Unilever Nigeria Plc.

Q1-18: Better-than-expected revenue and lower opex margin offset weaker gross margin

Update: Last week, UNILEVER published Q1-18 result showing net profit grew by 81% y/y, 2% ahead of our estimate (and 21% ahead of consensus). Revenue came in better-than-expected, operating expense was well-contained, and finance cost (though higher than we expected) was significantly lower, courtesy of the borrowings repaid last year. On the negative, however, gross margin was well-below expectation, after the positive surprises of the last three quarters of 2017FY.

Surprising bullish revenue: The revenue growth of 16% y/y (+19% q/q) was ahead of the 10% we estimated, but in line with consensus. The growth was even across the business segments, with Food growing by 16% y/y and HPC by 17% y/y. There were price increases up until Q2-17, the impact of which we believe is somewhat reflected in the latest revenue. We should also reiterate the impact of volume on revenue, reflecting the (1) campaigns and promotional activities that took place during the quarter (for *Knoor Chicken* seasoning and *Close-Up* toothpaste), (2) increased activities of distributors following the slack in Q4-17, and (3) introduction of new products, notably (from our routine checks), *Sunlight* bar soap and 70g and 25g *Sunlight* detergents. We raise 2018E revenue growth estimate to 13% (previously 7.5%), based on the (1) stronger-than-expected Q1 growth and (2) impact of the 5% increase in the price of *Lipton* tea implemented this month. Risks to our estimate are (1) the increasingly competitive environment, particularly in the HPC segment, possibly resulting in (2) softer products prices in the course of the year.

Sharp q/q fall in gross margin; no worries for now: Given the stability of both selling prices and the naira exchange rate during the period, we should mention that production costs, and consequently gross margin (72 bps y/y and 704 bps q/q to c.28%), may have been pressured by the rising price of petroleum products (which form key inputs in UNILEVER's production process). Notwithstanding the low outturn, we retain our gross margin estimate of 32% for 2018E, consistent with those achieved in the last three quarters of 2017FY. Recall that gross margin in Q1-17 (28%) was the lowest in all quarters of last year, before the improvement seen in the subsequent quarters.

EBIT grew 28% y/y (-c.7% q/q) while the margin increased by 124 bps y/y. This bigger growth in EBIT, over gross profit (13.5% y/y), was helped by opex, which only grew by 2% y/y (-3% q/q) while the proportion to revenue was 199 bps lower on y/y basis. UNILEVER's opex has grown by only a marginal 3% average in the last four years (slightly ahead of PZ's 5%) and this has been constructive to earnings. Management had mentioned during H1-17 call that it is controlling opex by (1) eliminating wastes, (2) validation of all expenses (ZBB), and (3) discriminating between expenses. We have forecast opex to grow by c.8% in 2018E (vs. 9% in 2017FY), suggesting we expect higher spending especially during the off-peak periods in Q2 and Q3.

Healthier balance sheet: Total borrowings reduced to NGN457 million, from NGN674 million as at end-December 2017, with gross debt-to-equity now at 0.6%, vs. 191% a year ago. The finance cost of NGN98.6 million reported was surprisingly higher – despite reduced borrowings – than the NGN69 million we estimated for the full year. We have consequently raised finance cost estimate for 2018E to NGN150 million. Cash remained strong at NGN47.5 billion, delivering interest income of NGN494 million (89% via bank deposits) that far exceeded the NGN130 million we estimated for the quarter. We retain our finance income estimate for 2018E, as the reported amount (which we do not expect will be delivered in the remaining quarters) is consistent with the NGN1.2 billion we modeled for the full year.

Valuation: We maintain our SELL recommendation but increase target price to NGN32.78 (previously NGN30.47) even as we slightly revise our estimates. On our numbers, UNILEVER currently trades on FY18E P/E and EV/EBITDA multiples of 27.9x and 12.6x respectively.

SELL

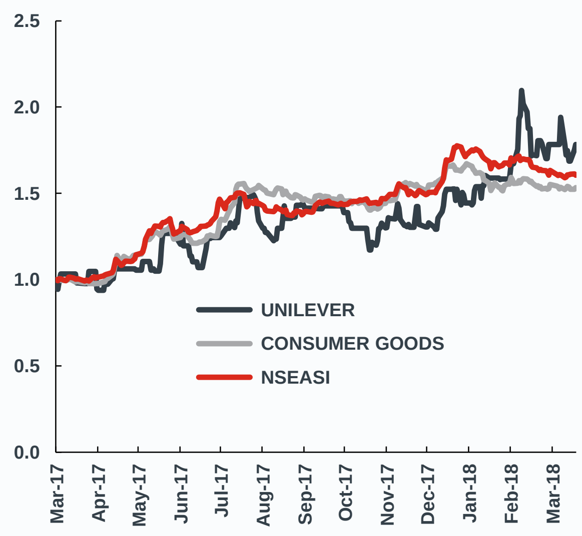
Target Price (NGN)	32.78
Current Price (NGN)	53.00
Implied Return (%)	-38.14

Company Data	
NSE Code	UNILEVER
Bloomberg Code	UNILEVER:NL
Reuters Code	UNILEVER.LG
Sector	CONSUMER GOODS
Market Cap. (NGN'bn)	304.49
Free Float (%)	32.11

Ratios	Q1-2018	Q1-2017	2017FY
Gross margin	27.660%	28.38%	31.89%
Opex margin	14.00%	15.98%	17.60%
EBITDA margin	16.45%	15.21%	19.04%
EBIT margin	13.66%	12.42%	14.27%
PAT margin	11.23%	7.23%	8.21%
RoAE*	18.99%	32.53%	17.01%
EPS (NGN)	0.50	0.28	1.78

*12 months

Price movement (UNILEVER vs. Benchmark Indices)



Source: NSE, Bloomberg, Cordros research

Summary of Quarterly Results.

Income Statement (N'bn)	31-Mar-18	31-Mar-17	y/y % Δ	q/q	Cordros Q1-18e	Q4-17	Q3-17	Q2-17	Q1-17
Revenue	**25.82**	22.17	*16.44%*	*19.29%*	**24.39**	21.64	24.02	22.93	22.17
Cost of sales	**18.68**	15.88	*17.62%*	*32.16%*	**-16.50**	14.13	16.50	15.32	15.88
Gross profit	**7.14**	6.29	*13.47%*	*-4.92%*	**7.90**	7.51	7.53	7.61	6.29
Operating expenses	**3.61**	3.54	*1.98%*	*-2.82%*	**-4.18**	3.72	4.74	3.97	3.54
Other income	**0.00**	0.01	*-100.00%*	*-100.00%*	**0.00**	-0.02	0.00	-0.01	0.01
EBIT	**3.53**	2.75	*28.06%*	*-6.53%*	**3.72**	3.77	2.78	3.64	2.75
Finance income	**0.49**	0.08	*529.74%*	*-52.48%*	**0.13**	1.04	0.25	0.23	0.15
Financial charges	**0.10**	0.65	*-84.92%*	*-77.09%*	**-0.04**	0.43	1.25	1.00	0.72
Profit before tax	**3.92**	2.18	*79.97%*	*-10.51%*	**3.81**	4.38	1.78	2.86	2.18
Taxation	**1.02**	0.58	*77.50%*	*-41.82%*	**-1.11**	1.76	0.63	0.79	0.58
Profit after tax	**2.90**	1.60	*80.85%*	*10.51%*	**2.70**	2.62	1.15	2.07	1.60

Ratios	31-Mar-18	31-Mar-17	Q4-17	Q3-17	Q2-17	Q1-17
Gross margin	***27.66%***	*28.38%*	*34.70%*	*31.32%*	*33.20%*	*28.38%*
OPEX margin	***14.00%***	*15.98%*	*17.18%*	*19.75%*	*17.31%*	*15.98%*
EBITDA margin	***16.45%***	*15.21%*	*28.51%*	*14.36%*	*18.71%*	*15.21%*
EBIT margin	***13.66%***	*12.42%*	*17.44%*	*11.58%*	*15.87%*	*12.42%*
PBT margin	***15.20%***	*9.83%*	*20.26%*	*7.41%*	*12.49%*	*9.83%*
PAT margin	***11.23%***	*7.23%*	*12.12%*	*4.78%*	*9.04%*	*7.23%*
COS margin	***72.34%***	*71.62%*	*65.30%*	*68.68%*	*66.80%*	*71.62%*
Interest cover	***35.81x***	*4.22x*	*8.8x*	*2.2x*	*3.6x*	*3.8x*
Tax rate	***26.10%***	*26.47%*	*40.15%*	*35.39%*	*27.59%*	*26.47%*
EPS (N)	***0.50***	*0.28*	*0.46*	*0.20*	*0.36*	*0.28*

Source: Company Accounts, Cordros Research estimates

Financial Statement (NGN'million).

Income Statement	2014a	2015a	2016a	2017a	2018e	2019e
Revenue	55,754	59,222	69,777	90,771	103,025	111,267
Cost of sales	-35,584	-38,174	-49,481	-61,828	-70,165	-75,767
Gross profit	20,170	21,048	20,296	28,943	32,861	35,501
Operating expenses	-15,561	-16,485	-14,615	-15,976	-18,143	-19,605
Other icome/expense	6	78	124	-18	21	22
Finance income	168	302	1,028	1,668	1,221	1,302
Finance costs	-1,910	-3,171	-2,726	-3,410	-150	-69
Profit before tax	2,873	1,771	4,106	11,207	15,810	17,151
Tax expense	-461	-579	-1,035	-3,757	-4,901	-5,317
Profit after tax	**2,412**	**1,192**	**3,072**	**7,450**	**10,909**	**11,834**

Financial Position	2014a	2015a	2016a	2017a	2018e	2019e
PPE	24,831	27,369	29,272	29,881	34,357	36,611
Intangible assets	1,398	1,169	940	329	379	403
Other non- current assets	398.2	208.8	140.2	79.5	91	97
Employee loan receivable	128.3	128.0	111.7	705.9	150	160
Retirement benefit surplus	410	290	485	130	812	865
Non-current assets	**27,165**	**29,165**	**30,949**	**31,126**	**35,788**	**38,136**
Inventories	8,615	6,173	9,878	11,479	13,198	14,064
Trade and other receivables	8,544	10,143	18,946	27,621	31,759	33,843
Employee loan receivable	77	85	73	79	91	97
Assets held for sale	-	171	171	-	-	-
Derivative assets	-	-	-	286	286	286
Cash and cash equivalents	1,335	4,435	12,474	50,494	58,101	61,931
Current assets	**18,571**	**21,008**	**41,543**	**89,959**	**103,435**	**110,220**
Total Assets	**45,736**	**50,172**	**72,491**	**121,084**	**139,224**	**148,357**
Trade and other payables	15,111	22,543	32,477	33,409	41,031	46,812
Current tax liabilities	213	160	503	2,799	3,425	3,900
Bank overdraft	3,953	4,536	-	-	-	-
Loans and borrowings	12,061	7,427	20,501	455	455	455
Deferred income	33	33	33	33	40	46
Current liabilities	**31,371**	**34,698**	**53,513**	**36,695**	**44,951**	**51,212**
Deferred tax liabilities	2,853	3,061	3,942	4,485	5,488	6,248
Retirement benefit obligation	2,757	3,369	2,613	3,454	4,227	4,813
Long service awards	342	267	181	206	252	287
Other employee benefits	44	88	74	86	105	120
Deferred income	128	96	63	30	37	42
Loans and borrowings	763	591	414	220	220	220
Total non-current liabilities	**6,887**	**7,472**	**7,288**	**8,481**	**10,328**	**11,729**
Total Liabilities	**38,257**	**42,169**	**60,801**	**45,176**	**55,279**	**62,941**
SHF	**7,479**	**8,003**	**11,690**	**75,908**	**83,945**	**85,416**

Profitability Ratios	2014a	2015a	2016a	2017a	2018e	2019e
Gross profit margin	36.2%	35.5%	29.1%	31.9%	31.9%	31.9%
EBITDA margin	12.1%	11.4%	12.0%	19.0%	19.1%	19.1%
Operating profit margin	8.3%	7.8%	8.3%	14.3%	14.3%	14.3%
PBT margin	5.2%	3.0%	5.9%	12.3%	15.3%	15.4%
Net profit margin	4.3%	2.0%	4.4%	8.2%	10.6%	10.6%
RoAE	28.7%	15.4%	31.2%	17.0%	13.6%	14.0%
RoAA	5.4%	2.5%	5.0%	7.7%	8.4%	8.2%
RoACE	12.1%	5.3%	11.6%	13.6%	13.5%	13.9%

Liquidity Ratios	2014a	2015a	2016a	2017a	2018e	2019e
Working capital (NGN'm)	-12,800	-13,690	-11,971	53,263	58,484	59,009
Current ratio	0.6x	0.6x	0.8x	2.5x	2.3x	2.2x
Quick ratio	0.3x	0.4x	0.6x	2.1x	2.0x	1.9x
Cash ratio	0.0x	0.1x	0.2x	1.4x	1.3x	1.2x

Efficiency Ratios	2014a	2015a	2016a	2017a	2018e	2019e
Fixed assets turnover	2.2x	2.2x	2.4x	3.0x	3.0x	3.0x
Current assets turnover	3.0x	2.8x	1.7x	1.0x	1.0x	1.0x
Total assets turnover	1.2x	1.2x	1.0x	0.7x	0.7x	0.8x
Inventory turnover	4.6x	5.2x	6.2x	5.8x	5.7x	5.6x
Receivables turnover	6.7x	6.3x	4.8x	3.9x	3.5x	3.4x
Payables turnover	2.0x	2.0x	1.8x	1.9x	1.9x	1.7x
Days inventory outstanding	80	71	59	63	64	66
Days collection/sales outstanding	55	58	76	94	105	108
Days payable outstanding	155	216	240	197	213	226
Cash conversion cycle	-20	-87	-104	-41	-44	-52

Solvency Ratios	2014a	2015a	2016a	2017a	2018e	2019e
Debt-to-capital	0.7x	0.6x	0.6x	0.0x	0.0x	0.0x
Debt-to-equity	199.4%	162.2%	212.4%	1.5%	0.8%	0.8%
Net debt/EBITDA	2.3x	1.2x	1.0x	-2.9x	-2.9x	-2.9x
Net debt-to-equity	2.1x	1.0x	0.7x	-0.7x	-0.7x	-0.7x
Interest coverage	2.4x	1.5x	2.1x	3.8x	98.2x	232.1x

Investment Ratios	2014a	2015a	2016a	2017a	2018e	2019e
Earnings per share (NGN)	0.64	0.32	0.81	1.78	1.90	2.06
Dividend per share (NGN)	0.10	0.05	0.10	0.71	1.80	1.96
Payout	15.7%	15.9%	12.3%	40.1%	95.0%	95.0%
Dividend yield	0.3%	0.1%	0.3%	1.7%	3.4%	3.7%
P/E	56.1x	120.0x	43.1x	23.0x	27.9x	25.7x
EV/EBITDA	22.3x	22.3x	16.9x	6.7x	12.6x	11.5x

Source: Company Accounts, Cordros Research

Disclosures.

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