

PZ Cussons Nigeria Plc.

Better-Than-Expected Recovery

PZ Cussons Nigeria Plc (PZ) released Q3-16/17 result last week (Friday), showing further improvement in profitability (from the loss reported in the first quarter) with 117% y/y and 46% q/q PAT growth respectively. The PAT (N1.89 billion) beat our estimate (N764.4 million) by a wide margin, primarily on higher-than-expected revenue (20% variance). The relatively lower COS and opex margins also accounted for the variance between the reported PAT and our estimate. By revising Q4-16/17 estimate higher, and accounting for the positive surprise in the third quarter, we have increased 2017 PAT to N3.36 billion (previously N1.19 billion). PZ has implemented aggressive price hikes which, in addition to restoring margin to parity with historical levels, have positioned revenue to grow at the highest since 2009.

But as highlighted in the update on the company's second quarter result, it is unlikely that PZ will replicate 2017 performance next year. Noting the modest outlook for inflation (especially considering the improvement in the FX environment), we expect producers will temper price hikes from the second half of this year and shift focus towards innovative sales and efficiency drive. For PZ, stable prices, amid slow volume recovery, especially in the currently challenged Personal Care and Electrical divisions, signal slower revenue growth from the record level achievable in 2017F. We retain our 3.5% top-line growth estimate for 2018F.

PZ's linkage to FX volatility via imports remains substantial, and save for major improvement in NGN/USD exchange rate or the moderation of raw material input prices, there are no visible internal measures that would lower production costs in the short term. The management has guided to the ongoing backward integration programme to substitute imported CPO with local sourcing as a potential margin enabler, the benefit of which it expects in the medium to long term. In the immediate however, management's guidance is for a sustainable 22% gross margin. Given our prognosis on costs and pricing, we do not expect gross margin to expand further from the 30% average achieved in the last two quarters, and consequently retained our 25% average forecast over the short term. For reference, gross margin dropped to 28% in Q3, from 33% in Q2, suggesting that PZ may have faced additional cost pressure during the period, given that prices were broadly unchanged.

On 15.2x 2017 FPE, PZ is trading at a discount to Bloomberg's SSA and Nigerian peer average (although the sample is very shallow), but at premium to the average of Nigerian Foods Products sector. We roll forward valuation to 2018, revise TP to N14.29 (previously N10.41), and upgrade recommendation to HOLD.

Income Statement (N'bn)	Q1-17	Q2-17	Q3-17	Q4-17e
Revenue	16.75	16.55	23.85	21.94
Cost of sales	-10.97	-10.86	-16.09	-15.48
Forex loss	-4.70	-0.24	-1.17	-0.32
Normalized cost of sales	-15.67	-11.10	-17.26	-15.80
Gross profit	1.08	5.45	6.59	6.14
Operating expenses	-3.57	-3.55	-3.94	-3.73
Other income	0.05	0.06	0.04	0.04
Net finance cost	0.00	0.06	0.09	0.06
Profit before tax	-2.44	2.01	2.78	2.51
Taxation	0.85	-0.71	-0.89	-0.75
Profit after tax	-1.59	1.31	1.89	1.76

Source: Company Account, Cordros Research

HOLD

Target Price (N)	14.29
Current Price (N)	14.00
Implied Return (%)	+2.10

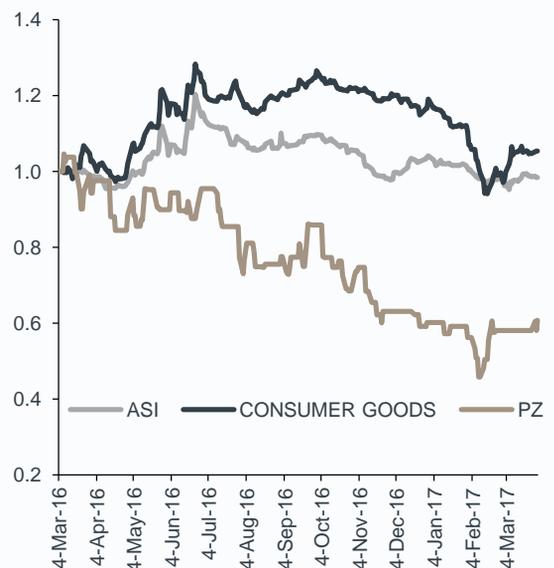
Company Data

NSE Code	PZ
Bloomberg Code	PZ:NL
Reuters Code	PZ.LG
Sector	CONSUMER GOODS
Market Cap. (N'bn)	55.59
Free Float (%)	26.97

Ratios	9M-17	9M-16	2017E
Gross margin	22.96%	26.05%	24.36%
Opex margin	19.36%	21.47%	18.70%
EBIT margin	3.86%	4.99%	5.89%
PAT margin	2.80%	3.25%	4.34%
RoAE	4.82%*	7.64%	7.90%
EPS (N)	0.40	0.41	0.86

*Trailing 12m

Price movement (PZ vs. Benchmark Indices)



Source: NSE, Bloomberg, Cordros Research

Financial Statement (N'billion).

Income Statement						Profitability Ratios					
	2014a	2015a	2016a	2017e	2018e		2014a	2015a	2016a	2017e	2018e
Revenue	72.91	73.13	69.53	79.09	81.86	Gross profit margin	26.3%	28.0%	24.9%	24.4%	25.0%
Cost of sales	-53.71	-52.67	-52.21	-59.83	-61.39	EBITDA margin	12.4%	12.3%	8.2%	8.9%	8.5%
Gross profit	19.19	20.45	17.32	19.26	20.46	PBT margin	9.5%	9.0%	4.5%	6.2%	5.6%
Operating expenses	-12.89	-13.80	-14.07	-14.79	-16.37	Net prof it margin	7.0%	6.3%	3.1%	4.3%	3.9%
Other income	0.28	0.12	0.29	0.19	0.20	RoAE	11.7%	10.6%	4.9%	7.8%	7.3%
Net finance (cost)/income	0.37	-0.22	-0.39	0.21	0.28	RoAA	7.1%	6.6%	3.0%	4.0%	3.3%
Profit before tax	6.95	6.56	3.15	4.87	4.58						
Tax	-1.87	-1.99	-1.02	-1.44	-1.35	Liquidity Ratios					
Profit after tax	5.08	4.57	2.13	3.43	3.23	Working capital (N'bn)	22.7	22.6	20.8	17.7	17.4
						Current ratio	2.0x	2.2x	1.8x	1.4x	1.4x
Financial Position						Efficiency Ratios					
	2014a	2015a	2016a	2017e	2018e		2014a	2015a	2016a	2017e	2018e
PPE	24.49	25.22	26.50	33.21	33.96	Quick ratio	1.1x	1.1x	1.1x	0.8x	0.8x
Total non-current assets	24.49	25.22	26.50	33.21	33.96	Cash ratio	0.2x	0.1x	0.5x	0.3x	0.3x
Inventory	20.29	21.01	19.28	26.37	26.97	Fixed assets turnover	3.0x	2.9x	2.6x	2.4x	2.4x
Debtors	20.68	17.91	15.59	21.49	21.98	Current assets turnover	1.6x	1.7x	1.5x	1.2x	1.2x
Deposit for LCs	1.03	0.92	0.19	2.94	3.01	Total assets turnover	1.0x	1.1x	0.9x	0.8x	0.8x
Cash & bank balances	4.48	2.33	12.87	13.63	13.90	Inventory turnover	0.4x	0.4x	0.4x	0.4x	0.4x
Total current assets	46.48	42.17	47.93	64.43	65.87	Receivables turnover	0.3x	0.3x	0.2x	0.2x	0.3x
Total Assets	70.97	67.39	74.43	97.64	99.83	Payables turnover	0.4x	0.4x	0.4x	0.6x	0.8x
Trade creditors	21.90	17.83	25.72	45.53	47.16	Days inventory outstanding	130	143	141	139	159
Taxation	1.86	1.67	1.29	1.08	1.12	Days collection/sales outstanding	103	96	88	86	97
Total current liabilities	23.76	19.56	27.10	46.74	48.42	Days payable outstanding	149	124	180	278	280
Deferred taxation	4.37	3.90	3.69	6.22	6.45	Cash conversion cycle	84	116	49	-53	-25
Provisions	0.11	0.25	0.24	0.61	0.61						
Total non-current liabilities	4.48	4.15	3.93	6.83	7.05	Investment Ratios					
Total liabilities	28.24	23.72	31.03	53.56	55.47		2014a	2015a	2016a	2017e	2018e
Total Equity	42.73	43.67	43.40	44.08	44.35	Earnings per share (N)	1.2	1.0	0.5	0.8	0.7
						Dividend per share (N)	0.8	0.8	0.5	0.7	0.7
						Payout	69.1%	79.3%	106.6%	86.7%	87.2%
						Dividend yield	2.2%	3.0%	2.3%	3.8%	3.6%

Source: Company Accounts, Cordros Research

Disclosures

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