

Nestle Nigeria Plc.

Slight upward revision to 2018-2019E earnings; SELL rating maintained

At our revised TP of NGN851.92 (previously NGN843.54), we maintain **SELL** rating on NESTLE's stock at the current market price of NGN1,380. The q/q sales revenue contraction reported in the seasonally-supportive Q4 is a volume pressure worthy of note. Besides, gross margin (-219 bps y/y and -107 bps q/q in Q4-17) appears less likely to improve materially in the absence of further price increases. That said, we note the potential stimulus to 2018E earnings from significantly lower finance charges and lower opex-to-sales ratio. On net, we revise 2018E net profit estimate 5% higher to NGN49.3 billion, equating to NGN62 dividend per share, and 4% yield on today's price.

Our latest 2018 sales revenue estimate of NGN268.6 billion (10% growth vs. 2017FY) is lower by 4% compared to the previous estimate. We based our estimate entirely on volume growth (driven by the Food segment), as we maintain our view that the odds are high against price increase in 2018. While NESTLE's market leading status accords the group some influence over pricing, we believe the implications to market share is high in today's resurgent competitive environment, amidst little recovering consumption expenditures.

We retain our gross margin estimate of 42% (vs. 41% in 2017FY) for 2018E. While noting the weakness experienced in Q4-17 as dampening growth outlook, we have based our benign growth estimate on moderating commodities price inflation and stable naira exchange rate outlook. Likewise, we estimate EBIT margin to expand modestly to 23% (vs. 22.8% in 2017FY) on slightly conservative opex growth expectation (13% in 2018F vs. 27% previously).

With NGN42.7 billion loans repaid (96% were intercompany loans), gross debt at the end of 2017F was NGN24.2 billion. New long term intercompany loan (NGN5.5 billion) was drawn also in 2017FY. Gross borrowing is currently split into 74% USD intercompany loans (vs. 92% in 2016FY) and 26% secured NGN borrowings (vs. 8% in 2016FY). The split was 70:30 during the pre naira devaluation and acute FX challenge period of 2011-2014FY. We estimate finance charge to reduce by more than 14x in 2018E on less geared balance sheet and stable naira outlook.

Ratios	31-Dec-17	Q4-2017	Q3-2017	Q2-2017	Q1-2017
Gross margin	41.31%	42.42%	43.49%	40.9%	38.4%
OPEX margin	18.50%	21.01%	17.61%	18.7%	16.8%
EBIT margin	22.81%	21.41%	25.88%	22.2%	21.6%
PBT margin	19.18%	20.96%	15.82%	16.7%	23.4%
PAT margin	13.81%	18.24%	10.16%	13.5%	13.7%
CoGS margin	58.69%	57.58%	56.51%	59.1%	61.6%
Interest cover	3.69x	56.90x	2.2x	2.3x	8.6x
Tax rate	27.98%	13.00%	35.81%	19.5%	41.5%
EBITDA margin	25.47%	24.40%	28.47%	24.76%	24.09%

SELL

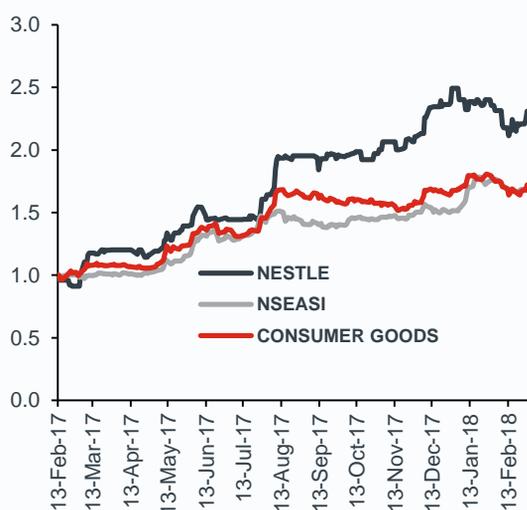
Target Price (NGN)	851.92
Current Price (NGN)	1,380.00
Implied Return (%)	-38.27

Company Data

NSE Code	NESTLE
Bloomberg Code	NESTLE:NL
Reuters Code	NESTLE.LG
Sector	CONSUMER GOODS
Market Cap. (NGN'bn)	1,109.72
Free Float (%)	36.25

Ratios	Q4-2017	Q4-2016	2017FY
Gross margin	42.42%	44.62%	41.31%
Opex margin	21.01%	20.12%	18.50%
EBITDA margin	24.40%	27.00%	25.47%
EBIT margin	21.41%	24.50%	22.81%
PAT margin	18.24%	14.19%	13.81%
EPS (N)	13.55	9.39	42.55

Price movement (NESTLE vs. Benchmark Indices)



Source: NSE, Bloomberg, Cordros research

Financial Statement (NGN'million).

Income Statement	2014a	2015a	2016a	2017a	2018e	2019e	Profitability Ratios	2014a	2015a	2016a	2017a	2018e	2019e
Turnover	143,329	151,272	181,911	244,151	268,567	296,766	Gross profit margin	42.7%	44.5%	41.4%	41.3%	42.0%	42.0%
Cost of sales	-82,099	-83,926	-106,583	-143,280	-155,769	-172,109	EBITDA margin	24.4%	26.2%	24.3%	25.5%	25.7%	25.7%
Gross profit	61,230	67,346	75,328	100,871	112,798	124,657	Operating profit margin	20.4%	22.3%	21.0%	22.8%	23.0%	23.0%
Gross opex	-32,030	-33,598	-37,114	-45,173	-51,028	-56,400	PBT margin	17.1%	19.4%	11.8%	19.2%	24.5%	24.8%
EBIT	29,200	33,747	38,213	55,698	61,770	68,256	Net profit margin	15.5%	15.7%	4.4%	13.8%	18.3%	18.6%
Interest income	552	444	4,199	6,239	6,133	7,516	RoAE	58.1%	64.2%	23.0%	89.0%	98.7%	97.0%
Interest exp	-5,306	-4,869	-20,864	-15,109	-2,236	-2,236	RoAA	20.8%	21.1%	5.5%	21.3%	31.3%	31.6%
PBT	24,446	29,322	21,548	46,829	65,667	73,537	RoACE	32.6%	34.8%	10.6%	44.8%	66.5%	68.0%
Tax	-2,210	-5,586	-13,623	-13,105	-16,417	-18,384							
PAT	22,236	23,737	7,925	33,724	49,251	55,153							
Financial Position	2014a	2015a	2016a	2017a	2018e	2019e	Liquidity Ratios	2014a	2015a	2016a	2017a	2018e	2019e
PPE	67,515	69,148	70,172	72,378	75,534	77,811	Working capital (NGN'mn)	-7,249	-11,017	-23,297	-7,176	3,435	8,164
Intangible assets	-	-	-	-	-	-	Current ratio	0.8x	0.8x	0.8x	0.9x	1.0x	1.1x
LT receivables	1,158	1,352	1,678	1,921	2,197	2,368	Quick ratio	0.6x	0.6x	0.6x	0.6x	0.7x	0.8x
Non-current assets	68,673	70,500	71,850	74,299	77,731	80,179	Cash ratio	0.1x	0.2x	0.4x	0.2x	0.3x	0.3x
Inventories	10,956	10,814	20,638	23,910	27,339	29,473							
Trade and other receivables	22,331	24,446	24,035	31,430	35,937	38,742	Efficiency Ratios	2014a	2015a	2016a	2017a	2018e	2019e
Prepayments	398	525	1,712	2,025	2,316	2,496	Fixed assets turnover	2.1x	2.2x	2.6x	3.4x	3.6x	3.8x
Cash and cash equivalents	3,705	12,930	51,351	15,139	24,531	30,065	Current assets turnover	3.8x	3.1x	1.9x	3.4x	3.0x	2.9x
Current assets	37,389	48,715	97,736	72,505	90,123	100,776	Total assets turnover	1.4x	1.3x	1.1x	1.7x	1.6x	1.6x
Total Assets	106,062	119,215	169,586	146,804	167,854	180,955	Inventory turnover	7.9x	7.7x	6.8x	6.4x	6.1x	6.1x
Trade and other payables	26,657	36,662	64,662	49,056	54,340	58,807	Receivables turnover	7.1x	6.5x	7.5x	8.8x	8.0x	7.9x
Bank overdraft	1,238	305	155	3,714	3,714	3,714	Payables turnover	2.9x	2.7x	2.1x	2.5x	3.0x	3.0x
Short term borrowings	12,730	17,109	40,130	10,913	10,913	10,913	Days inventory outstanding	46	47	54	57	60	60
Current tax liabilities	3,479	5,040	15,490	15,099	16,725	18,100	Days collection outstanding	51	56	49	41	46	46
Provisions	535	616	597	899	996	1,078	Days payable outstanding	119	159	221	125	127	125
Current liabilities	44,638	59,732	121,033	79,680	86,688	92,612	Cash conversion cycle	-21	-56	-119	-27	-22	-19
Long term borrowings	18,386	12,530	10,384	9,565	9,565	9,565							
Deferred tax liabilities	5,271	6,564	5,186	10,405	14,132	17,282	Solvency Ratios	2014a	2015a	2016a	2017a	2018e	2019e
Employee benefits	1,828	2,382	2,104	2,276	2,521	2,728	Debt-to-capital ratio	0.5x	0.4x	0.6x	0.4x	0.3x	0.2x
Non-current liabilities	25,484	21,476	17,674	22,245	26,218	29,575	Net debt-to-equity ratio	0.8x	0.4x	0.0x	0.2x	-0.1x	-0.2x
Total Liabilities	70,122	81,208	138,708	101,926	112,906	122,188	Interest coverage	5.5x	6.9x	1.8x	3.7x	27.6x	30.5x
SHF	35,940	38,007	30,878	44,878	54,948	58,767							
							Investment Ratios	2014a	2015a	2016a	2017a	2018e	2019e
							Earnings per share (NGN)	28.05	29.95	10.00	42.55	62.13	69.58
							Dividend per share (NGN)	27.50	29.35	9.80	41.69	60.89	68.19
							Dividend Payout	98%	98%	98%	98%	98%	98%
							Dividend yield	2.7%	3.4%	1.2%	3.0%	4.3%	4.9%
							PE	36.1x	28.7x	81.0x	36.6x	22.2x	19.8x
							EV/EBITDA	23.7x	17.6x	14.5x	18.0x	16.0x	14.4x

Source: Company Accounts, Cordros Research

Disclosures

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SELL (UNDERWEIGHT) - Over the next twelve months, we expect the stock to be more than 10% below the current market price.

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