

PZ Cussons Nigeria Plc.

Earnings to Recover After a Bumpy Start to 2018

Guidance from our recent discussion with the management of PZ is for flat to slight earnings growth in 2018F. The consumer environment is expected to remain challenging and competition intense. Outlook for prices is dovish (there has been a marginal price cut this year for Electrical goods, wherein increase was higher last year), yet volumes are unlikely to recover strongly. Dollar liquidity has improved, outlook is positive, and likewise, the expected impact on business performance.

From the loss in Q1 (discussed in our first glance released on Tuesday), we expect PZ will return to profit in the coming quarters, and close 2018F with N3.52 billion net profit (vs. N3.69 billion in 2017FY). The assumptions driving our forecast are (1) continued revenue growth, (2) modest margin recovery, and (3) higher opex (ratio of revenue to increase by 70 bps) and effective tax rate (to increase by 448 bps). **After contracting in 2018F, we expect earnings to grow from 2019F and reach the N5 billion mark (last attained in 2014FY) in 2021F.**

Latest economic data (rising PMI, consumer confidence, and business expectation) suggest that the pressure that Nigerian consumers face may be over-exaggerated. With prices largely stable and economic activities improving, we think consumers are actually better-off now, compared to a year ago. For PZ, we expect earlier recovery in the Home Care division (volume was down by only 3% in 2017FY), given the essential nature and affordability of products in that category. A number of initiatives, including distribution expansion and new product launches, will hasten recovery in the Personal Care division (where volume was down by 15% in 2017FY). Although recovery in the Electrical division is expected to lag the others, both the price cut and improved dollar liquidity are expected to impact positively on sales. **For hindsight, the 16% q/q contraction in PZ's Q1-18 revenue is by far less than the 37% average q/q decline recorded during the same period, since 2012 (within available data).**

We think the 24% gross margin guidance given by management, consistent with our forecast, is attainable. We refer to subdued pressure from the external environment (as relates to forex) and internal efficiency measures derivable from the recently launched SAP project as enabling drivers. **That said, margin recovery will remain modest even after 2018F on continued consumers sensitivity to price points.**

The stock has accumulated 67% YtD, supported by the same positive investor sentiment that has driven both the broader and consumer goods indices up by 31.6% and 28.3% respectively YtD. Following the upward review of our estimates, we have increased our 2018F TP slightly higher to N14.86 (previously N14.26). **While we remain constructive of PZ, we believe the stock has outrun the level supportive of its fundamentals. SELL.**

Income Statement (N'bn)	Q1-18a	Q2-18e	Q3-18e	Q4-18e
Revenue	18.90	20.79	24.95	23.70
Cost of sales	-14.70	-15.59	-18.71	-17.77
Gross profit	4.20	5.20	6.24	5.92
Operating expenses	-4.14	-4.55	-4.24	-4.03
Other income	0.03	0.06	0.06	0.06
Finance income	0.08	0.10	0.10	0.10
Finance expense	-0.35	0.01	0.01	0.01
Profit before tax	-0.18	0.82	2.17	2.07
Taxation	0.06	-0.23	-0.61	-0.58
Profit after tax	-0.12	0.59	1.56	1.49

Source: Company Account, Cordros Research estimates

SELL

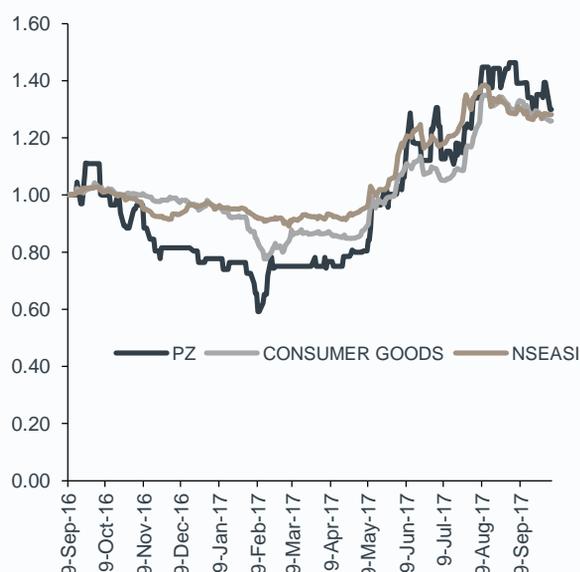
Target Price (N)	14.86
Current Price (N)	24.23
Implied Return (%)	-38.66

Company Data

NSE Code	PZ
Bloomberg Code	PZ:NL
Reuters Code	PZ.LG
Sector	CONSUMER GOODS
Market Cap. (N'bn)	96.20
Free Float (%)	26.73

Ratios	Q1-18	Q1-17	2018F
Gross margin (LFL)	22.22%	6.45%	24.40%
Opex margin	21.90%	21.32%	19.20%
EBIT margin (LFL)	0.09%	-2.43%	5.45%
PAT margin	-0.33%	-8.57%	3.98%
EPS (N)	-0.03	-0.40	0.89

Price movement (PZ vs. Benchmark Indices)



Source: NSE, Bloomberg, Cordros Research

Financial Statement (N'billion).

Income Statement (N'bn)						Profitability Ratios					
	2016a	2017a	2018e	2019e	2020e		2016a	2017a	2018e	2019e	2020e
Revenue	69.53	79.63	88.33	97.17	107.37	Gross profit margin	24.9%	24.0%	24.4%	24.5%	24.6%
Cost of sales	-52.21	-60.48	-66.78	-73.36	-80.95	EBITDA margin	8.2%	8.7%	8.5%	8.7%	8.9%
Gross profit	17.32	19.15	21.56	23.81	26.42	PBT margin	4.5%	6.0%	5.5%	5.8%	6.0%
Operating expenses	-14.07	-14.73	-16.96	-18.56	-20.40	Net profit margin	3.1%	4.6%	4.0%	4.2%	4.3%
Other income	0.29	0.20	0.22	0.25	0.29	RoAE	4.9%	8.3%	7.7%	8.5%	9.6%
Net finance (cost)/income	-0.39	0.20	0.06	0.10	0.13	RoAA	3.0%	4.5%	3.7%	3.9%	4.1%
Profit before tax	3.15	4.81	4.88	5.60	6.44						
Tax	-1.02	-1.12	-1.36	-1.56	-1.79	Liquidity Ratios					
Profit after tax	2.13	3.69	3.52	4.04	4.64	Working capital (N'bn)	20.8	18.2	15.8	14.5	13.5
						Current ratio	1.8x	1.4x	1.3x	1.3x	1.2x
Financial Position (N'bn)						Quick ratio	1.1x	0.8x	0.7x	0.6x	0.6x
PPE	26.50	28.51	33.39	36.74	39.73	Cash ratio	0.5x	0.2x	0.2x	0.2x	0.1x
Intangible assets	-	1.02	1.33	1.46	1.58						
Total non-current assets	26.50	29.53	34.72	38.20	41.31	Efficiency Ratios					
Inventories	19.28	28.71	31.11	34.23	37.02	Fixed assets turnover	2.6x	2.8x	2.6x	2.6x	2.7x
Trade and other receivables	15.59	17.22	21.61	23.78	25.72	Current assets turnover	1.5x	1.3x	1.4x	1.4x	1.4x
Deposit for imports	0.19	6.60	2.96	3.27	3.55	Total assets turnover	0.9x	0.9x	0.9x	0.9x	0.9x
Cash & cash equivalents	12.87	8.02	7.74	8.48	9.12	Inventory turnover	0.4x	0.4x	0.4x	0.4x	0.4x
Total current assets	47.93	60.56	63.43	69.76	75.40	Receivables turnover	0.2x	0.2x	0.2x	0.2x	0.2x
Total Assets	74.43	90.09	98.15	107.96	116.71	Payables turnover	0.4x	0.5x	0.6x	0.6x	0.7x
Bank overdraft	-	-	1.49	1.49	1.49	Days inventory outstanding	141	145	163	163	161
Trade and other payables	25.72	39.72	42.53	49.64	55.70	Days collection/sales outstanding	88	75	80	85	84
Current taxation payable	1.29	2.56	3.54	4.14	4.65	Days payable outstanding	180	240	232	247	251
Warranty provisions	0.09	0.09	0.03	0.04	0.05	Cash conversion cycle	49	-20	11	1	-6
Total current liabilities	27.10	42.37	47.59	55.30	61.89						
Deferred taxation	3.69	2.40	2.97	3.47	3.90	Investment Ratios					
Warranty provisions	0.24	0.18	0.92	1.30	1.61	Earnings per share (N)	0.54	0.93	0.89	1.02	1.17
Total non-current liabilities	3.93	2.58	3.89	4.77	5.51	Dividend per share (N)	0.50	0.50	0.71	0.81	0.94
Total liabilities	31.03	44.95	51.48	60.07	67.40	Payout	93.2%	53.9%	80.0%	80.0%	80.0%
Total Equity	43.40	45.14	46.67	47.90	49.31	Dividend yield	2.3%	2.7%	2.9%	3.4%	3.9%

Source: Company Accounts, Cordros Research

Disclosures

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