

PZ Cussons Nigeria Plc.

Parent company confirms challenging H2!

Update: PZ Cussons Plc (PZC), the parent company of PZ Nigeria Plc (PZN), stated in a trading update released yesterday, that **it now expects its profit for the year ending May 2018 to fall short of expectations**. Trading conditions in Nigeria and the UK were unfavourable in H1, and apparently, the usual peak season uplift has not occurred to the expected level thus far in H2.

In our note published on 20th February 2018, we estimated that PZN's 2018E net profit will be lower by 7% vs. 2017FY. **But the tone of the parent company's communication of this earnings warning has raised concern for us that the decline might be bigger. The guidance provided by PZC is for 18-23% decline in Group 2018E PBT vs. 2017FY.**

There's actually sales pressure in "Naija": The management of the Nigerian subsidiary actually confirmed to us in February that the operating environment has been more challenging than expected since December 2017, and could impact the group's performance in the traditionally strong second half, and indeed, 2018F. Whilst consumer's discretionary income remains under pressure with subdued buying levels, local competition has increased, and are constraining volumes. Besides, cross border trade (accounting for 5% of revenue) has been majorly constrained by some sort of currency devaluation in Sudan. The Personal Care (-5% y/y volume in H1) and Electrical (-20% y/y volume in H1) divisions remain under pressure, while Home Care (+7% y/y volume in H1) has been resilient. In essence, the 23% y/y revenue growth in H1-18 was entirely price-driven. Revenue growth should moderate to 8% in H2, by our estimate.

Including on margins: In yesterday's update, the parent company mentioned that intense competition is resulting in lower prices and margins, but "noticeably in the milk category". Overall, for us, we should mention that PZN's gross (24%) and EBIT (3%) margins are currently below their 2013-2016 averages (c.27% and 8% respectively), and, while we see little downside pressure from current levels, we also do not expect them to return to historical levels soon.

But there could be light in the end: In light of the aforementioned, the Group said it has initiated some remedial actions in Nigeria, including a (1) reassessment of the structure of its operating model to further reduce the overhead base, (2) review of product costs with a focus on areas such as packaging reduction, and (3) re-prioritisation of the new product pipeline to focus on fewer, bigger projects requiring lower levels of complexity. Clearly executed, we believe these efficiency measures will be potentially positive for margins.

Valuation: We have a SELL recommendation for PZN (NGN15.19 TP), with YtD return of 12%. On our numbers, PZN is trading at 2018F P/E and EV/EBITDA multiples of 26.7x and 10.5x respectively, relative to MEA peer averages of 22x and 15.6x respectively.

SELL

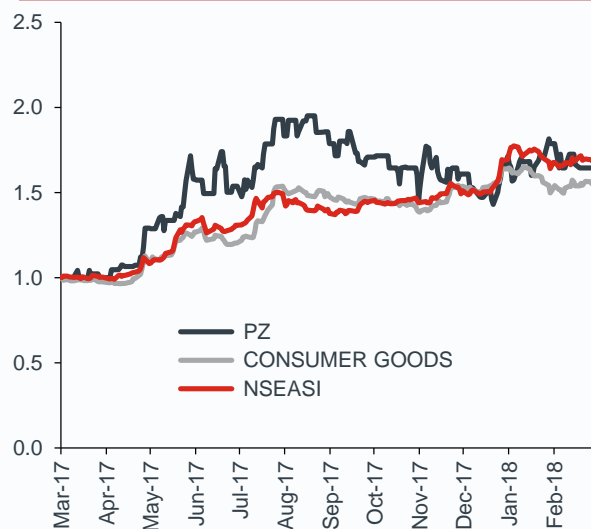
Target Price (NGN)	15.19
Current Price (NGN)	23.00
Implied Return (%)	-33.97

Company Data

NSE Code	PZ
Bloomberg Code	PZ:NL
Reuters Code	PZ.LG
Sector	CONSUMER GOODS
Market Cap. (NGN'bn)	91.32
Free Float (%)	26.73

Ratios	Q2-18	Q2-17	2018F
Gross margin (LFL)	24.99%	32.92%	24.40%
Opex margin	19.38%	21.45%	18.49%
EBIT margin (LFL)	5.75%	11.77%	5.96%
PAT margin	3.21%	7.84%	3.64%
EPS (NGN)	0.16	0.27	0.84

Price movement (PZ vs. Benchmark Indices)



Source: NSE, Bloomberg, Cordros Research

Financial Statement (NGN'billion).

Income Statement (NGN'bn)							Profitability Ratios						
	2015a	2016a	2017a	2018e	2019e	2020e		2015a	2016a	2017a	2018e	2019e	2020e
Revenue	73.13	69.53	79.63	91.31	99.98	109.98	Gross profit margin	28.0%	24.9%	24.0%	24.4%	24.5%	24.6%
Cost of sales	-52.67	-52.21	-60.48	-69.01	-75.46	-82.90	EBITDA margin	12.1%	8.2%	8.7%	8.8%	9.0%	9.2%
Gross profit	20.45	17.32	19.15	22.30	24.52	27.08	EBIT margin	9.3%	5.1%	5.8%	6.0%	6.2%	6.4%
Operating expenses	-13.80	-14.07	-14.73	-16.98	-18.49	-20.23	PBT margin	9.0%	4.5%	6.0%	5.4%	6.2%	6.4%
Other income	0.12	0.29	0.20	0.12	0.14	0.16	Net profit margin	6.3%	3.1%	4.6%	3.75%	4.3%	4.5%
Net finance (cost)/income	-0.22	-0.39	0.20	-0.52	0.03	0.03	RoAE	10.6%	4.9%	8.3%	7.5%	9.1%	10.0%
Profit before tax	6.56	3.15	4.81	4.92	6.20	7.05	RoAA	6.6%	3.0%	4.5%	3.8%	4.5%	4.6%
Tax	-1.99	-1.02	-1.12	-1.49	-1.88	-2.14							
Profit after tax	4.57	2.13	3.69	3.43	4.31	4.91	Liquidity Ratios						
							Working capital (NGN'bn)	22.6	20.8	18.2	17.0	15.9	14.4
Financial Position (NGN'bn)							Current ratio	2.2x	1.8x	1.4x	1.4x	1.3x	1.2x
PPE	25.22	26.50	28.51	31.48	34.47	37.92	Quick ratio	1.1x	1.1x	0.8x	0.7x	0.7x	0.6x
Intangible assets	-	-	1.02	1.13	1.24	1.36	Cash ratio	0.1x	0.5x	0.2x	0.2x	0.2x	0.1x
Total non-current assets	25.22	26.50	29.53	32.61	35.71	39.28	Efficiency Ratios						
Inventories	21.01	19.28	28.71	28.96	31.71	34.89	Fixed assets turnover	2.9x	2.6x	2.8x	2.9x	2.9x	2.9x
Trade and other receivables	17.91	15.59	17.22	20.53	22.48	24.72	Current assets turnover	1.7x	1.5x	1.3x	1.5x	1.5x	1.5x
Deposit for imports	0.92	0.19	6.60	3.16	3.46	3.80	Total assets turnover	1.1x	0.9x	0.9x	1.0x	1.0x	1.0x
Cash & cash equivalents	2.33	12.87	8.02	6.97	7.63	8.40	Inventory turnover	0.4x	0.4x	0.4x	0.4x	0.4x	0.4x
Total current assets	42.17	47.93	60.56	59.62	65.28	71.81	Receivables turnover	0.3x	0.2x	0.2x	0.2x	0.2x	0.2x
Total Assets	67.39	74.43	90.09	92.23	100.99	111.09	Payables turnover	0.4x	0.4x	0.5x	0.6x	0.6x	0.6x
Bank overdraft	-	-	-	-	-	-	Days inventory outstanding	143	141	145	153	147	147
Trade and other payables	17.83	25.72	39.72	40.28	46.62	54.24	Days collection/sales outstanding	96	88	75	75	78	78
Current taxation payable	1.67	1.29	2.56	2.28	2.64	3.08	Days payable outstanding	124	180	240	213	225	239
Warranty provisions	0.06	0.09	0.09	0.10	0.11	0.13	Cash conversion cycle	116	49	-20	15	0	-14
Total current liabilities	19.56	27.10	42.37	42.65	49.37	57.45	Investment Ratios						
Deferred taxation	3.90	3.69	2.40	2.89	3.34	3.89	2015a	2016a	2017a	2018e	2019e	2020e	
Warranty provisions	0.25	0.24	0.18	0.11	0.13	0.15	Earnings per share (NGN)	1.15	0.54	0.93	0.86	1.09	1.24
Total non-current liabilities	4.15	3.93	2.58	3.00	3.47	4.04	Dividend per share (NGN)	0.81	0.50	0.50	0.69	0.87	0.99
Total liabilities	23.72	31.03	44.95	45.65	52.84	61.48	Payout	70.4%	93.2%	53.9%	80.0%	80.0%	80.0%
Total Equity	43.67	43.40	45.14	46.58	48.15	49.61	Dividend yield	3.0%	2.3%	2.7%	3.0%	3.8%	4.3%
							PE	23.4x	40.4x	20.1x	26.7x	21.2x	18.6x

Source: Company Accounts, Cordros Research

Disclosures

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