Nigerian Breweries Plc.

A notably weak Q2-18 earnings; HOLD

Update: NB reported 33.1% y/y decline in Q2-18 EPS, impacted by sales and gross margin declines, as well as higher effective tax rate, which offset a significantly lower net finance cost. Both the achieved revenue and net profit trailed our estimates for the three months period by 6% and 39% respectively. And annualized, the H1-18 EPS of NGN2.31 is 8% behind consensus estimate for 2018E.

Competition, seasonality, and price hike impact revenue: The reported Q2-18 revenue was less than Q2-17 by 0.03% and trailed our estimate by a wider margin. NB has now recorded y/y decline in revenue for three quarters in a row. At current run-rate (-5% in H1-18), and considering sales is typically slower in H2, we no longer expect NB to grow revenue in the 2018 fiscal year. Our revised revenue estimate of NGN337.7 billion is lower by 2% (vs. +7% previously) compared to 2017FY. And we also expect a downward revision of consensus' estimate of NGN362.2 billion (+5% vs. 2017FY) following the latest result. Heineken (NB's parent) had guided in May to declining sales volume in Nigeria. On one hand, we believe unit volume was affected by Ramadan-related decline in beer consumption. But more broadly, we reiterate that NB's market share is under pressure from the growing presence of competition – INTBREW (not covered) specifically – in the West and East markets. We should also mention the price hike in early June as possibly impacting volume.

A concerned margins contraction: Q2-18 gross margin came in at 42.4%, down by about 300 bps y/y and q/q, and at strong variance to the 46.4% rate we expected. Our assumption is that NB may have absorbed the additional costs associated with the newly approved excise duties for alcoholic beverages, effective June. For instance, we are aware that NB increased the prices of beer earlier in June (***Star Radler, Life, Gulder, and Goldberg***), but rolled some back by the end of the month. While we expect NB will eventually pass on the extra costs to consumers, we expect it will be measured and staggered, amidst increasing competition for market share (for instance, we understand INTBREW retained the prices of its product after the new excise duties took effect). Consequently, we revise our gross margin estimate for 2018E 150 bps lower to 41.5%, while retaining estimates over 2019-2020E at 43% average.

The Q2-18 result shows EBITDA and EBIT were lower by 20% y/y and 31% y/y respectively, with 24% (-606 bps) and 16% (-686 bps) margins. Both opex and the margin were higher than our estimates. Overall, we forecast EBITDA and EBIT to contract by 6% each in 2018E, with 25.2% (vs. 26.5% in 2017FY) and 15.8% (vs. 16.6% in 2017FY) margins respectively.

Significantly lower net finance costs: Net finance cost of NGN1.7 billion was recorded in Q2-18, 53% lower y/y, comprising 356% y/y increase in finance income and 48% reduction in finance costs. On finance costs, we note that the balance of borrowings is little changed compared to Q1-18 (+4%) and doubles Q2-17's, suggesting that the strong double-digit decline is achieved on the back of stable FX.

Estimate and valuation: The net impact of the changes to our model is a cut to our 2018E EPS estimate to NGN3.89 (from NGN4.94 previously) and TP to NGN93.14 (previously NGN107.25), with HOLD rating. NB's stock has lost 19% since we updated on Q1-18 result, with a SELL recommendation. On our estimates, the stock is trading at forward (2018E) P/E and EV/EBITDA multiples of 27x and 10.1x, a discount to its five-year historical averages of 30.1x and 12.2x respectively.

HOLD

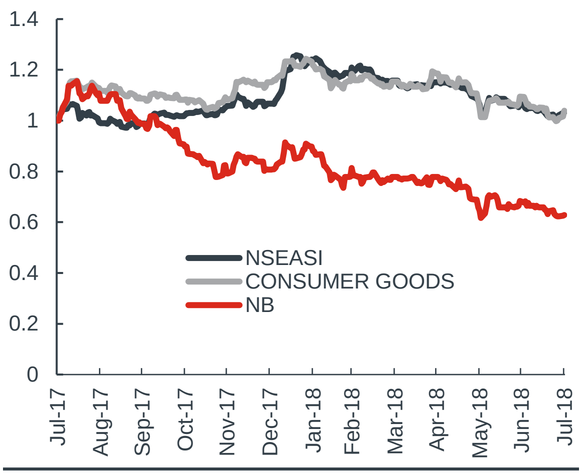
Target Price (NGN)	93.14
Current Price (NGN)	105.00
Implied Return (%)	-11.29
Expected Dividend Yield (%)	3.70
Expected Total Return	-7.59

Company Data	
NSE Code	NB
Bloomberg Code	NB:NL
Reuters Code	NB. LG
Sector	CONSUMER GOODS
Market Cap. (NGN' bn)	839.68
Free Float (%)	47.32

Ratios	Q2-2018	Q2-2017	2017FY
Gross margin	42.44%	45.44%	41.66%
Opex margin	27.12%	24.82%	25.73%
EBITDA margin	24.06%	30.12%	26.48%
EBIT margin	15.56%	22.42%	16.58%
PAT margin	9.18%	13.73%	9.59%
EPS (NGN)	1.03	1.54	4.13

*Trailing 12m

Price movement (NB vs. Benchmark Indices)



Source: NSE, Bloomberg, Cordros Research

Summary of Results.

Income Statement (NGN'bn)	30-Jun-18	30-Jun-17	y/y ∆	Q2-18	Q2-18 y/y	Cordros Q2 est.
Turnover	172.7	181.0	-4.6%	89.7	0.0%	95.9
Cost of sales	(96.6)	(99.2)	-2.6%	(51.6)	5.5%	(51.4)
Gross profit	76.1	81.8	-7.0%	38.1	-6.6%	44.5
OPEX	(44.9)	(44.3)	1.3%	(24.3)	9.2%	(23.6)
Other income/(exp.)	0.4	1.8	-76.3%	0.2	-86.8%	0.2
Operating income	31.6	39.3	-19.6%	14.0	-30.6%	21.1
Net finance charges	(4.1)	(5.3)	-22.7%	(1.7)	-52.7%	(2.7)
Profit Before Tax	27.5	34.1	-19.1%	12.3	-26.0%	18.3
Taxation	(9.1)	(10.3)	-11.6%	(4.1)	-5.8%	(4.8)
Profit after tax	18.4	23.8	-22.4%	8.2	-33.1%	13.5

Ratios	30-Jun-18	30-Jun-17	Q2-18	Q1-18	Q4-17	Q3-17	Q2-17	Q1'17
COS margin	55.9%	54.8%	57.6%	54.2%	59.0%	65.6%	54.6%	55.6%
Gross margin	44.1%	45.2%	42.4%	45.8%	41.0%	34.4%	45.4%	44.4%
OPEX margin	26.0%	24.5%	27.1%	24.8%	24.7%	30.7%	24.8%	23.6%
EBIT margin	18.3%	21.7%	15.6%	21.3%	16.5%	4.0%	22.4%	21.0%
Interest cover	7.8x	7.5x	8.4x	7.3x	5.7x	1.1x	5.8x	10.9x
PBT margin	16.0%	18.8%	13.7%	18.4%	13.6%	0.5%	18.5%	19.1%
PAT margin	10.7%	13.1%	9.2%	12.3%	10.1%	0.4%	13.7%	12.5%
Tax rate	33.1%	30.3%	33.1%	33.1%	25.9%	29.6%	26.0%	34.3%

Source: Company Accounts, Cordros Research estimates

Financial Statements (NGN billion).

Income Statement	2015a	2016a	2017a	2018e	2019e
Revenue	293.91	313.74	344.56	337.67	356.24
Cost of sales	-151.44	-178.22	-201.01	-197.54	-203.06
Gross profit	142.46	135.52	143.55	140.13	153.18
Operating expenses	-80.72	-83.24	-88.65	-87.79	-89.76
Other income	0.48	0.62	2.22	0.84	0.89
Net finance cost	-7.71	-13.23	-10.49	-8.33	-8.32
Profit before tax	54.51	39.67	46.63	44.86	55.99
Tax	-16.46	-11.26	-13.58	-13.77	-17.18
Profit after tax	38.06	28.42	33.05	31.09	38.81

Financial Position	2015a	2016a	2017a	2018e	2019e
Property, plant and equipment	197.30	191.18	195.23	192.17	202.40
Intangible assets and goodwill	100.61	99.48	98.28	99.03	104.30
Investments	0.15	0.15	0.15	0.15	0.15
Other receivables	0.32	0.62	0.55	0.46	0.49
Prepayments	0.35	1.15	0.53	0.72	0.76
Total non-current assets	***298.74***	***292.59***	***294.74***	***292.53***	***308.10***
Inventory	28.41	31.24	42.73	35.59	37.49
Trade and other receivables	16.51	19.97	20.38	35.77	37.67
Prepayments	1.04	0.30	1.04	1.82	1.91
Deposits for imports	2.23	8.43	7.47	1.86	1.96
Assets held for sale	4.18	2.45	0.00	0.00	0.00
Cash and cash equivalents	5.11	12.16	15.87	7.63	8.03
Total current assets	***57.48***	***74.56***	***87.49***	***82.67***	***87.06***
Total Assets	***356.22***	***367.15***	***382.23***	***375.20***	***395.17***
Loans and borrowings	-	17.00	8.00	16.20	16.20
Employee benefits	11.90	10.10	13.21	13.90	14.76
Deferred tax liabilities	31.91	29.88	26.67	25.58	27.16
Total non-current liabilities	***43.82***	***56.98***	***47.88***	***55.69***	***58.12***
Bank overdraft/Comm paper	19.21	0.87	0.47	15.61	15.61
Current tax liabilities	20.22	19.02	19.61	23.63	25.08
Dividend payable	12.40	12.68	8.03	9.47	10.06
Loans and borrowings	3.00	-	-	-	-
Provisions	-	0.50	0.00	0.00	0.00
Trade and other payables	85.25	111.68	127.95	94.43	102.22
Total current liabilities	***140.08***	***144.76***	***156.05***	***143.14***	***152.97***
Total liabilities	***183.90***	***201.73***	***203.93***	***198.83***	***211.09***
Total Equity	**172.32**	**165.41**	**178.30**	**176.37**	**184.08**

Profitability Ratios	2015a	2016a	2017a	2018e	2019e
Gross profit margin	48.5%	43.2%	41.7%	41.5%	43.0%
EBITDA margin	30.8%	26.3%	26.5%	25.2%	27.5%
EBIT margin	21.17%	16.86%	16.58%	15.75%	18.05%
PBT margin	18.5%	12.6%	13.5%	13.3%	15.7%
Net profit margin	12.9%	9.1%	9.6%	9.2%	10.9%
RoAE	22.4%	16.8%	19.2%	17.5%	21.5%
RoAA	12.3%	11.9%	11.5%	11.4%	11.2%

Liquidity Ratios	2015a	2016a	2017a	2018e	2019e
Working capital (NGN'bn)	-82.6	-70.2	-68.6	-60.5	-65.9
Current ratio	0.4x	0.5x	0.6x	0.6x	0.6x
Quick ratio	0.2x	0.3x	0.3x	0.3x	0.3x
Cash ratio	0.0x	0.1x	0.1x	0.1x	0.1x

Efficiency Ratios	2015a	2016a	2017a	2018e	2019e
Fixed assets turnover	1.5x	1.6x	1.8x	1.8x	1.8x
Current assets turnover	5.1x	4.2x	3.9x	4.1x	4.1x
Total assets turnover	0.8x	0.9x	0.9x	0.9x	0.9x
Inventory turnover	0.2x	0.2x	0.2x	0.2x	0.2x
Receivables turnover	0.1x	0.1x	0.1x	0.1x	0.1x
Payables turnover	0.6x	0.6x	0.6x	0.6x	0.5x
Days inventory outstanding	69	61	67	72	66
Days collection/sales outstanding	20	21	21	30	38
Days payable outstanding	46	2	1	29	28
Cash conversion cycle	43	81	88	74	75

Investment Ratios	2015a	2016a	2017a	2018e	2019e
Earnings per share (N)	4.8	3.6	4.1	3.89	4.85
Dividend per share (N)	4.8	3.6	4.1	3.89	4.85
Payout	100.0%	99.9%	99.9%	100.0%	100.0%
Dividend yield	3.8%	2.4%	3.2%	3.7%	4.6%
PE	26.3x	41.3x	31.7x	27.0x	21.6x
EV/EBITDA	11.2x	14.3x	11.4x	10.1x	8.8x

Source**:** Company Accounts, Cordros Research estimates

Disclosures.

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