

# PZ Cussons Nigeria Plc.

## Less Optimistic Outlook Unchanged

Following the loss after tax suffered at the beginning of the current financial year, PZ's earnings got a reprieve in the second quarter (September-November 2016) after forex losses associated with COGS reduced significantly (-95% q/q). Besides, upward price adjustments positively impacted revenue (+6% y/y), with gross margin reaching record high of 33% over the three months period.

**That said, our less optimistic view of PZ, and indeed the Nigerian consumer environment, is unchanged.** Importantly, we think the recovery prospect of the HPC segment of the consumer goods sector is well behind the Food Products category. Worse still for PZ is that recovery prospect is a lot weaker in the higher margin Household Durables category accounting for 34% of total revenue. **Expectedly, management confirmed to significant decline in volume across the business divisions over H1-16/17 (HPC -20/30% and Electricals -40%) accompanying the 40/60% increase in prices (taken in phases, via absolute increases and product resizing) during the period.** Considering the low visibility on the near end to the ongoing strain on consumer purchasing power (particularly in relation to the potential downward adjustment of the Naira exchange rate), we think PZ will struggle to keep up with management's 10-13% revenue growth forecast over 2017F and 2018F.

**In addition, the possibility of costs doubling from current levels limits the prospect of improvement in margins.** Added to exchange rate fluctuation risk, PZ's input costs face potential pressure from the likely increase in raw materials prices (e.g. petrochemicals and CPOs) with global commodities prices poised to adjust upwards alongside the rally in crude oil prices and a strengthening USD. This, in essence, is reflective of management's guidance to 22% sustainable gross margin, 400bps below the long term average. On the potential impact of FX, we note the build-up in payables over the first half (to N41.5 billion, from end-2016 N25.7 billion) on continued USD scarcity. **Management noted specifically that further devaluation would lead to additional transactional impacts on outstanding USD liabilities and ongoing input costs. The impact on earnings could be a replica of the first quarter (June-August 2016) experience.**

**On the positive, visible success has been achieved with the containment of operating expenses.** Growth was 2% in 2016FY and was only 1% in H1-16/17. That said, PZ will need to improve top-line growth for earnings to fully benefit from the seemingly stable OPEX. **The proportion of OPEX to revenue has increased consistently since 2010 (15.2%), reaching 21% as at end-November 2016.**

The fall in PZ's share price to N12.16, [before the (likely) momentary increase to N14.05 last week], following the release of the Q2 result reflects in part, the paucity of investor confidence on the strength of earnings recovery going forward. **On PE basis, PZ's share (16.6x FPE) is expensive at current price relative to Nigerian Foods Products (10.0x FPE) peers. SELL (TP: N10.41).**

Income Statement (N' bn)	H1-16/17	H1-15/16	Nov-16/17	Q2 y/y	Q2 q/q
Revenue	33.30	30.62	16.55	5.6%	-1%
Cost of sales	-26.77	-22.30	-11.10	-3.2%	-29%
Gross profit	6.53	8.32	5.45	29.9%	404%
Operating expenses	-7.12	-7.00	-3.55	1.0%	-1%
Other income	0.11	0.13	0.05	-20.6%	-15%
Net finance cost	0.06	-0.30	0.06	-141.1%	5848%
Profit before tax	-0.43	1.15	2.01	231.9%	-183%
Taxation	0.14	-0.37	-0.71	179.0%	-184%
Profit after tax	-0.29	0.78	1.30	270.3%	-182%

## SELL

Target Price (N)	10.41
Current Price (N)	14.05
Implied Return (%)	-25.90

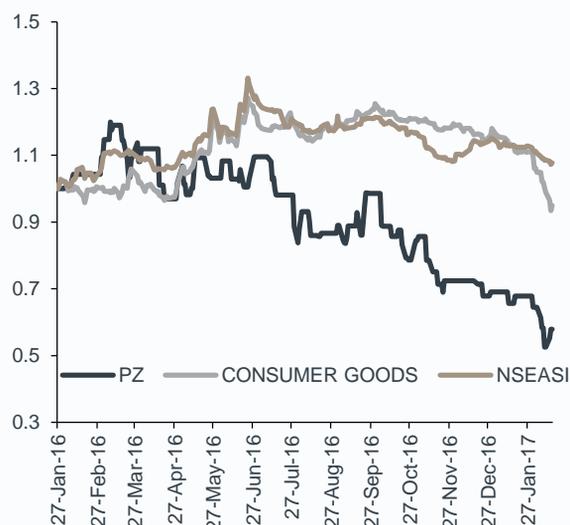
### Company Data

NSE Code	PZ
Bloomberg Code	PZ:NL
Reuters Code	PZ.LG
Sector	CONSUMER GOODS
Market Cap. (N'bn)	55.79
Free Float (%)	26.97

Ratios	H1-17	H1-16	2017E
Gross margin	19.61%	27.17%	22.54%
Opex margin	21.38%	22.86%	20.64%
EBIT margin	-1.45%	4.75%	2.11%
PAT margin	-0.87%	2.54%	1.66%
RoAE	2.58%*	5.37%*	2.81%
EPS (N)	-0.07	0.20	0.30

\*Trailing 12m

### Price movement (PZ vs. Benchmark Indices)



## Financial Statement (N'billion).

Income Statement (N'bn)						Profitability Ratios					
	2014a	2015a	2016a	2017e	2018e		2014a	2015a	2016a	2017e	2018e
Revenue	72.91	73.13	69.53	72.03	74.55	Gross profit margin	26.3%	28.0%	24.9%	22.5%	24.9%
Cost of sales	-53.71	-52.67	-52.21	-55.82	-55.99	EBITDA margin	12.4%	12.3%	8.2%	5.4%	7.5%
Gross profit	19.19	20.45	17.32	16.21	18.56	PBT margin	9.5%	9.0%	4.5%	2.3%	4.5%
Operating expenses	-12.89	-13.80	-14.07	-14.87	-15.66	Net profit margin	7.0%	6.3%	3.1%	1.7%	3.2%
Other income	0.28	0.12	0.29	0.17	0.19	RoAE	11.7%	10.6%	4.9%	2.8%	5.6%
Net finance (cost)/income	0.37	-0.22	-0.39	0.17	0.25	RoAA	7.1%	6.6%	3.0%	1.5%	2.6%
Profit before tax	6.95	6.56	3.15	1.69	3.34						
Tax	-1.87	-1.99	-1.02	-0.50	-0.99	Liquidity Ratios					
<b>Profit after tax</b>	<b>5.08</b>	<b>4.57</b>	<b>2.13</b>	<b>1.19</b>	<b>2.36</b>	Working capital (N' bn)	22.7	22.6	20.8	17.6	18.2
						Current ratio	2.0x	2.2x	1.8x	1.4x	1.4x
						Quick ratio	1.1x	1.1x	1.1x	0.8x	0.8x
						Cash ratio	0.2x	0.1x	0.5x	0.3x	0.3x
Financial Position (N'bn)						Efficiency Ratios					
	2014a	2015a	2016a	2017e	2018e		2014a	2015a	2016a	2017e	2018e
PPE	24.49	25.22	26.50	30.24	30.93	Fixed assets turnover	3.0x	2.9x	2.6x	2.4x	2.4x
<b>Total non-current assets</b>	<b>24.49</b>	<b>25.22</b>	<b>26.50</b>	<b>30.24</b>	<b>30.93</b>	Current assets turnover	1.6x	1.7x	1.5x	1.2x	1.2x
Inventory	20.29	21.01	19.28	24.02	24.56	Total assets turnover	1.0x	1.1x	0.9x	0.8x	0.8x
Debtors	20.68	17.91	15.59	19.57	20.02	Inventory turnover	0.4x	0.4x	0.4x	0.4x	0.4x
Deposit for LCs	1.03	0.92	0.19	2.68	2.75	Receivables turnover	0.3x	0.3x	0.2x	0.2x	0.3x
Cash & bank balances	4.48	2.33	12.87	12.41	12.66	Payables turnover	0.4x	0.4x	0.4x	0.6x	0.7x
<b>Total current assets</b>	<b>46.48</b>	<b>42.17</b>	<b>47.93</b>	<b>58.68</b>	<b>59.98</b>	Days inventory outstanding	130	143	141	142	158
<b>Total assets</b>	<b>70.97</b>	<b>67.39</b>	<b>74.43</b>	<b>88.92</b>	<b>90.91</b>	Days collection/sales outstanding	103	96	88	89	97
Trade creditors	21.90	17.83	25.72	40.03	40.71	Days payable outstanding	149	124	180	262	265
Taxation	1.86	1.67	1.29	0.95	0.97	Cash conversion cycle	84	116	49	-31	-10
<b>Total current liabilities</b>	<b>23.76</b>	<b>19.56</b>	<b>27.10</b>	<b>41.08</b>	<b>41.79</b>	Investment Ratios					
Deferred taxation	4.37	3.90	3.69	5.47	5.56	Earnings per share (N)	1.2	1.0	0.5	0.2	0.5
Provisions	0.11	0.25	0.24	0.53	0.52	Dividend per share (N)	0.8	0.8	0.5	0.2	0.5
<b>Total non-current liabilities</b>	<b>4.48</b>	<b>4.15</b>	<b>3.93</b>	<b>6.00</b>	<b>6.09</b>	Payout	69.1%	79.3%	106.6%	103.1%	90.2%
<b>Total liabilities</b>	<b>28.24</b>	<b>23.72</b>	<b>31.03</b>	<b>47.08</b>	<b>47.88</b>	Dividend yield	2.2%	3.0%	2.3%	2.0%	3.9%
<b>Total Equity</b>	<b>42.73</b>	<b>43.67</b>	<b>43.40</b>	<b>41.84</b>	<b>43.03</b>						

Source: Company Accounts, Cordros Research

# Disclosures

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