Business Data Management
Professor G. Venkatesh
Professor M Suresh Babu
Department of Humanities and Social Sciences
Indian Institute of Technology Madras
FMCG industry - Nestle

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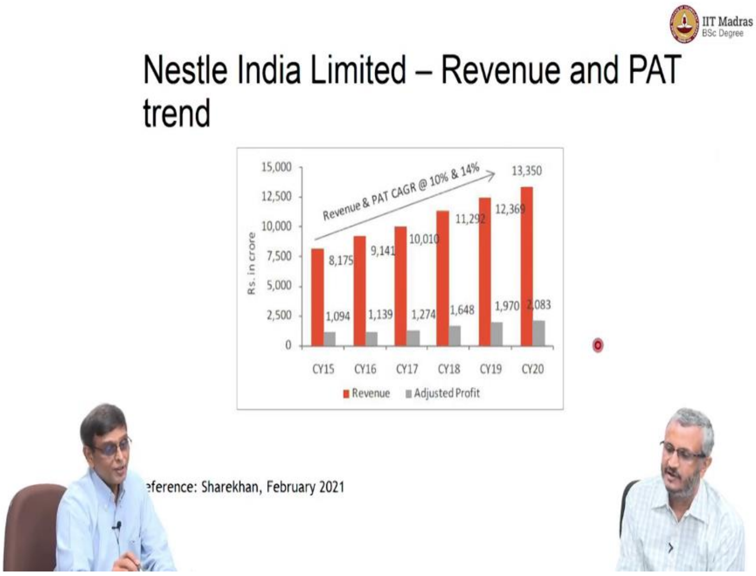

Professor G. Venkatesh: Let us look at the next one, Nestle. This one is another different type. It is FMCG. So, FMCG basically, there are categories. Like baby food, coffee, tea, all that stuff or, whatever it is.

Professor M Suresh Babu: So, the uniqueness of this industry is product differentiation.

Professor G. Venkatesh: Product differentiation, tremendous product.

Professor M Suresh Babu: It is a monopolistically competitive market.

Professor G. Venkatesh: Because even though Nestle may not be number 1 in the industry. Unilever and all that are higher, much higher, way ahead. Even Patanjali, I think, is relatively high now. Nestle might be 4 or 5 or something in the list ranking. But even then, in their categories where they are leaders, they are way ahead of everybody else. And they are leaders.

Professor M Suresh Babu: So, you create that niche where you are a monopolist.

Professor G. Venkatesh: Like noodles or whatever it is. And even baby food. I think Nestle is way above everybody. And they make huge margins in those businesses. So, both revenue and PAT have been growing between 10 % and 14 % year on year. And this looks good.

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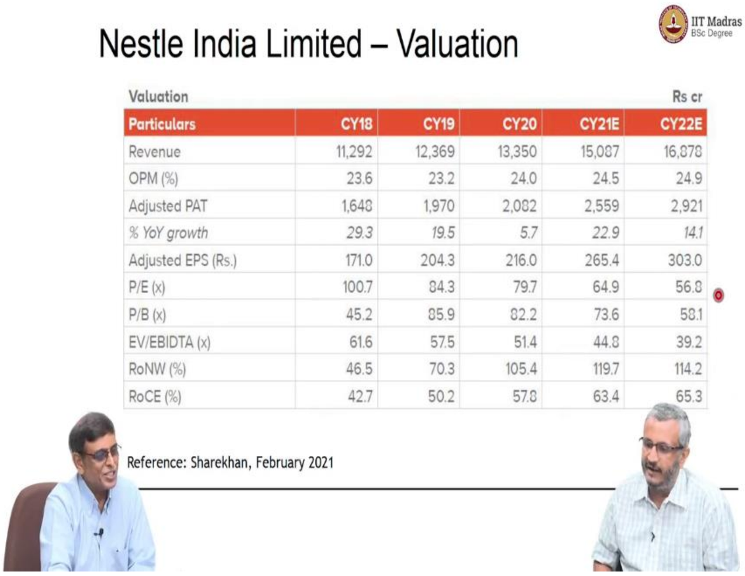

Particulars	CY18	CY19	CY20	CY21E	CY22E
Revenue	11,292	12,369	13,350	15,087	16,878
OPM (%)	23.6	23.2	24.0	24.5	24.9
Adjusted PAT	1,648	1,970	2,082	2,559	2,921
% YoY growth	*29.3*	*19.5*	*5.7*	*22.9*	*14.1*
Adjusted EPS (Rs.)	171.0	204.3	216.0	265.4	303.0
P/E (x)	100.7	84.3	79.7	64.9	56.8
P/B (x)	45.2	85.9	82.2	73.6	58.1
EV/EBIDTA (x)	61.6	57.5	51.4	44.8	39.2
RoNW (%)	46.5	70.3	105.4	119.7	114.2
RoCE (%)	42.7	50.2	57.8	63.4	65.3

But actually, we will see that there is some concern. Since the last year, things have been declining, so FMCGG today is not in favor among investors. It is actually in the decline stage.

Professor M Suresh Babu: I see. So, these are the valuation ratios.

Professor G. Venkatesh: These are valuation ratios.

Professor M Suresh Babu: Price-earnings ratio.

Professor G. Venkatesh: So, you can see our ROCE here also, similar to page industries is in the 50 % range, and expected even go up to 60-odd % range.

Professor M Suresh Babu: 60 %,65 %.

Professor G. Venkatesh: Which is in line with the international benchmarks. For this industry.

Professor M Suresh Babu: And revenues?

Professor G. Venkatesh: Revenue growth? Yeah. Not very high, but in some fact, actually it is in the declining. It is in the declining stage.

Professor M Suresh Babu: That is why even the projections are not very good.

Professor G. Venkatesh: In fact, these are, I think, still optimistic. Things are looking bad because of the demand due to post COVID. And even before COVID, we have seen a slight dip in demand.

Professor M Suresh Babu: Aggregate demand?

Professor G. Venkatesh: And that is affecting this industry as well. But see the price-earnings ratios-this one. So, I mean, you can explain it with growth, but there is not that much growth in this case. You can explain it by profitability, but these guys are not increasing their profitability. So, it is kind of overvalued at this stage.

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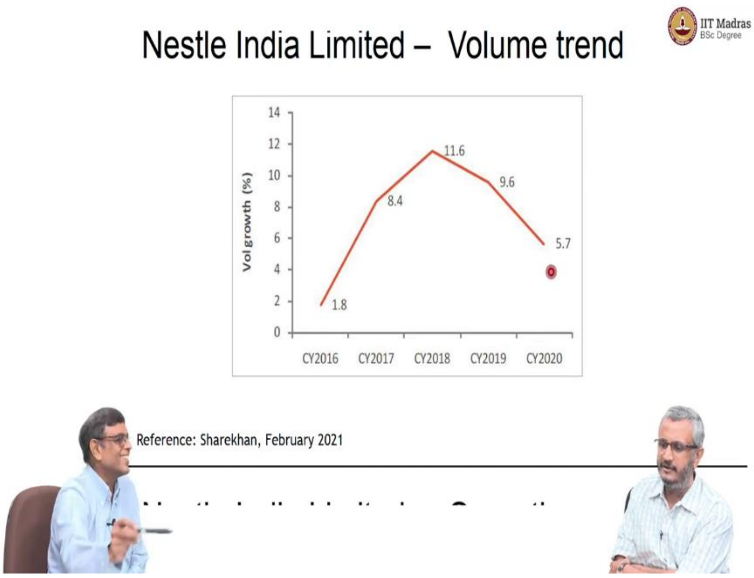

Professor G. Venkatesh: This industry. So, here is a chart that basically shows what is happening to volume growth? You can see, it went up to 11.6. So, the volume growth rate in India historically, FMCG has been in a 15 % number. It will be GDP plus inflation rate you add up so that, like 13, 14 %. I do not know what it is? , it will be correct. So, you add inflation to the GDP growth rate. So, GDP growth rate 7 %, or $7\frac{1}{2}$%. Plus, you add inflation 4, 5 %. So, it should be at least $12\frac{1}{2}$%.

Professor M Suresh Babu: 12 %, $12\frac{1}{2}$%.

Professor G. Venkatesh: So, this industry has been doing 15 %. But if you see now, that is declining.

Professor M Suresh Babu: Decline. So, the way to interpret this is that the firm has not been able to grow or keep pace in terms of sales growth. It has not been able to sell in the market as much as it would have liked to sell.

Professor G. Venkatesh: Right.

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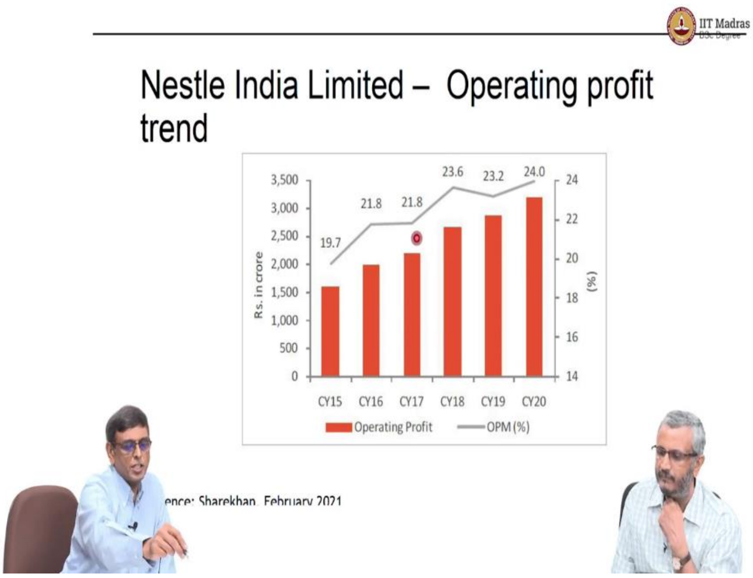

Professor G. Venkatesh: So, see the operating profit. Margin has been pretty okay. They manage their costs pretty okay. In fact, it has been an improving trait.

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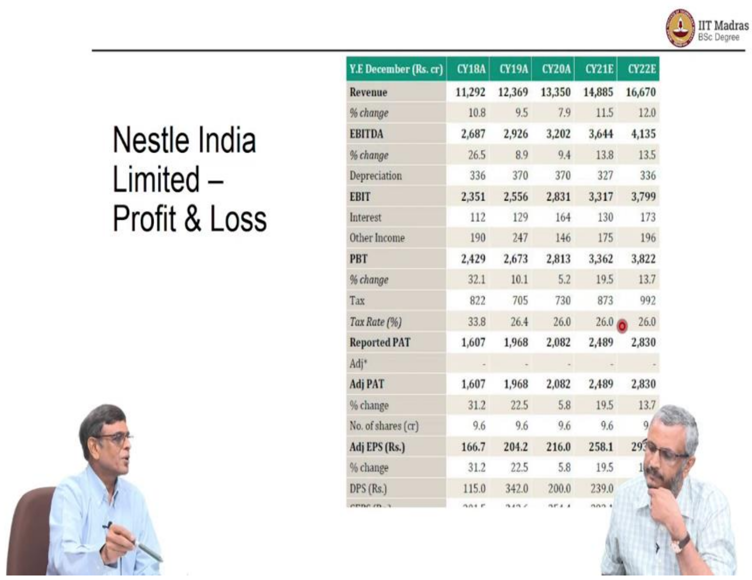

Y.E December (Rs. cr)	CY18A	CY19A	CY20A	CY21E	CY22E
Revenue	11,292	12,369	13,350	14,885	16,670
% change	10.8	9.5	7.9	11.5	12.0
EBITDA	2,687	2,926	3,202	3,644	4,135
% change	26.5	8.9	9.4	13.8	13.5
Depreciation	336	370	370	327	336
EBIT	2,351	2,556	2,831	3,317	3,799
Interest	112	129	164	130	173
Other Income	190	247	146	175	196
PBT	2,429	2,673	2,813	3,362	3,822
% change	32.1	10.1	5.2	19.5	13.7
Tax	822	705	730	873	992
Tax Rate (%)	33.8	26.4	26.0	26.0	26.0
Reported PAT	1,607	1,968	2,082	2,489	2,830
Adj*	-	-	-	-	-
Adj PAT	1,607	1,968	2,082	2,489	2,830
% change	31.2	22.5	5.8	19.5	13.7
No. of shares (cr)	9.6	9.6	9.6	9.6	[illegible]
Adj EPS (Rs.)	166.7	204.2	216.0	258.1	[illegible]
% change	31.2	22.5	5.8	19.5	[illegible]
DPS (Rs.)	115.0	342.0	200.0	239.0	[illegible]

Professor G. Venkatesh: So.

Professor M Suresh Babu: Profit and loss statement?

Professor G. Venkatesh: See, I mean, what we had shown in the first chart, nothing new to show over here.

Professor M Suresh Babu: Tax?

Professor G. Venkatesh: So, the tax rate is what I wanted to show you. So, you can see that 33.8 %, the tax rate, has come down to 26.4 % and then come down to 26 %, projected to remain at 26

%. So, they have been able to take advantage of the favorable tax regime now in India, the lower tax regime 22%. Plus, because you have to do surcharge and this and that and so on. So, added up, it comes to about 26 %.

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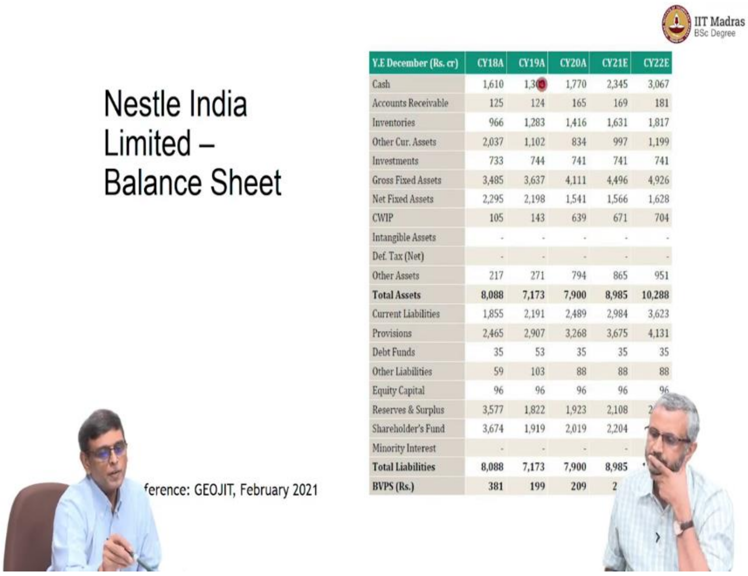

Y.E December (Rs. cr)	CY18A	CY19A	CY20A	CY21E	CY22E
Cash	1,610	1,30[illegible]	1,770	2,345	3,067
Accounts Receivable	125	124	165	169	181
Inventories	966	1,283	1,416	1,631	1,817
Other Cur. Assets	2,037	1,102	834	997	1,199
Investments	733	744	741	741	741
Gross Fixed Assets	3,485	3,637	4,111	4,496	4,926
Net Fixed Assets	2,295	2,198	1,541	1,566	1,628
CWIP	105	143	639	671	704
Intangible Assets	-	-	-	-	-
Def. Tax (Net)	-	-	-	-	-
Other Assets	217	271	794	865	951
Total Assets	**8,088**	**7,173**	**7,900**	**8,985**	**10,288**
Current Liabilities	1,855	2,191	2,489	2,984	3,623
Provisions	2,465	2,907	3,268	3,675	4,131
Debt Funds	35	53	35	35	35
Other Liabilities	59	103	88	88	88
Equity Capital	96	96	96	96	96
Reserves & Surplus	3,577	1,822	1,923	2,108	[illegible]
Shareholder's Fund	3,674	1,919	2,019	2,204	[illegible]
Minority Interest	-	-	-	-	[illegible]
Total Liabilities	**8,088**	**7,173**	**7,900**	**8,985**	[illegible]
BVPS (Rs.)	**381**	**199**	**209**	[illegible]	[illegible]

Professor G. Venkatesh: So, from the balance sheet perspective, you see that we can do that; we will do the ratios.

Professor M Suresh Babu: I do not see Nestle is increasing their investments very high in the future.

Professor G. Venkatesh: Again, here we have high indeed. You do not see many investments.

Professor M Suresh Babu: Because 733, they are going up to 741 and gross fixed assets, perhaps.

Professor G. Venkatesh: Not growing much.

Professor M Suresh Babu: Over a longer period, they have been only growing. So, does that mean that the firm is not very keen on expanding more or is not growing?

Professor G. Venkatesh: It is not growing. I mean, they have not seen growth. They are kind of stuck. That is clear. It is coming out very clearly. So, we are just showing up. There is not much investing, just managing cash. It is just a utility-like thing. So, it is just generating cash-good cash, good ROCE, and good operating margin.

Professor M Suresh Babu: And doing that business.

Professor G. Venkatesh: Maybe, buy back shares, give dividends. It is a good dividend-paying company. So, you pay a dividend. I do not know if the dividend is listed here, but yeah, they pay good dividends.

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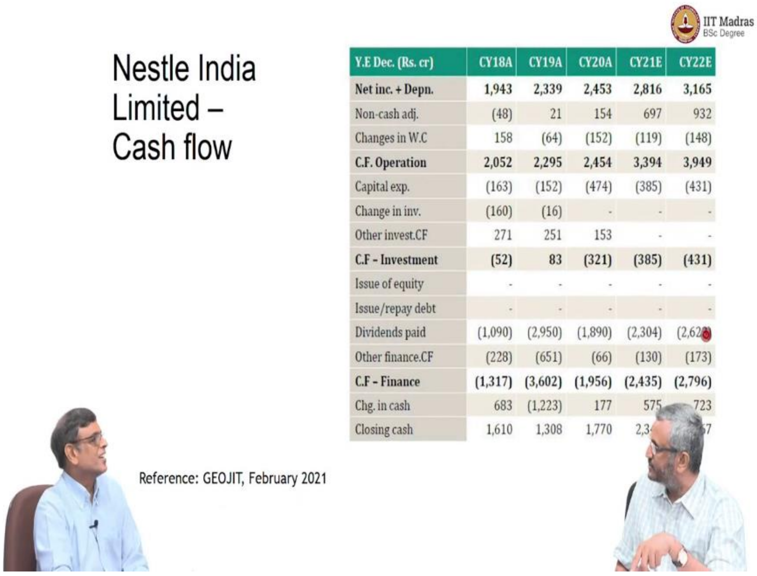

Y.E Dec. (Rs. cr)	CY18A	CY19A	CY20A	CY21E	CY22E
Net inc. + Depn.	**1,943**	**2,339**	**2,453**	**2,816**	**3,165**
Non-cash adj.	(48)	21	154	697	932
Changes in W.C	158	(64)	(152)	(119)	(148)
C.F. Operation	**2,052**	**2,295**	**2,454**	**3,394**	**3,949**
Capital exp.	(163)	(152)	(474)	(385)	(431)
Change in inv.	(160)	(16)	-	-	-
Other invest.CF	271	251	153	-	-
C.F - Investment	**(52)**	**83**	**(321)**	**(385)**	**(431)**
Issue of equity	-	-	-	-	-
Issue/repay debt	-	-	-	-	-
Dividends paid	(1,090)	(2,950)	(1,890)	(2,304)	[illegible]
Other finance.CF	(228)	(651)	(66)	(130)	(173)
C.F - Finance	**(1,317)**	**(3,602)**	**(1,956)**	**(2,435)**	**(2,796)**
Chg. in cash	683	(1,223)	177	575	723
Closing cash	1,610	1,308	1,770	[illegible]	[illegible]

Professor G. Venkatesh: So, this is cash or dividend. You can see again here; this is a huge cash generator. See the cash, 2,000 crores of cash in a year- a phenomenal cash machine. They are generating a huge amount of cash without investments. A Little bit is being invested, but most of it is being given out as a dividend. So, if they saw growth, they would not give out so much dividend; they will keep it to grow. But since they are not saying that they are giving.

Professor M Suresh Babu: So, as a retail investor, I am very happy to put my money into this because I will get the dividend.

Professor G. Venkatesh: You will get dividends. It is like getting the interest from your bank or getting a fixed deposit or something.

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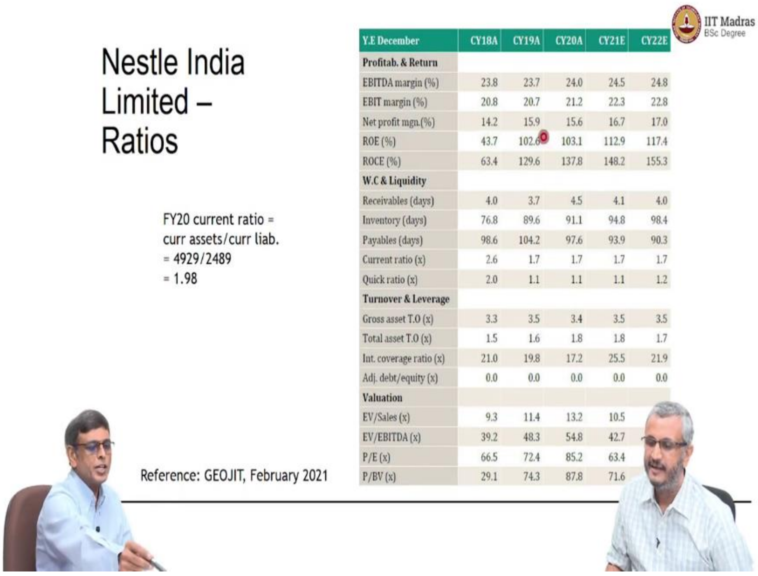

Y.E December	CY18A	CY19A	CY20A	CY21E	CY22E
Profitab. & Return					
EBITDA margin (%)	23.8	23.7	24.0	24.5	24.8
EBIT margin (%)	20.8	20.7	21.2	22.3	22.8
Net profit mgn.(%)	14.2	15.9	15.6	16.7	17.0
ROE (%)	43.7	102.6	103.1	112.9	117.4
ROCE (%)	63.4	129.6	137.8	148.2	155.3
W.C & Liquidity					
Receivables (days)	4.0	3.7	4.5	4.1	4.0
Inventory (days)	76.8	89.6	91.1	94.8	98.4
Payables (days)	98.6	104.2	97.6	93.9	90.3
Current ratio (x)	2.6	1.7	1.7	1.7	1.7
Quick ratio (x)	2.0	1.1	1.1	1.1	1.2
Turnover & Leverage					
Gross asset T.O (x)	3.3	3.5	3.4	3.5	3.5
Total asset T.O (x)	1.5	1.6	1.8	1.8	1.7
Int. coverage ratio (x)	21.0	19.8	17.2	25.5	21.9
Adj. debt/equity (x)	0.0	0.0	0.0	0.0	0.0
Valuation					
EV/Sales (x)	9.3	11.4	13.2	10.5	[illegible]
EV/EBITDA (x)	39.2	48.3	54.8	42.7	[illegible]
P/E (x)	66.5	72.4	85.2	63.4	[illegible]
P/BV (x)	29.1	74.3	87.8	71.6	[illegible]

Professor G. Venkatesh: So, again, here we can do the ratios the same way. And here, again, these people have.

Professor M Suresh Babu: 1.98, which is also very high. And their inventory days, as we see, is 3 months or close to 3 months. And we have the current ratio, as well as the quick ratio.

Professor G. Venkatesh: But, of course, they have calculated it 1.7 or something, whereas we got 1.9. So, there seems to be a discrepancy. I think, when students do it, also they should not just take the number from here. They should do it themselves and see whether there is a correct match or not because analysis could be a mistake.

Professor M Suresh Babu: And one more point G.V. The return on capital employed seems to be very high.

Professor G. Venkatesh: Where is ROCE?

Professor M Suresh Babu: Here.

Professor G. Venkatesh: 63, 129, 137. It means that 1-rupee invested in this business generates a profit of 1.37 rupees in 1 year.

Professor M Suresh Babu: Fantastic.

Professor G. Venkatesh: Yeah, it doubles. My 1-rupee investment almost doubles or more than doubles every year.

Professor M Suresh Babu: And it is expected to touch 155.3.

Professor G. Venkatesh: Look at that.

Professor M Suresh Babu: Phenomenal.

Professor G. Venkatesh: Phenomenal ROCEs. Phenomenal. And ROE is also similar. So, it is a rare case. And that is because of the way the business is structured. Because they use subcontracting, they do not lock capital. It is a business which tries to maximize the use of its capital. They do not use much of their capital.

Professor M Suresh Babu: And the net profit margin also seems to be above the cement industry, as well as textiles.

Professor G. Venkatesh: Correct. The net profit margin is about 15 %.

Professor M Suresh Babu: 15 %!

Professor G. Venkatesh: You will see, IT is much higher, but it is much higher than that.

Professor M Suresh Babu: Yeah. Around 9 % in cement and 11 %.

Professor G. Venkatesh: And about 14 %, 11 %, 12 %, 14 %, so that seems a little high.

Professor M Suresh Babu: Here, it is higher than that.

Professor G. Venkatesh: In fact, I would say Nestle is lower than Hindustan Lever. So, the other companies are better; Patanjali might be lower.

Professor M Suresh Babu: So, there are wide inter-industry variations in terms of the profit margins.