

Unilever Nigeria Plc.

Expensive! SELL!

Despite significant revenue and EBIT growth in Q3, UNILEVER recorded y/y and q/q PBT contractions, and would have posted a loss after tax, save for a tax credit (N449.8 million). The company's production costs have risen quite significantly over the last two quarters, denying earnings the benefits from price increases (PIs). Notwithstanding, we look for 2016F PAT growth of 32% (previously 46%), driven specifically by (1) the continued impact of a strong first quarter performance (76% PAT growth) and (2) the tax credit booked in the third quarter.

Having said that, we believe it will take a while for UNILEVER's PAT to recover to the 2009-2013 level (of N4 billion and more). We forecast PAT to contract by 37.4% to N987 million in 2017 (vs. 5% growth initially forecasted) -- on (1) significant drop in revenue growth; (2) elevated production cost base; (3) tax charges, compared to expected credit in 2016; and (4) high interest expenses on increased debt balance - before rising to N2.6 billion and N2.9 billion in 2018 and 2019.

The performance of Nigeria's consumer goods companies will remain largely subdued in the short to medium term. While we expect production costs to peak at 2016 level, it is unlikely to decelerate in 2017, thus -- with further price increases (to match the carry-forward inflation) limited by very slow recovery in average purchasing power -- suggesting benign prospect for margin improvement. Note that our outlook for costs does not underestimate upside risk from Nigeria's unresolved FX challenges going into next year.

UNILEVER's finance cost in Q3 was at a record high level, likewise outstanding borrowings. The company has a recent history of debt accumulation impacting adversely on earnings through high finance costs. We have increased finance cost expectation for 2017 on the back of (1) increased borrowings over the last two quarters, after a marked reduction in the first quarter and (2) forex losses on USD loans (representing 53.4% of total loans).

On the positive, we note that sales, even amidst tough business environment, will remain supported by measures such as continued innovation (e.g improved packaging), local campaigns, brand extension, and the resilience of the Food division. Rather than PIs, we think revenue (via volume) will be buoyed by these measures, in addition to favourable brand mix (emphasizing expected recovery in the Personal Care division).

The stock has accumulated 12% gain YtD, but gained 44% in Q3, which we find unfounded. Despite weak earnings recovery prospect, UNILEVER is currently the most overvalued (-68.8% implied return) among our universe of consumer companies, with the stock trading on a forward PE of 69x, at 38% premium to Bloomberg's SSA, MEA and Nigerian peers. SELL.

Income Statement (N'bn)	30-Sep-16	30-Sep-15	Q3-16	Q3-16 y/y	Q3-16 q/q
Revenue	49.87	42.70	17.59	25.9%	13.5%
Cost of sales	35.17	27.84	13.25	49.4%	18.5%
Gross profit	14.70	14.86	4.35	-15.0%	0.6%
Operating expenses	11.60	12.57	3.40	-21.1%	-16.3%
Other income	0.01	0.08	0.01	7.3%	
EBIT	3.11	2.37	0.95	18.3%	275.1%
Finance income	0.14	0.22	-0.08	-187.1%	-146.7%
Financial charges	1.75	2.39	0.85	8.4%	143.5%
Profit before tax	1.51	0.20	0.02	-77.8%	-65.0%
Taxation	-0.06	0.06	-0.45	-966.5%	-2961.7%
Profit after tax	1.57	0.14	0.47	755.0%	807.3%

SELL

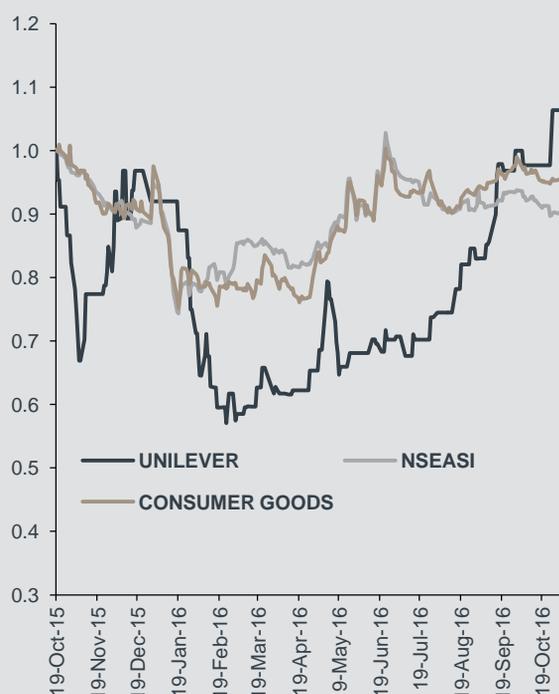
Target Price (N)	15.14
Current Price (N)	48.50
Implied Return (%)	68.78

Company Data

NSE Code	UNILEVER
Bloomberg Code	UNILEVER:NL
Reuters Code	UNILEVER.LG
Sector	CONSUMER GOODS
Market Cap. (N'bn)	22.31
Free Float (%)	183.49

Ratios	9M-16	9M-15	2016FY
Gross margin	29.48%	34.81%	29.62%
Opex margin	23.25%	29.44%	24.26%
EBIT margin	6.24%	5.55%	5.37%
PAT margin	3.14%	0.33%	2.23%
RoAE	31.51%	10.47%	18.13%
EPS (N)	0.41	0.04	0.42

Price movement (UNILEVER vs. Benchmark Indices)



Financial Statement (N'billion).

Income Statement (N'm)	2014a	2015a	2016f	2017f	2018f	Profitability Ratios	2014a	2015a	2016f	2017f	2018f
Revenue	55,754	59,222	68,344	73,812	78,610	Gross prof it margin	36.2%	35.5%	29.6%	29.6%	32.0%
Cost of sales	-35,584	-38,174	-48,102	-51,950	-53,455	EBITDA margin	11.7%	11.4%	8.5%	8.5%	10.9%
Gross profit	20,170	21,048	20,243	21,862	25,155	Operating prof it margin	8.3%	7.8%	5.4%	5.4%	7.7%
Operating expenses	-15,561	-16,485	-16,583	-17,917	-19,090	PBT margin	5.2%	3.0%	2.2%	1.9%	4.7%
Other income/expense	6	78	8	9	10	Net prof it margin	4.3%	2.0%	2.3%	1.3%	3.2%
Finance income	168	302	219	360	380	RoAE	28.7%	15.4%	18.1%	10.8%	26.4%
Finance costs	-1,910	-3,171	-2,360	-2,883	-2,753	RoAA	5.4%	2.5%	2.8%	1.5%	3.6%
Profit before tax	2,873	1,771	1,526	1,431	3,702	RoACE	12.1%	5.3%	6.4%	3.6%	9.8%
Tax expense	-461	-579	51	-444	-1,148						
Profit after tax	2,412	1,192	1,577	987	2,554						
Financial Position (N'm)	2014a	2015a	2016f	2017f	2018f	Liquidity Ratios	2014a	2015a	2016f	2017f	2018f
PPE	24,831	27,369	23,724	25,383	26,784	Working capital (N'm)	-12,800	-13,690	-11,922	-8,334	-6,603
Intangible assets	1,398	1,169	879	941	993	Current ratio	0.6x	0.6x	0.8x	0.8x	0.9x
Other non- current assets	398.2	209	97	104	111	Quick ratio	0.3x	0.4x	0.6x	0.7x	0.7x
Employee loan receivable	128.3	128	93	100	106	Cash ratio	0.0x	0.1x	0.3x	0.4x	0.4x
Assets held for sale	-	171	151	162	172						
Pension scheme surplus	409.7	290	301	323	341	Efficiency Ratios	2014a	2015a	2016f	2017f	2018f
Non-current assets	27,165	29,165	25,094	26,851	28,336	Fixed assets turnover	2.2x	2.2x	2.9x	2.9x	2.9x
Inventories	8,615	6,173	7,339	7,853	8,286	Current assets turnover	3.0x	2.8x	1.7x	1.8x	1.8x
Trade and other receivables	8,544	10,143	14,999	16,048	16,934	Total assets turnover	1.2x	1.2x	1.1x	1.1x	1.1x
Employee loan receivable	77.22	85	62	67	71	Inventory turnover	4.6x	5.2x	7.1x	6.8x	6.6x
Cash and cash equivalents	1,335	4,435	16,831	18,002	18,988	Receivables turnover	6.7x	6.3x	5.4x	4.8x	4.8x
Current assets	18,571	21,008	39,382	42,132	44,451	Payables turnover	2.0x	2.0x	1.8x	1.6x	1.5x
Total Assets	45,736	50,172	64,476	68,983	72,787	Days inventory outstanding	80	71	51	53	55
Trade and other payables	15,111	22,543	32,313	34,259	35,506	Days collection/sales outstanding	55	58	67	77	77
Current tax liabilities	213	160	94	103	107	Days payable outstanding	155	216	245	241	242
Bank overdraft	3,953	4,536	3,179	2,758	3,260	Cash conversion cycle	-20	-87	-127	-111	-111
Loans and borrowings	12,061	7,427	15,690	13,315	12,148						
Deferred income	33	33	28	31	33	Solvency Ratios	2014a	2015a	2016f	2017f	2018f
Current liabilities	31,371	34,698	51,305	50,466	51,054	Debt-to-capital ratio	0.7x	0.6x	0.6x	0.6x	0.6x
Deferred tax liabilities	2,853	3,061	2,496	2,725	2,824	Net debt-to-equity ratio	-2.1x	-1.2x	0.3x	0.4x	0.4x
Retirement benefit obligation	2,757	3,369	2,939	3,207	3,324	Interest coverage	2.4x	1.5x	1.6x	1.4x	2.2x
Long service awards	342	267	273	298	310						
Other employee benefits	44	88	84	92	96	Investment Ratios	2014a	2015a	2016f	2017f	2018f
Deferred income	128	96	-2,627	2,786	4,141	Earnings per share (N)	0.6	0.3	0.4	0.3	0.7
Loans and borrowings	763	591	616	530	541	Dividend per share (N)	0.1	0.1	0.4	0.2	0.6
Total non-current liabilities	6,887	7,472	3,780	9,637	11,236	Payout	15.7%	15.9%	95.0%	95.0%	95.0%
Total Liabilities	38,257	42,169	55,085	60,103	62,290	Dividend yield	0.3%	0.1%	1.0%	0.7%	1.7%
SHF	7,479	8,003	9,391	8,880	10,497						

Source: Company Accounts, Cordros Research

Disclosures

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