



## NIGERIA | EQUITIES | BREWERIES | NIGERIAN BREWERIES PLC

### Excise Duty to Weigh on Macroeconomic Improvement

We maintain our SELL recommendation on Nigerian Breweries Plc given the 3% downside implied by our N111.8 fair value on the stock. Following the release of its Q1 2018 results, we forecast Nigerian Breweries Plc (NB) FY 2018 P/E multiple at 28.4x, lower than our FY 2018 P/E multiple of 33.0x forecast for Guinness Nigeria Plc (GN) but higher than 26.9x which is the average in the industry. The premium attached to GN's FY 2018E P/E may be due to the company recovering from a weak base.

We opine that top line performance in the near term may continue to be limited given the potential introduction of the new excise tax in June 2018 as well as the heightened competition in the brewery space as a result of the growing national presence of International Breweries Plc. In addition, while the improving macro environment and downward trend in inflation may be supportive of consumer sentiments, we expect revenue to be driven by value and mainstream brands such as Life, Goldberg, Turbo King and Williams in the near term.

While our forecast for performance in 2018 is reflective of the above, we highlight the potential positive impact of the improving macroeconomic environment as implied by the recently released Q1 2018 GDP figures and the potential review of minimum wage, which may drive volume growth in H2 2018. We also expect product innovation, as the company newly introduced Stella and Tiger beer into the market, to increase its product portfolio, cost efficiency as evident in its recent results, as well as a more favourable FX environment to continue to drive FY 2018 performance.

Share data	
Bloomberg	NB NL
Reuters	NB NG
Industry	BREWERIES
Rating -New	SELL
Rating - Old	SELL
Price (25 May 2018)	N115.4
Price Target - New	N111.8
Price Target - Old	N129.9
Upside/Downside	-3.2%
Market Cap. (N'million)	922,842.5
Avg. Daily Value Traded (N'million)	560.9
Shares Outstanding (Million)	7,996.9
Free Float	47.6%

### Price Movement Relative to NSE-ASI



### Historic Performance against NSE-ASI

Performance Over	1M	3M	6M	12M	YTD
Absolute	-1.90%	0.65%	-4.85%	-12.17%	-8.30%
Relative to NSE-ASI	-0.95%	4.99%	-15.27%	-56.14%	-14.01%

Source: Bloomberg, Reuters, Investment One Research

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Financials and valuation metrics (YE 31 Dec)	2016A	2017A	2018E	2019E
Sales	313,743	344,563	354,899	377,968
PBT	39,675	46,630	49,849	58,279
PBT margin	12.6%	13.5%	14.0%	15.4%
Basic EPS	3.58	4.13	4.49	5.25
EPS growth (y/y)	-25.3%	15.3%	8.6%	16.9%
P/E	42.5x	35.7x	26.3x	22.4x
EV/EBIT (x)	22.5x	19.0x	14.3x	12.5x
Dividend yield (%)	3.5%	3.1%	3.9%	4.5%

Source: Company financials, Investment One Research



Volume to support top line in the near term.

Nonetheless, we remain conservatively optimistic in our view of top line performance in 2018 through to 2019, which we forecast to average 4%. Unlike GN, which recorded a 15.0% y/y improvement in topline to N34.9billion in Q3 2018, NB's recently released Q1 2018 results revealed a decline in topline due to weak demand, as highlighted by Heineken the parent company.

We point out that this is similar to what was observed in the company's Q4 2017 results. The top line performance combined with the 37.02% y/y spike in net finance cost more than outweighed the 139bps y/y expansion in gross profit margin leading to a 12.56% y/y and 10.88% y/y decline in PBT and PAT to N15.25billion and N10.20billion respectively.

Given our view of the company's inability to take significant price increases through 2018 due to the potential implementation of the excise tax in June 2018, in order to remain competitive, we expect top line to see support from election spending, product innovation and the potential review of minimum wage in Q3 2018. Although the Heineken brand has returned to growth in 2017 as highlighted by management, we may continue to see value and mainstream brands, with lower contribution to margin, be the major driver of sales in the medium term.

Key Ratio Performance



Source: Company Financials, Investment One Research



### Gradual margin recovery on price increase

Gross profit margin increased by 139bps y/y to 45.82% in Q1 2018, the highest since Q2 2016. This compares favourably with Guinness Nigeria Plc with a Q3 2018 margin of 33.19%. We attribute this to management's focus on its cost leadership programme to achieve efficiency and optimization of its resources. Given the feat achieved in Q1 2018 and the continued stability in the FX environment, which we expect to bode well for input cost, we forecast gross profit margin to average 44.00% over FY 2018-2019, 234bps higher compared to FY 2017 levels. We also expect stable commodity prices estimated to grow at an average of 2.1% through 2019 by World bank to be supportive of gross profit margin.

### Stringent Opex/Sales ratio

To remain competitive and support bottom line performance, NB has continued to maintain opex/sales ratio around the 27% levels since Q1 2013 compared to 30% levels for GN.

Also, the company's plans to improve consumer value engagement, increase market penetration and ensure a balance in the management of input cost and prices consumers are willing to pay for its products as highlighted by management may be further supportive of PBT performance.

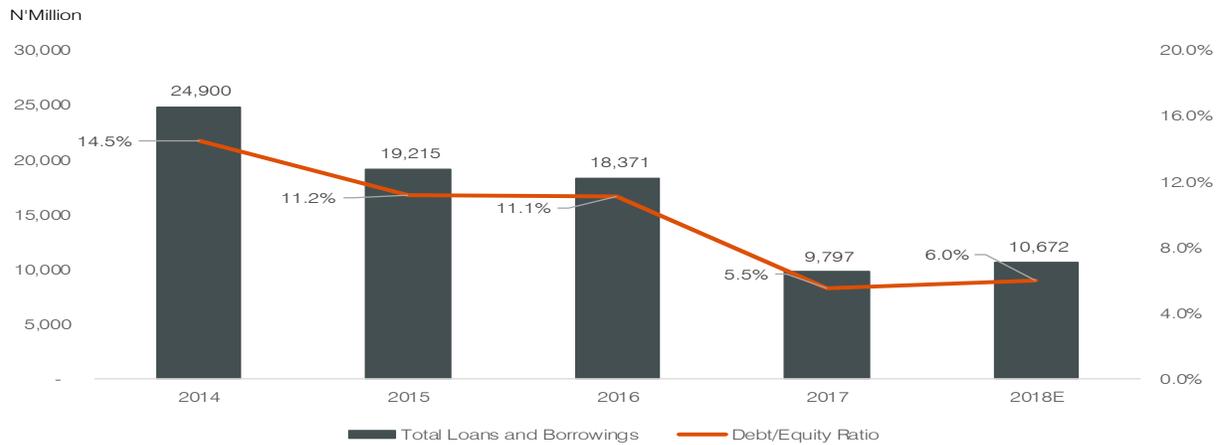
Consequently, we forecast a 16.8% y/y and 15.7% y/y growth in PBT in 2018 and 2019 respectively driven by our 4%/y/y average growth in sales, 210bps y/y contraction in opex/sales and 34.1% y/y average reduction in net finance cost through 2019.

### Massive trade payables continue to support lower debt

NB continues to record impressive cash conversion ratio relative to peers majorly due to larger trade payables. Compared to GN with a cash conversion ratio of 96% in FY 2017, NB recorded a cash conversion ratio of 79% in FY 2017. We also believe that the reliance on short term debt through the issuance of Commercial Papers to fund working capital needs combined with the longer trade days count is also supportive of its lower debt to equity of 5.5% in FY 2017 with a 6.0% estimate in FY 2018, compared to GN who had a debt to equity of 97.6% in FY 2017 and an estimate of 15.0% in FY 2018 according to our forecast. Consequently, NB's interest coverage printed at 5.4x in FY 2017 with a 6.5x forecast for FY 2018 due to the relatively lower debt to equity ratio compared to GN 1.0x in FY 2017 and 2.5x in FY 2018 according to our estimate.



Total Loans & Borrowings and Debt to Equity Ratio Performance



Source: Company Financials, Investment One Research

Risk to our outlook

Given our forecast of Nigerian Breweries Plc performance in 2018 through 2019, we underline tougher than expected competition from international breweries, inability of the company to keep opex/sales low at current levels, higher than expected commodity prices as forecasted by World Bank and escalated political risk beyond expectation as downside risks to our outlook.



### Summary of Financials (N millions). Year End 31 Dec

Income Statement	2016A	2017A	2018E	2019E
Turnover	313,743	344,563	354,899	377,968
Gross profit	135,525	143,549	156,156	170,086
Total opex	-83,237	-88,647	-92,731	-98,000
Other income	616	2,219	631	639
EBIT	52,903	57,121	64,056	72,725
EBITDA	82,645	91,248	96,217	104,627
Net finance cost	-13,229	-10,491	-14,207	-14,446
PBT	39,675	46,630	49,849	58,279
Taxation	-11,258	-13,581	-13,958	-16,318
PAT	28,417	33,049	35,891	41,961
Balance Sheet	2016A	2017A	2018E	2019E
Fixed assets	191,182	195,230	195,370	197,521
Other non-current assets	101,256	99,355	97,978	96,577
Non current assets	292,587	294,735	293,497	294,248
Stocks	31,245	42,729	40,864	42,743
Trade debtors	19,974	20,384	24,356	24,037
Cash and bank balances	12,156	15,867	27,508	35,152
Current assets	74,559	87,493	101,612	110,702
Total assets	367,146	382,228	395,109	404,950
Borrowings	17,000	9,326	10,201	10,866
Deferred tax	29,877	26,667	26,667	26,667
Non current Liabilities	56,978	49,203	50,077	50,743
Trade and other trade payables	111,184	126,621	138,536	147,601
Taxation	19,024	19,606	19,606	19,606
Dividend payable	12,676	8,029	8,029	8,029
Current liabilities	144,255	154,727	166,642	175,707
Shareholders funds	165,914	178,298	178,298	178,298

Source: Company financials, Investment One Research



### Summary of Financials (N millions). Year End 31 Dec

Cash Flow Statement	2016A	2017A	2018E	2019E
Profit pre WC. chngs.	74,591	88,038	90,552	101,164
Working capital changes	23,515	15,754	9,379	7,609
Tax paid	-15,049	-15,588	-13,958	-16,318
Operating cash flow	70,101	72,051	85,973	92,455
Capex	-19,213	-32,122	-30,865	-34,053
Cash flow from investing activities	-18,809	-32,065	-30,670	-33,715
Net cash flow after investment	51,291	39,986	54,079	57,308
Cash flow from financing activities	-25,951	-35,875	-43,662	-51,095
Net increase/decrease in cash	25,340	4,110	11,641	7,644
Cash balance b/d	-14,108	11,286	15,396	27,037
Cash balance c/d	11,232	15,396	27,037	34,681
Profitability Ratios	2016A	2017A	2018E	2019E
Gross margin	43.2%	41.7%	44.0%	45.0%
EBITDA margin	26.3%	26.5%	27.1%	27.7%
EBIT margin	16.9%	16.6%	18.0%	19.2%
PBT margin	12.6%	13.5%	14.0%	15.4%
Net profit margin	9.1%	9.6%	10.1%	11.1%
ROCE av.	18.8%	20.0%	20.8%	23.0%
ROCE / WACC	1.2x	1.4x	1.0x	1.8x
Opex/sales	26.5%	25.7%	26.1%	25.9%
Activity Ratios	2016A	2017A	2018E	2019E
Inventory turnover	6.0x	5.4x	4.8x	5.0x
Days of inventory on hand	61.1	67.2	76.8	73.4
Receivables turnover	25.6x	26.6x	18.9x	15.6x
Days of sales outstanding	14.2	13.7	19.3	23.4
Payables turnover	1.8x	1.8x	1.5x	1.5x
No. of payable days	198.0	204.2	245.8	248.9
Cash conversion cycle	-122.7	-123.4	-149.8	-152.2
Working capital turnover	-3.7x	-4.2x	-4.0x	-3.9x
Fixed asset turnover	1.1x	1.2x	1.2x	1.3x
Capital employed turnover	1.5x	1.6x	1.7x	1.9x
Total asset turnover	0.9x	0.9x	0.9x	0.9x
Liquidity & Solvency Ratios	2016A	2017A	2018E	2019E
Current ratio	0.52	0.57	0.61	0.63
Quick ratio	0.30	0.29	0.36	0.39
Cash ratio	0.14	0.15	0.21	0.24
Debt-to-capital ratio	10.0%	5.2%	5.6%	6.0%
Debt-to-equity ratio	11.1%	5.5%	6.0%	6.4%
Financial leverage	2.2x	2.1x	2.2x	2.3x



### Valuation

Our N111.80 price target is derived using a discounted cash flow (DCF) model over the 2018-2027 period. We assume that sales growth reaches a terminal value of 12.0% in 2027 while EBIT improves to 22% by 2027 from our 2018 estimates. Our WACC is 15.9%, assuming 13.0% risk free rate, 1.0 beta, 7.1% after tax cost of debt and 5.0% equity risk premium.

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### Recommendations and Movements in Price Target

Date	Price (N)	Old Price Target (N)	New Price Target (N)	Old Recommendation	New Recommendation
24-July-15	129.0	114.5	114.5	SELL	SELL
1-Sep-15	126.9	114.5	99.8	SELL	SELL
2-Feb-16	100.0	99.8	91.4	SELL	SELL
16-Jun-16	141.76	91.4	95.2	SELL	SELL
1-Feb-17	139.80	95.2	90.2	SELL	SELL
9-Jun-17	156.50	90.2	129.9	SELL	SELL
23-May-18	123.7	129.9	111.8	SELL	SELL

### Investment One Equity Research Recommendation Definitions

#### BUY

The stock is considered to be fundamentally strong with the potential to deliver returns in excess of 15% above the current price based on the analyst's target price.

#### HOLD

The stock is considered to be fairly priced, with potential to deliver returns between 5% and 15% above the current price based on the analyst's target price.

#### SELL

The stock is considered to be overvalued with weakening fundamentals, with returns expected to be below 5% based on the current price and the analyst's target price.



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