.45x	24.58x	13.94x	8.96x
Debt to Asset Ratio	2.67x	1.54x	1.66x	1.75x	1.73x	1.80x	2.05x
Debt to EBIT Ratio	1.79x	4.93x	2.97x	3.52x	4.02x	4.05x	3.32x
Current Ratio	1.33x	1.26x	1.22x	1.57x	1.75x	1.80x	1.68x
Quick Ratio	0.93x	0.91x	0.87x	1.30x	1.46x	1.50x	1.38x

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Movements in Price Target

Company Name: Nestle Nigeria Plc

Date	Price (N)	Previous Target Price(N)	New Target Price (N)	Previous Recommendation	New Recommendation
10- Aug-2023	1,175.00	1,493.49	1,324.952	BUY	BUY

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Company	Disclosure
Nestle Nigeria Plc	

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