

PZ Cussons Nigeria Plc.

Trading conditions remain tough heading into 2019

Update: We update on PZ following a challenging 2018FY, with Q4 earnings particularly showing persisting difficult trading conditions. **PZ Group (the parent company) did confirm that trading conditions in Nigeria have been the “toughest” it has experienced “in many years”, with less optimistic outlook.** In response, the group is implementing a number of revenue improvement initiatives, including cost savings, but the immediate impact on earnings is difficult to adapt into our model, given the extremely uncertain economic and consumer recovery, as well as inflation outlook.

Revenue improvement initiatives: The group said pack resizing and new launches have taken place across the HPC portfolio, with a view to improving revenue going forward. In Electricals, a new range of energy efficient models “suitable” for the Nigerian market has been launched to offer a competitive hedge in 2019E. **Overall, we believe the focus is on portfolio expansion, accessibility, affordability, and push for higher margin - a trend we have observed among our universe of local consumer goods companies.** That said, for PZ, we are conservative with a forecast 5% revenue growth in 2019E, as the group’s trading statement in June suggests trading conditions are yet to improve in Nigeria as at early Q1-19. However, we retained our average 10% revenue growth forecast for 2020-2021E on better economic outlook, and as we expect the new launches would have gained stronger acceptability among consumers.

Margins. Focus on cost savings and mix: At 23.7% in 2018FY (on LFL basis), PZ’s gross margins have now declined for three years in a row. EBITDA and EBIT margins have also weakened by over 500 bps each between 2015-2018FY. **Margins have largely been impacted by low utilization and cost inflation, although management said that prolonged lack of liquidity at the consumer level, amidst intense competition, has resulted in lower prices across some HPC product categories.** Elsewhere, opex is increasing at a faster pace than revenue at 6% 3-year CAGR (vs. 3% revenue CAGR), and way-above UNILEVER’s 1% 3-year CAGR (with 3-year revenue CAGR of 18%).

The margin improvement initiatives underway, according to management, cover (1) mix – focus on launching and pushing higher margin products and (2) cost savings – via reduction of packaging, overheads, and plastic consumption, as well as optimization of product portfolio across the HPC segment. We forecast gross, EBITDA, and EBIT margins to rise slightly to 24%, 7.4%, and 4.1% respectively in 2019E (2018FY: 23.7%, 7%, and 3.7% respectively), **although we do not see these margins reaching the recent year highs of 28%, 12%, and 9% respectively achieved in 2015FY over our forecast period.**

Changes to earnings estimates and TP: Our adjusted PBT estimate is NGN3.2 billion in 2019E (-43%), on lower revenue (-9%), gross margin (-50 bps), and net finance costs of NGN330.4 million (previously NGN184.5 million net finance income) estimates. But on our revised TP of NGN14.60/s, the stock trades at 11.2% upside, with HOLD rating. PZ’s stock has lost 41% since we last updated in March with a SELL recommendation. **Whilst the company’s challenged earnings have been largely priced-in, we believe the stock’s current price is also reflective of the overall bearish market condition.**

HOLD

Target Price (NGN)	14.60
Current Price (NGN)	13.50
Implied Return (%)	8.15
Expected Dividend Yield (%)	3.07
<u>Expected Total Return</u>	<u>11.22</u>

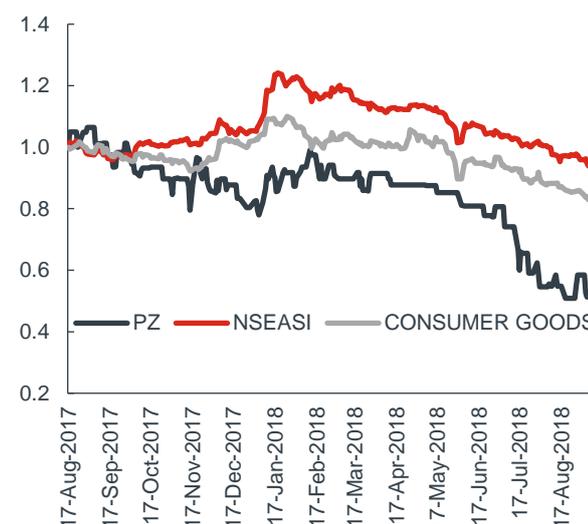
Company Data

NSE Code	PZ
Bloomberg Code	PZ:NL
Reuters Code	PZ.LG
Sector	CONSUMER GOODS
Market Cap. (NGN' bn)	53.60
<u>Free Float (%)</u>	<u>26.73</u>

Ratios	Q4-2018	Q4-2017	2018FY
*Gross margin	23.74%	26.83%	23.67%
Opex margin	21.52%	16.33%	20.15%
*EBITDA margin	7.64%	10.48%	6.99%
*EBIT margin	2.50%	10.73%	3.68%
PAT margin	3.41%	9.28%	2.39%
<u>EPS (NGN)</u>	<u>0.15</u>	<u>0.46</u>	<u>0.46</u>

*Like-for-like basis

Price movement (PZ vs. Benchmark Indices)



Source: NSE, Bloomberg, Cordros Research

Summary of Results.

Income Statement (N'bn)	2018FY	2017FY	y/y	y/y	May'18	Feb'18	Nov'17	Aug'17
Revenue	80.55	78.22	3.0%	1.2%	17.29	22.14	22.22	18.90
Cost of sales	-56.10	-50.27	11.6%	8.5%	-11.07	-16.23	-15.89	-12.91
Gross profit	24.46	27.95	-12.5%	-12.5%	6.22	5.91	6.33	5.99
Operating expenses	-16.23	-14.73	10.1%	10.1%	-3.72	-4.06	-4.31	-4.14
Other income	0.13	0.20	-35.2%	-35.2%	0.05	0.02	0.03	0.03
Net finance cost	-6.04	-8.60	-29.8%	-29.8%	-2.20	-0.77	-1.01	-2.07
Profit before tax	2.31	4.81	-51.9%	-51.9%	0.35	1.10	1.05	-0.18
Taxation	-0.39	-1.12	-65.6%	-65.6%	0.24	-0.35	-0.34	0.06
Profit after tax	1.93	3.69	-47.7%	-47.7%	0.59	0.75	0.71	-0.12

Ratio	2018FY	2017FY	May'18	Feb'18	Nov'17	Aug'17
Gross margin	30.36%	35.73%	35.97%	26.70%	28.50%	31.71%
Normalized gross margin	23.67%	24.48%	23.74%	23.51%	24.99%	22.22%
OPEX margin	20.15%	18.84%	21.52%	18.34%	19.38%	21.90%
Cost of sales margin	69.64%	64.27%	64.03%	73.30%	71.50%	68.29%
Normalized COS margin	76.33%	75.52%	76.26%	76.49%	75.01%	77.78%
EBIT margin	10.21%	16.90%	14.44%	8.36%	9.12%	9.81%
Normalized EBIT margin	3.68%	5.90%	2.50%	5.26%	5.75%	0.48%
PBT margin	2.87%	6.15%	2.01%	4.96%	4.72%	-0.96%
PAT margin	2.39%	4.71%	3.41%	3.38%	3.21%	-0.65%

Source: Company Accounts, Cordros Research estimate

Financial Statements (NGN billion).

Income Statement (NGN'bn)	2016a	2017a	2018a	2019e	2020e
Revenue	69.53	79.63	80.55	84.58	93.04
Cost of sales	-52.21	-60.48	-61.49	-64.28	-70.62
Gross profit	17.32	19.15	19.06	20.30	22.42
Operating expenses	-14.07	-14.73	-16.23	-16.95	-18.56
Other income	0.29	0.20	0.13	0.14	0.17
Net finance (cost)/income	-0.39	0.20	-0.65	-0.33	-0.38
Profit before tax	3.15	4.81	2.31	3.16	3.65
Tax	-1.02	-1.12	-0.39	-0.95	-1.10
Profit after tax	2.13	3.69	1.93	2.21	2.56
Non-controlling interest	-0.27	-0.36	-0.08	-0.15	-0.18
Equity holders of the Parent Company	1.86	3.32	1.85	2.06	2.38

Financial Position (NGN'bn)	2016a	2017a	2018a	2019e	2020e
PPE	26.50	28.51	28.43	29.18	30.46
Intangible assets	-	1.02	0.95	0.98	1.02
Other LT receivables	-	-	0.02	-	-
Total non-current assets	26.50	29.53	29.41	30.16	31.48
Inventories	19.28	28.71	26.04	26.72	27.90
Trade and other receivables	15.59	17.22	16.57	17.01	17.75
Deposit for imports	0.19	6.60	2.34	2.40	2.50
Cash & cash equivalents	12.87	8.02	14.26	14.66	15.30
Total current assets	47.93	60.56	59.21	60.79	63.46
Total Assets	74.43	90.09	88.62	90.95	94.94
Bank overdraft	-	-	1.00	0.24	0.26
Trade and other payables	25.72	39.72	40.20	40.87	43.71
Current taxation payable	1.29	2.56	0.46	0.47	0.50
Warranty provisions	0.09	0.09	0.08	0.09	0.09
Total current liabilities	27.10	42.37	40.98	41.66	44.56
Deferred taxation	3.69	2.40	2.42	2.46	2.63
Warranty provisions	0.24	0.18	0.10	0.11	0.11
Total non-current liabilities	3.93	2.58	2.53	2.57	2.75
Total liabilities	31.03	44.95	43.51	44.22	47.30
Total Equity	43.40	45.14	45.11	46.72	47.63

Profitability Ratios	2016a	2017a	2018a	2019e	2020e
Gross profit margin	24.9%	24.0%	23.7%	24.0%	24.1%
EBITDA margin	8.2%	8.7%	7.0%	7.4%	7.6%
EBIT margin	5.1%	5.8%	3.7%	4.1%	4.3%
PBT margin	4.5%	6.0%	2.9%	3.7%	3.9%
Net profit margin	3.1%	4.6%	2.39%	2.6%	2.7%
RoAE	4.9%	8.3%	4.3%	4.8%	5.4%
RoAA	3.0%	4.5%	2.2%	2.5%	2.7%

Liquidity Ratios	2016a	2017a	2018a	2019e	2020e
Working capital (NGN'bn)	20.8	18.2	18.2	19.1	18.9
Current ratio	1.8x	1.4x	1.4x	1.5x	1.4x
Quick ratio	1.1x	0.8x	0.8x	0.8x	0.8x
Cash ratio	0.5x	0.2x	0.3x	0.4x	0.3x

Efficiency Ratios	2016a	2017a	2018a	2019e	2020e
Fixed assets turnover	2.6x	2.8x	2.8x	2.9x	3.1x
Current assets turnover	1.5x	1.3x	1.4x	1.4x	1.5x
Total assets turnover	0.9x	0.9x	0.9x	0.9x	1.0x
Inventory turnover	0.4x	0.4x	0.4x	0.4x	0.4x
Receivables turnover	0.2x	0.2x	0.2x	0.2x	0.2x
Payables turnover	0.4x	0.5x	0.6x	0.6x	0.6x
Days inventory outstanding	141	145	162	150	141
Days collection/sales outstanding	88	75	77	72	68
Days payable outstanding	180	240	239	232	226
Cash conversion cycle	49	-20	0	-10	-17

Investment Ratios	2016a	2017a	2018a	2019e	2020e
Earnings per share (NGN)	0.47	0.84	0.46	0.52	0.60
Dividend per share (NGN)	0.50	0.50	0.15	0.41	0.48
Payout	106.6%	59.7%	32.3%	80.0%	80.0%
Dividend yield	2.3%	2.7%	0.7%	3.1%	3.6%
PE	46.2x	22.3x	47.0x	26.0x	22.5x
EV/EBITDA	12.9x	9.5x	12.9x	6.2x	5.4x

Source: Company Accounts, Cordros Research estimates

Disclosures.

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