

Guinness Nigeria Plc.

First Glance: Q3-17; Investors Unmoved By Marked Improvement in PAT

Late yesterday, GUINNESS released Q3-17 results, and surprised with a record gross margin (54.71%) recovery that was by far the biggest contributor to the company's first quarterly profit in exactly one year. Also supporting the PAT of N2.1 billion reported during the period was a 53.6% y/y increase in revenue.

The realized gross margin (GM) was higher 988 bps y/y and 3010 bps q/q. And while the q/q improvement in GM is (1) consistent with the recovery observed across the recently announced consumer goods Jan-Mar 2017 margins (except CADBURY's) and (2) appears flattered by a very low base, the recovery to level exceeding both the previous year's, and historical average, is an obvious outlier.

While noting the recent price increases which are helping with margins, we highlight the following productivity programs, via which DIAGEO (the parent company of GUINNESS) said most of the margin headwinds in Nigeria are being mitigated: there was specific mention of the (1) right-sizing of brewery workforce, (2) optimization of spans of control and reduced layers, (3) improvement of the efficiency of breweries through a manufacturing excellence program, (4) improvement of bottling efficiency by 10%, (5) reduction of waste and energy and water usage, (6) reduction of logistic costs at double-digit, and (7) continued expansion of supplier base to secure the best prices. DIAGEO said its Nigerian operation has also delivered cost savings from the implementation of zero-based budgeting system for indirect spends, as well as marketing efficiencies from negotiating better media and point of sale costs. We understand GUINNESS is currently sourcing around 70% of third-party raw materials locally, and medium term goal remains at 80%. Management also said its packaging is approximately 100% locally sourced, albeit not immune to embedded FX impact.

The high double-digit y/y revenue growth mainly reflects the impact of higher mean price, following the increases implemented in the last nine months. Management said its unit price increase has been conservative, considering the weak demand environment, as well as competition. In addition, the y/y revenue reflects GUINNESS' renewed commitment to RTM (especially at the retail end), higher export sales (224% y/y), broader products portfolio (e.g spirits and the launch of Guinness Herbs), and the resilience of value brands (Satzbrau and Dubic Malt).

On the negative however, operating expenses (opex) increased by 43.2% y/y and 25.2% q/q, with the margin of 41% being the highest under the current financial year. The significant increase in marketing expenses (390%) and depreciation (24% y/y) underpinned the increase in opex.

Also worth highlighting is the 125.7% y/y increase in finance charges, comprising N435 million loss (Nil in Q3-16) on foreign exchange transactions and N2.1 billion (87.4% y/y and 12.4% q/q) as interest expense on loans and borrowings and overdraft facilities. Both GUINNESS' gross (N1 billion) and net debt (N 2.1 billion) increased from end-December values. Shareholders recently approved the request for rights issue to enable GUINNESS optimize its capital structure by deleveraging its balance sheet, potentially reducing its finance costs.

Notwithstanding the marked shift in the latest result, GUINNESS' stock closed flat in today's trading. The stock is down 5% since releasing H1-17 result and 24% YtD, with investors, perhaps still focused on the (1) previous disappointing results and (2) pending rights issue. We maintain HOLD recommendation on the stock. Our estimates are under review.

HOLD

Target Price (N)*	56.72
Current Price (N)	60.00
Implied Return (%)	-5.48

Company Data

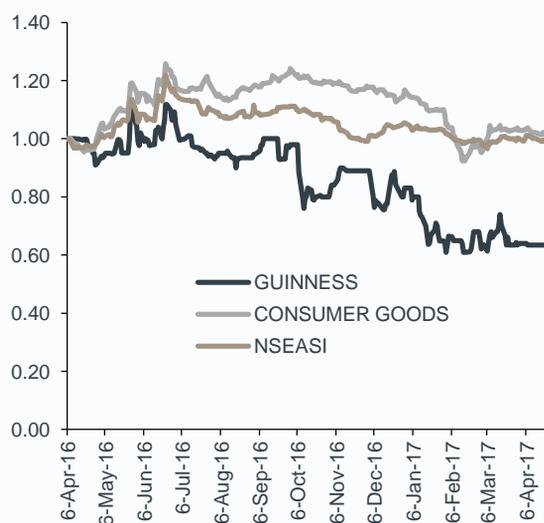
NSE Code	GUINNESS
Bloomberg Code	GUINNESS:NL
Reuters Code	GUINNES.LG
Sector	CONSUMER GOODS
Market Cap. (N'bn)	130.35
Free Float (%)	45.61

Ratios	Q1-2017	Q1-2016	2016FY
Gross margin	54.71%	44.83%	41.00%
Opex margin	41.28%	44.26%	37.16%
EBIT margin	14.08%	1.16%	4.33%
PAT margin	6.95%	-1.56%	-1.98%
RoAE	0.98%**	12.62%**	-1.56%
EPS (N)	1.40	-0.20	-1.34

*Under Review

**Trailing 12m

Price movement (GUINNESS vs. Benchmark Indices)



Source: NSE, Bloomberg, Cordros Research

Financial Statement (N'billion).

Income Statement (N'bn)						Profitability Ratios					
	2015a	2016a	2017f	2018f	2019f	2015a	2016a	2017f	2018f	2019f	
Turnover	118.50	101.97	126.60	139.26	151.79	Gross profit margin	47.17%	41.00%	28.19%	29.19%	30.19%
Cost of sales	-62.60	-60.16	-90.92	-98.62	-105.97	EBITDA margin	22.79%	13.08%	9.04%	10.06%	11.10%
Gross profit	55.89	41.81	35.68	40.64	45.82	Operating profit margin	13.22%	4.33%	1.76%	2.81%	3.87%
M&D expenses	-27.11	-24.89	-22.52	-24.68	-26.80	PBT margin	9.11%	-2.30%	-3.99%	1.92%	2.96%
Administrative expenses	-13.83	-13.01	-11.60	-12.71	-13.81	Net profit margin	6.58%	-1.98%	-3.99%	1.36%	2.09%
Other income/expenses	0.72	0.50	0.67	0.67	0.67	RoAE	16.69%	-4.48%	-13.76%	3.75%	4.73%
Operating profit/loss	15.67	4.42	2.23	3.92	5.88	RoAA	6.12%	-1.56%	-3.42%	1.17%	1.89%
Interest expenses	-5.58	-7.95	-9.12	-2.09	-2.28						
Interest income	0.71	1.19	1.84	0.85	0.89	Liquidity Ratios					
Profit before tax	10.80	-2.35	-5.05	2.68	4.49	Working capital (N'bn)	-12.59	-19.24	-21.97	-11.49	-17.63
Taxation	-3.00	0.33	0.00	-0.79	-1.32	Current ratio	0.73x	0.71x	0.75x	0.86x	0.80x
Profit after tax	7.79	-2.02	-5.05	1.89	3.17	Quick ratio	0.49x	0.52x	0.49x	0.55x	0.52x
						Cash ratio	0.13x	0.09x	0.13x	0.14x	0.13x
Financial Position (N'bn)						Efficiency Ratios					
	2015a	2016a	2017f	2018f	2019f	2015a	2016a	2017f	2018f	2019f	
Property, plant and equipment	87.75	87.23	89.41	92.58	96.40	Fixed assets turnover	1.35x	1.17x	1.42x	1.50x	1.57x
Intangible assets	0.94	1.71	1.58	1.65	1.74	Current assets turnover	3.54x	2.13x	1.89x	2.01x	2.11x
Prepayments	0.01	0.18	0.22	0.25	0.28	Total assets turnover	0.97x	0.74x	0.80x	0.85x	0.89x
Other receivables	0.02	-	0.02	0.03	0.05	Inventory turnover	5.17x	5.06x	4.95x	4.08x	4.22x
Total non-current assets	88.74	89.12	91.23	94.52	98.46	Receivables turnover	6.83x	4.85x	4.43x	4.47x	4.69x
Inventories	10.75	13.02	23.74	24.59	25.62	Payables turnover	2.01x	1.74x	2.08x	1.67x	1.46x
Trade and other receivables	15.50	26.51	30.64	31.74	33.06	Days inventory outstanding	71	72	74	89	86
Prepayments	1.45	2.49	1.27	1.33	1.40	Days collection/sales outstanding	53	75	82	82	78
Cash and cash equivalents	5.80	5.84	11.37	11.66	12.02	Days payable outstanding	90	161	123	117	114
Total current assets	33.51	47.87	67.02	69.32	72.09	Cash conversion cycle	34	-14	33	54	51
Total assets	122.25	136.99	158.25	163.83	170.55	Investment Ratios					
Loans and borrowings	12.25	14.03	18.63	-	-		2015a	2016a	2017f	2018f	2019f
Non current financial liabilities	-	-	-	-	-	Earnings per share (N)	5.18	-1.34	-3.36	0.87	1.46
Employee benefits	2.21	1.25	1.67	1.26	1.41	Dividend per share (N)	3.20	3.20	3.20	3.20	3.20
Deferred tax liabilities	13.34	12.94	17.18	12.91	14.35	Payout	62%	-239%	-95%	368%	220%
Total non-current liabilities	27.80	28.22	37.48	14.17	15.76	Dividend yield	2.66%	3.85%	4.92%	4.92%	4.92%
Bank overdraft	1.47	2.94	3.91	3.80	4.11						
Current tax liabilities	2.28	0.59	0.79	0.60	0.68						
Dividend Payable	3.90	3.86	5.13	3.87	4.30						
Loans and borrowings	6.97	22.20	29.46	3.80	4.11						
Trade and other payables	31.48	37.53	49.70	68.74	76.51						
Total current liabilities	46.10	67.11	88.99	80.80	89.72						
Total liabilities	73.91	95.33	126.46	94.98	105.48						
Share Capital	0.75	0.75	0.75	1.09	1.09						
Share premium	8.96	8.96	8.96	48.63	48.63						
Share based payment reserve	0.02	-	-	-	-						
Retained earnings	38.61	31.95	22.07	19.14	15.36						
Total equity	48.34	41.66	31.79	68.86	65.07						

Source: Company Accounts, Cordros Research

Disclosures

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