



Nestle upbeat despite consumer gloom, raises outlook

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By Katie Reid



ZURICH (Reuters) - The world's largest food company Nestle (NESN.VX: [Quote](#), [Profile](#), [Research](#), [Stock Buzz](#)) posted a top-of-the-range 6-percent rise in first-half profit on Thursday as it gave a slightly more upbeat forecast for 2008 and accelerated its share buyback programme.

The Swiss-based maker of Nescafe coffee, KitKat chocolate bars and Maggi soups is battling higher commodity costs like its rivals, and has pushed up prices to offset these effects but it is seeing some slowdown in volume growth in its second quarter.

Net profit rose to 5.2 billion Swiss francs (\$4.95 billion) in the first six months on 2008, slightly ahead of average analyst expectations for 5.05 billion and at the top of a 5.05 to 5.21 billion range.

Underlying sales, which strip out currency effects and acquisitions, rose 8.9 percent, in line with forecasts.

But pricing accounted for a higher-than-expected 5.4 percentage points and volume was 3.5 percent -- below the first-quarter's 4.5 percent.

Nestle shares fell more than 2 percent on concern over the volume growth and as the strong Swiss franc weighed on sales.

The shares were down 1 percent at 46.66 francs at 1310 GMT, slightly underperforming the DJ Stoxx European food and beverage index .

"With Q2 RIG (volume growth) below expectations and the margin quality open to debate, this may weigh on the shares," said industry analyst Jeff Stent at brokers Citi in London.

Julian Hardwick, an analyst at RBS, said: "Marketing spending was down 120 basis points -- a bigger decline than Unilever's (ULVR.L: [Quote](#), [Profile](#), [Research](#), [Stock Buzz](#))(UNc.AS: [Quote](#), [Profile](#), [Research](#), [Stock Buzz](#)) 70 basis points fall which sent its shares down 10 percent, and this may well be taken negatively for Nestle as some investors may take the view that marketing is being used to make the margin numbers."

But independent analyst **James Amoroso** said this was the right response to a "perfect storm of input costs, negative forex and reduced 'feel good' consumer factors".

Chief Financial Officer James Singh said in a conference call that Nestle was fully supporting its brands to make sure they remained competitive.

"With respect to what we call advertising and consumer promotion, our activities are increasing but we are finding better ways, more creative ways to get better value for money," Singh said.

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The maker of Buitoni pasta, Nespresso coffee and Friskies cat food gave a slightly more upbeat forecast, expecting organic growth in 2008 "at least" at the 2007 level of 7.4 percent.

It previously said it would "approach" that figure.

Nestle repeated that it expects "improved" earnings before interest and tax (EBIT) margins in 2008.

"Top line has always been amongst the best in the industry, but the group is now showing it can continuously improve margins too," said analyst Alex Molloy at Credit Suisse.

Like rivals Unilever and Danone (DANO.PA: [Quote](#), [Profile](#), [Research](#), [Stock Buzz](#)), Nestle has pushed through price hikes to offset spiralling input costs.

It sees 2.2 billion francs in extra costs for coffee, cocoa, and milk for 2008 weighted to the first half, suggesting a slowdown in price increases in the second half.

Singh said the group would raise prices further if needed.

"Most of our pricing actions are today in place, but I do not want to tell you that we are not going to take further price increases this year. We will if we think that this is the right thing to do," he said.

The group is speeding up its 25-billion franc three-year share buyback programme announced in August 2007 and said 13 billion francs would be completed by the end-2008. It will buy back 9 billion francs in 2008, 2 billion more than planned.

Overall group sales rose 3.8 percent to 53.07 billion francs, slightly below the average forecast in a Reuters poll of analysts of 53.41 billion francs.

Bottled water sales volumes fell 3.1 percent but Singh said water sales, which includes Vittel and Perrier brands, should improve in the second half.

Consumers are moving away from premium-priced waters to more affordable products and customers have also become more price sensitive with frozen food, Singh said.

Nestle has lost retail market share with water in the U.S. and marginally in Europe.

Its shares trade at about 14 times forecast 2009 earnings, above Unilever at 13 times and below Danone at 15.5 times, according to Reuters data.

(Editing by David Jones and Jason Neely)