



NESTLE LANKA PLC [NEST.N0000]

MAINTAIN BUY

TOP-LINE SHAPE UP ON EMERGING CONSUMER DEMAND

Fair Value: 2021E - LKR 1,550 [+48%]

Total Return with DPS: 2021E - 50% [AER 98%]

2022E - LKR 1,650 [+58%]

2022E - 67% [AER 38%]

NEST recorded a massive growth in earnings for 1Q2021 up by 170.3%YoY to record at LKR 1.7Bn compared to LKR 0.6Bn recorded in 1Q2020. The profit boost is largely attributable to the surge in revenue by 24.9% to LKR 11.5Bn in contrast to LKR 9.2Bn in 1Q2020 supported by the rise in domestic retail sales. The gradual revival in consumer demand, which was suppressed due to the Covid-19 pandemic, and the positive impact on export sales stemming from the downward pressure on rupee are counted as plus points for NEST's growth forecast. Therefore, we are reinstating our earnings forecast while profitability targets are upgraded for 2021E and 2022E to LKR 4.7Bn and LKR 5.2Bn, respectively. Thereby, we upgrade our fair value for 2021E to LKR 1,550 (previous TP – LKR 1,500) and 2022E to LKR 1,650. **MAINTAIN BUY**

LKR (Mn)	1Q2020	1Q2021	YoY	2019	2020	YoY
Earnings (LKR 'Mn)						
Revenue	9,170	11,455	+25%	36,355	37,866	+4%
Gross Profit	2,965	4,079	+38%	11,941	12,219	+2%
EBIT	953	1,721	+81%	4,089	4,497	+10%
PBT	904	1,817	+101%	3,770	4,264	+13%
Net Profit	644	1,742	+170%	2,566	2,947	+15%
Balance Sheet (LKR 'Mn)						
Shareholder's Equity	4,636	5,796	+25%	5,510	5,934	+8%
Borrowings	4,041	4,037	+0%	2,972	2,138	-28%
NAVPS	86.3	107.9		102.6	110.4	

Earnings surged by 170.3%YoY as consumer demand uprise

NEST's earnings for 1Q2021 up by 170.3%YoY to book at LKR 1.7Bn, mostly derived from the growth in revenue by 24.9%YoY to LKR 11.5Bn on the back of improved consumer demand and gradual expansion of export performances. A portion of top-line growth in the form of export sales, mainly oriented on coconut milk powder product and dairy products, can also be attributable to the sharp depreciation of LKR against USD by 7.0% during 1Q2021. In view of stronger than expected quarterly results, we upgrade our revenue targets for 2021E and 2022E to LKR 43.7Bn (+9% from previous target) and LKR 47.6Bn (+13% from previous target) respectively. Moreover, in line with the expected growth in top-line, we restated our earnings targets for 2021E and 2022E to LKR 4.7Bn and LKR 5.2Bn, respectively.

Enhanced margins in 1Q2021 amidst increase in raw material prices

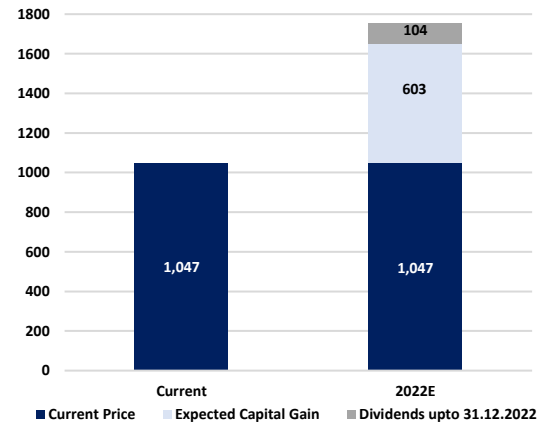
Despite the challenges triggered during Covid-19 pandemic in sourcing key raw materials such as wheat, sugar, etc., due to the import restrictions along with the rapid increase in prices, including the locally sourced coconuts, NEST's GP margin improved by 328bps to 36% during 1Q2021 compared to 32% in 1Q2020. Therefore, we expect GP margin to stabilize within the range of 35% - 36% during 2021E and 2022E on the back of the solid top-line growth.

New Income tax regime to boost bottom-line

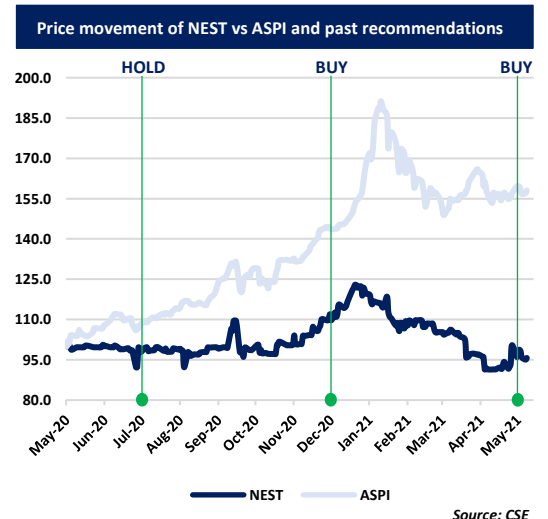
NEST's tax expense has significantly shrunk by 71.2%YoY to LKR 74.9Mn in 1Q2021 as a direct result of adopting new multiple tax brackets for manufacturing at 18%, export at 14% and the other income at 24%, as opposed to the previous standard rate of 28%. These revisions are also expected to have a retrospective effect from 1st Jan 2020 enabling NEST to achieve remarkable tax savings in the coming years to aid the bottom-line growth.

FV is upgraded to LKR 1,550 for 2021E and LKR 1,650 for 2022E - MAINTAIN BUY

On the strength of the topline growth steered by progressive revival of consumer demand and the expected upswing in the export sales, we upgrade our NEST's fair value to LKR 1,550 for 2021E and LKR 1,650 for 2022E with a total return of 50% and 67% respectively. **MAINTAIN BUY**



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Source: CSE

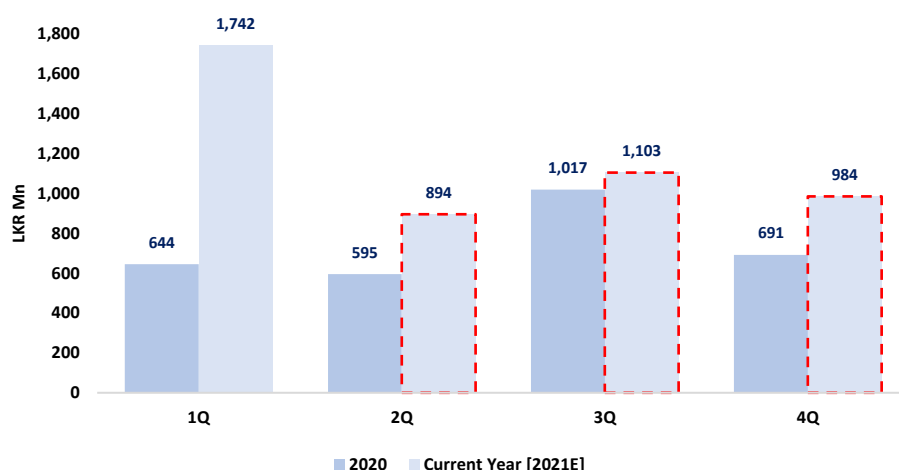
Minimum Return for BUY:

Buy Below 2021E - [AER of 13% with DPS]: LKR 1,456
 NEST categorized as 'Grade B' counter

Disclosure on Shareholding:

First Capital Group or the covering analyst did not hold 1% or more of the total outstanding share capital of NEST during the five trading days prior to the issuance of this document.

Quarterly Earnings



Estimate Revision

In LKR Mn	2021E-O	2021E-R	% Change	2022E - O	2022E - R	% Change
Earnings Estimate						
Revenue	40,081	43,692	+9%	42,086	47,570	+13%
Gross Profit	13,784	15,729	+14%	14,894	16,887	+13%
EBIT	4,673	5,787	+24%	5,354	6,413	+20%
Profit before Tax	4,621	5,759	+25%	5,292	6,384	+21%
Net Profit	3,327	4,723	+42%	3,810	5,235	+37%
Adjusted EPS	61.9	87.9		49.4	97.4	
Growth YoY	7%	60%		15%	11%	
Balance Sheet Estimate						
Shareholders' Equity	6,678	7,701	+15%	7,727	8,450	+9%
Borrowings	3,572	741	-79%	3,672	746	-80%
Adjusted NAVPS	124.3	143.3		143.8	157.3	
Ratio Estimate						
ROE (%)	50%	61%		49%	62%	
PER (x)	19.8	11.9		17.3	10.7	
PBV (x)	9.9	7.3		8.5	6.7	

Valuation Table

P/E 31 December	2017	2018	2019	2020	2021E	2022E	2023E
Estimates (LKR 'Mn)							
Revenue	37,601	37,337	36,355	37,866	43,692	47,570	50,095
Operating Profit	4,888	5,147	4,089	4,497	5,787	6,413	6,514
Net Profit	3,636	3,486	2,566	2,947	4,723	5,235	5,317
EPS (LKR)	67.7	64.9	47.8	54.9	87.9	97.4	99.0
YoY % Growth	-17%	-4%	-26%	15%	60%	11%	2%
Valuations							
PER (x)	15.5x	16.1x	21.9x	19.1x	11.9x	10.7x	10.6x
PBV (x)	11.7x	10.0x	10.2x	9.5x	7.3x	6.7x	6.4x
DY (%)	4.8%	4.8%	4.5%	5.3%	8.0%	8.8%	9.0%

Valuation Summary

Expected NEST price	2021E	2022E
PER based target price	1,582	1,754
DCF Valuation based target price	1,533	1,551
Average Target Price	1,558	1,652
Target price after Rounding off	1,550	1,650

Return	2021E	2022E
Target Price	1,550	1,650
Current Price	1,047	1,047
Capital Gain (LKR)	503	603
Dividend upto 31 Dec (LKR)	20	104
Capital Gain %	48%	58%
Dividend Yield %	2%	10%
Total Return %	50%	67%
Annualized Return %	98%	38%

Discounted Cash flow Valuation

DCF based Valuation	2021E	2022E
Enterprise Value	82,341	83,204
(-) Debt	(826)	(830)
(+) Cash	839	942
Total Value of Equity	82,354	83,315
No. of shares	54	54
Target Price	1,533	1,551

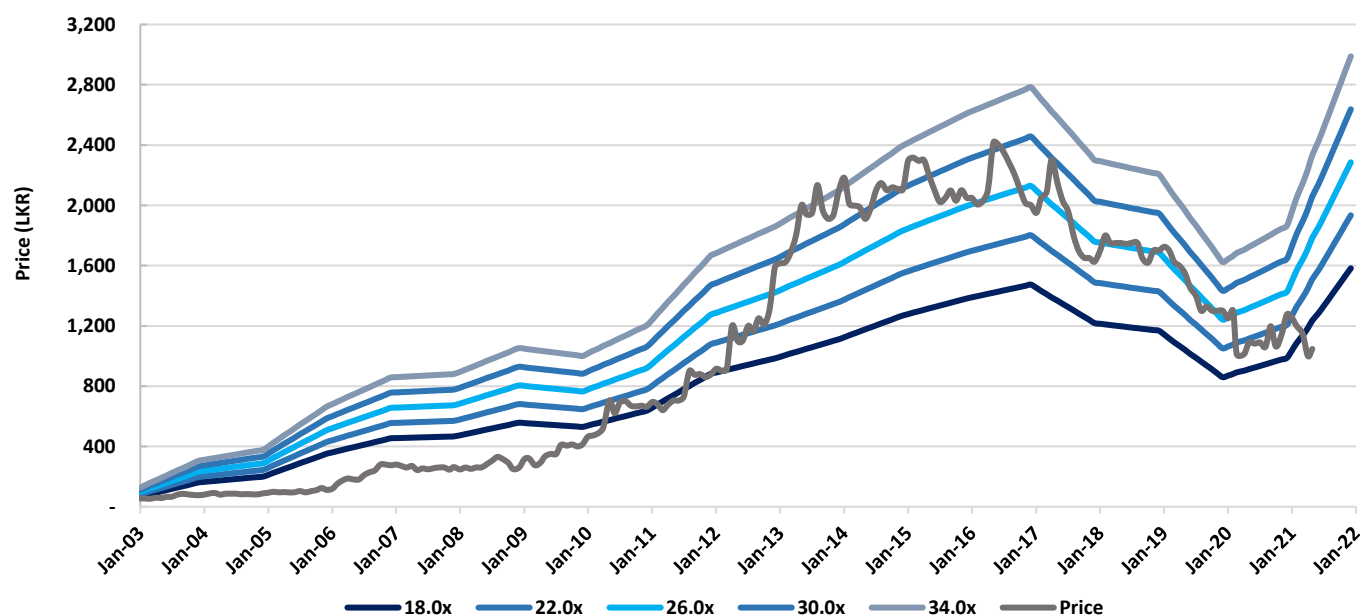
COE	2021E	2022E
R_f	7.0%	7.5%
R_m	15%	16%
Growth %	3%	3%
β	0.50	0.50
$K_e = R_f + \beta (R_m - R_f)$	11%	12%

PER Valuation

PER based Valuation	2021E	2022E
Earnings (LKR 'Mn)	4,723	5,235
No. of Shares ('Mn)	54	54
EPS	87.9	97.4
Expected Average PER	18x	18x
Price at 18.0x Earnings	1,582	1,754

WACC	2021E	2022E
K_e	11%	11%
K_d	9%	9%
D/E Assumption	30 / 70	30 / 70
Terminal Growth (%)	3%	3%
WACC	10%	10%

PER Chart



Appendix I: Statement of Income and Expenses

Income Statement (LKR Mn)	2017	2018	2019	2020	2021E	2022E	2023E
Y/E 31st December							
Revenue	37,601	37,337	36,355	37,866	43,692	47,570	50,095
Cost of Sales	-24,525	-23,630	-24,414	-25,647	-27,963	-30,682	-32,562
Gross Profit	13,076	13,707	11,941	12,219	15,729	16,887	17,533
Other Operating Income / (Expense)	-45	-135	-136	-57	-57	-57	-57
Marketing, Selling and Distribution Expenses	-5,828	-6,056	-5,224	-5,129	-7,209	-7,611	-8,015
Administrative Expenses	-2,315	-2,369	-2,493	-2,536	-2,676	-2,807	-2,948
Results from Operating Activities	4,888	5,147	4,089	4,497	5,787	6,413	6,514
Finance Income	30	46	37	39	71	71	71
Finance Expenses	-183	-252	-356	-272	-99	-100	-100
Net Finance Expense	-153	-206	-319	-233	-28	-29	-29
Profit Before Taxation	4,735	4,941	3,770	4,264	5,759	6,384	6,485
Income Tax Expense	-1,099	-1,456	-1,204	-1,317	-1,037	-1,149	-1,167
Profit for the Year	3,636	3,486	2,566	2,947	4,723	5,235	5,317
EPS	67.7	64.9	47.8	54.9	87.9	97.4	99.0

Appendix II: Statement of Financial Position

Balance Sheet (LKR Mn)	2017	2018	2019	2020	2021E	2022E	2023E
As at 31st December							
ASSETS							
Non-Current Assets							
Property, Plant and Equipment	5,366	9,210	9,012	8,397	8,284	7,926	7,917
	8,170	10,237	9,756	9,270	9,307	8,799	8,940
Current Assets							
Inventories	2,870	2,988	3,486	4,948	5,680	6,184	6,512
Trade and Other Receivables	3,647	3,362	2,687	2,046	2,622	3,806	4,008
Cash and Cash Equivalents	129	218	508	2,508	839	942	997
	7,406	7,422	7,115	9,942	9,580	11,372	11,957
Total Assets	15,577	17,659	16,871	19,212	18,888	20,171	20,898
EQUITY AND LIABILITIES							
Equity							
Stated Capital	537	537	537	537	537	537	537
Retained Earnings	4,264	5,098	4,972	5,397	7,164	7,913	8,257
	4,801	5,635	5,510	5,934	7,701	8,450	8,794
Non-Current Liabilities							
Non Current Financial Liabilities	12	2,008	1,984	84	84	84	84
	1,496	3,689	3,772	2,084	2,084	2,084	2,084
Current Liabilities							
Trade and Other Payables	4,770	4,635	4,951	6,225	5,593	6,136	6,512
Bank Overdrafts	2,592	1,524	988	2,054	741	746	751
Total Current Liabilities	9,280	8,335	7,589	11,194	9,102	9,637	10,020
Total Liabilities	10,776	12,024	11,361	13,278	11,186	11,721	12,104
Total Equity and Liabilities	15,577	17,659	16,871	19,212	18,888	20,171	20,898
NAVPS	89.4	104.9	102.6	110.4	143.3	157.3	163.7



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