

## Weaker-than-Expected Results as Excise Duty Weighs on Profitability

### INVESTMENT SUMMARY

The nine-month to September 2018 results recently released by the Nigerian Breweries Plc showed a setback in the top-line as revenue declined by 5.63% to ₦255.00 billion (vs. ₦270.21 billion in nine-month to September 2017). The newly introduced excise duty rate by the Federal Government of Nigeria in June 2018 contributed to the weaker-than-expected revenue of the company. The excise duty expense was ₦16.93 billion in 9M'18 and this resulted to a net revenue of ₦238.07 billion in 9M'18 (vs. ₦254.67 billion in 9M'17). However, we are impressed with the reduction in the cost of sales as lower revenue translated to lower cost. Cost of sales decreased by 3.01% to ₦143.35 billion in 9M'18 (vs. ₦147.81 billion in 9M'17). Sales to revenue ratio rose to 60.21% in 9M'18, from 58.04% reported in 9M'17. Consequently, gross profit declined by 11.37% to ₦94.72 billion in 9M'18 (vs. ₦106.86 billion in 9M'17). Marketing and distribution expenses fell by 0.80% to ₦51.45 billion in 9M'18 (vs. ₦51.86 billion in 9M'17) while administrative expenses increased by 9.72% to ₦16.18 billion in 9M'18 (vs. ₦14.75 billion in 9M'17). Profit before tax declined by 34.72% to ₦22.47 billion in 9M'18 (vs. ₦34.43 billion in 9M'17). The company made a provision of ₦7.68 billion for tax (9M'17: ₦10.42 billion) and as a result, profit after tax reduced by 38.40% to ₦14.79 billion in 9M'18 (vs. ₦24.01 billion reported in 9M'17). The setback in the profitability reflected on 12-month trailing EPS as it reduced by 26.27% to ₦2.98, from ₦4.04 recorded in the previous period. The company rewarded the shareholders with interim dividend of ₦0.60 (9M'17: ₦1.00). Based on the recent figures released by the company, we downgrade our forecasts and as a result we downgrade our target price to ₦94.19 (Previous target price: ₦96.34). However, we upgrade our recommendation to a **BUY** as the current market value of the stock (₦81.00) is far below its intrinsic value per share.

Fig. 1: Quarterly results highlights

	3Q2018	2Q2018	3Q2017	Q/q Δ	Y/y Δ
Net Revenue (₦mn)	65,406	89,693	73,680	-27.08%	-11.23%
Operating profit (₦mn)	-3,875	13,952	2,979	-127.77%	-230.1%
Net profit (₦mn)	-3,645	8,321	260	-19.33%	-1501%

Source: Bloomberg, PAC Research

Oluwole Adeyeye

oluwole.adeyeye@panafricancapitalholdings.com

### Price:

- Current	₦81.00
- Target	₦94.19
<b>Recommendation:</b>	<b>BUY</b>

\* As at Tuesday November 6, 2018

Fig. 2: Stock data

FYE	December
Price Mov't: YtD / 52wk	-39.96%/-44.15%
52-week range	₦155.00- ₦75.00
30-day Average vol.	1,964,548
Shares Outstanding (mn)	7,996.90
Market Cap. (₦bn)	647.75
EPS, ₦- 12months trailing	2.98
DPS, ₦- FY2017	4.13

Source: NSE, Company's Annual Reports, PAC Research

Fig. 3: Key ratios

	9M'18	9M'17
Gross profit margin	39.79%	41.96%
Net profit margin	6.21%	9.43%
Equity multiplier	2.15x	2.16x
Asset turnover	0.66x	0.66x

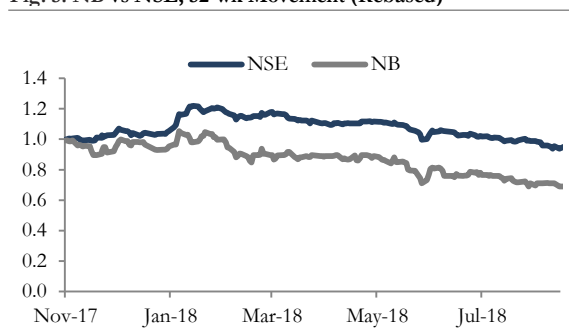
Source: NSE, PAC Research

Fig. 4: Valuations

	FY2016	FY2017	FY2018F	FY2019F
P/E	22.60	19.60x	23.64x	19.61x
P/B	3.87x	3.63x	3.74x	3.86x
PEG	-0.89x	1.28x	1.38x	0.95x
EV/EBITDA	32.05x	26.20x	43.88x	31.93x
P/S	2.05x	1.88x	2.03x	1.84x
ROE	17.13%	18.54%	15.82%	19.66%
ROA	7.74%	8.65%	7.36%	8.69%
Div. Yield	3.48%	4.01%	4.37%	4.85%

Source: NSE, PAC Research

Fig. 5: NB vs NSE, 52-wk Movement (Rebased)



Source: Bloomberg, PAC Research

Fig. 6: Net Revenue – 9M'17-12M'20E (Billion NGN)

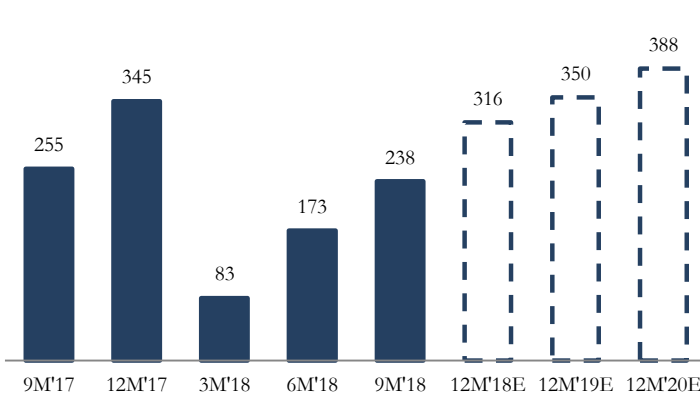


Fig. 7: Revenue, COS to Rev. and GP Margin - 9M'17-12M'20E

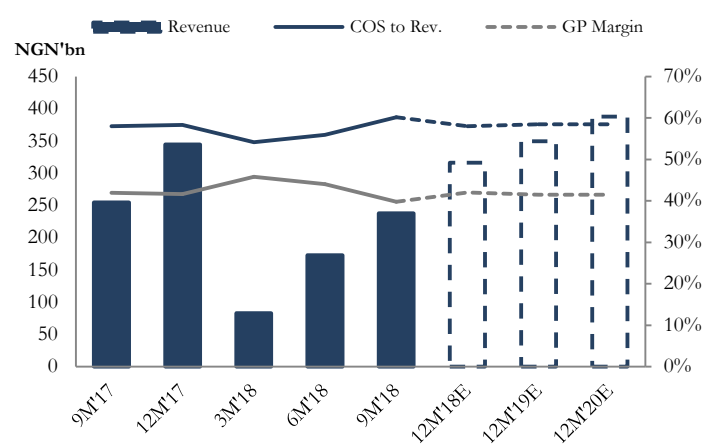


Fig. 8: PBT, PAT and Tax Margin - 9M'17-12M'20E

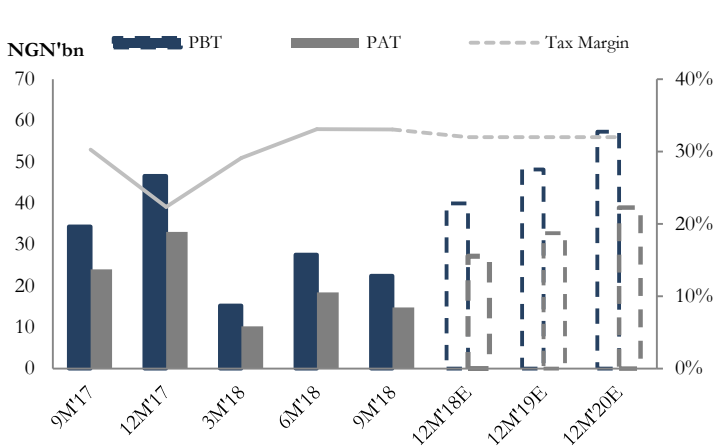
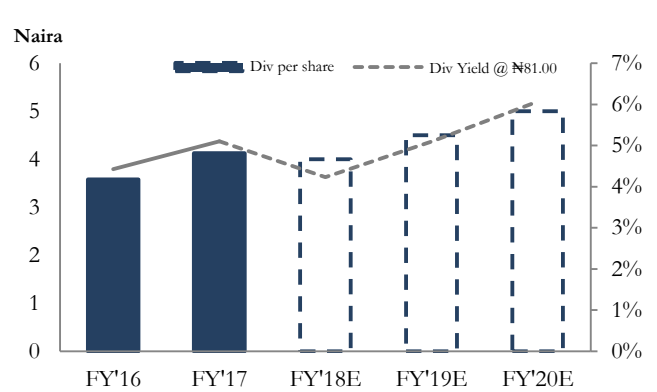


Fig. 9: Dividend Per Share and Dividend Yield - 9M'17-12M'20E



Source: NSE, PAC Research

PLEASE NOTE THAT WE COULD NOT HAVE COMPREHENSIVE REPORTS DUE TO THE LACK OF ADEQUATE INFORMATION FROM THE NIGERIAN BREWERIES PLC.

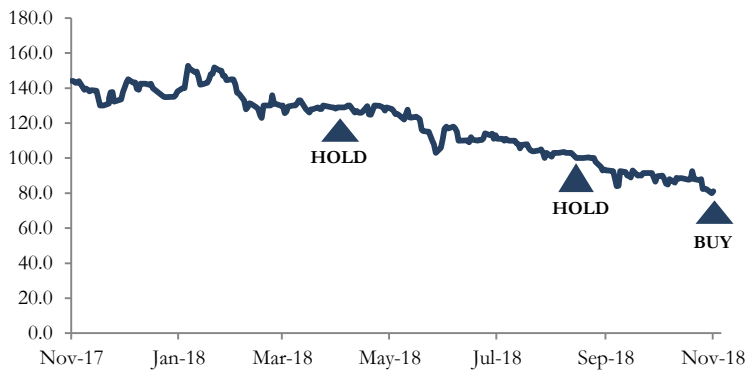
### Valuation

Our valuation puts the target price of the stock at ₦94.19 and this indicates that the stock is undervalued by 16.28% at current price of ₦81.00. In arriving at the target price, we employed discounted cashflow valuation methodology. Consequently, we maintained **BUY** recommendation on the stock of the company.

Our valuation and forecasts considered several factors (both quantitative and qualitative) among which are; the previous financial reports of the company, the current figures released by the company, the challenging operating environment in Nigeria, increased competition within the industry and a cautious outlook from the management.

*Our valuation puts the target price of the stock at ₦94.19 and this indicates that the stock is undervalued by 16.28% at current price of ₦81.00*

**Fig. 10: Share Price History**



Source: NSE, PAC Research

**Fig. 11: Statement of Profit or Loss, N'mn**

	2016	2017	2018E	2019E
Revenue	313,743	344,563	316,308	349,521
<i>Change</i>		9.82%	-8.20%	10.50%
Cost of sales	178,219	201,013	183,459	204,470
<i>Change</i>		12.79%	-8.73%	11.45%
Gross profit	135,525	143,549	132,850	145,051
<i>Change</i>		5.92%	-7.45%	9.18%
Other income	616	2,219	791	1,049
<i>Change</i>		260.36%	-64.36%	32.60%
Marketing & Distr. Exp.	61,312	66,899	67,374	69,205
<i>Change</i>		9.11%	0.71%	2.72%
Administrative expenses	21,925	21,748	19,927	21,670
<i>Change</i>		-0.81%	-8.37%	8.75%
Results from op. activities	52,903	57,121	46,339	55,224
<i>Change</i>		7.97%	-18.88%	19.17%
Net Finance costs	13,229	10,491	6,389	7,060
<i>Change</i>		-20.69%	-39.10%	10.50%
Profit Before Taxation	39,675	46,630	39,950	48,164
<i>Change</i>		17.53%	-14.33%	20.56%
Taxation	11,258	13,581	12,784	15,412
<i>Change</i>		20.64%	-5.87%	20.56%
Profit After Taxation	28,417	33,049	27,166	32,751
<i>Change</i>		16.30%	-17.80%	20.56%

**Fig. 12: Statement of Financial Position, N'mn**

	2016	2017	2018E	2019E
PPE	191,182	195,230	189,785	195,732
Intangible assets	99,478	98,277	96,474	101,361
Investments	150	150	158	175
Other receivables	623	552	569	699
Prepayments	1,154	526	633	524
Inventories	31,245	42,729	39,222	34,952
Trade and other rec.	19,974	20,384	20,560	19,224
Cash and bank Bal.	12,156	15,867	14,566	16,095
Total Assets	367,146	382,228	369,132	376,679
current tax liabilities	19,024	19,606	17,999	19,888
Dividend payable	12,676	8,029	7,908	8,738
Trade and Other pa.	111,184	127,947	116,401	120,585
Loans and Borrowings	17,000	8,000	18,979	20,971
Employee benefits	10,101	13,210	12,127	13,400
Deferred tax liab.	29,877	26,667	23,565	26,039
Total liabilities	201,233	203,930	197,410	210,099
Net Assets	165,914	178,298	171,722	166,580

**Fig. 13: Profitability Ratio**

	2016	2017	2018E	2019E
Gross profit margin	43.20%	41.66%	42.00%	41.50%
Net Profit Margin	9.06%	9.59%	8.59%	9.37%
operating profit margin	16.86%	16.58%	14.65%	15.80%
Return on Equity	17.13%	18.54%	15.82%	19.66%
Return on Assets	7.74%	8.65%	7.36%	8.69%
EBITDA Margin	6.44%	7.09%	4.70%	5.85%
ROCE	23.73%	25.26%	20.47%	24.33%

**Fig. 14: Asset Utilisation**

	2016	2017	2018E	2019E
cash/.sales	0.04	0.05	0.05	0.05
Sales to inventory (x)	10.04	8.06	8.06	10.00
Sales to total assets (x)	0.85	0.90	0.86	0.93
sales/EBITDA	15.52	14.10	21.28	17.09
Sales to total fixed assets	1.64	1.76	1.67	1.79
Equity multiplier	2.21	2.14	2.15	2.26

**Fig. 15: Liquidity Ratios**

	2016	2017	2018E	2019E
Quick ratio	0.30	0.29	0.30	0.29
Current ratio	0.52	0.56	0.57	0.52
Cash ratio	0.08	0.10	0.10	0.11
Interest Coverage	2.91	4.37	6.01	6.56
Op. Cash Flow Ratio	0.37	0.37	0.32	0.37
Debt/net income	0.63	0.26	0.71	0.65
Debt/operating profit	0.34	0.15	0.42	0.39
Debt to asset	0.05	0.02	0.05	0.06
Debt to equity	0.11	0.05	0.11	0.13
Total liabilities/equity	1.21	1.14	1.15	1.26
Total liab./ Total Assets	0.55	0.53	0.53	0.56
Inventory turnover	3.73	2.72	2.24	2.76
Inventory days	122.18	67.16	75.87	66.20
Account rec. days	23.24	21.59	23.73	20.08

**Fig. 16: Shareholders' Investment Ratios**

	2016	2017	2018E	2019E
Earnings per share	3.58	4.13	3.43	4.13
DiV per share	3.58	4.13	4.00	4.50
NAVPS	20.92	22.30	21.66	21.01
Earnings yield	4.42%	5.10%	4.23%	5.10%
FCFPS	9.09	9.01	9.10	9.19

Source: Company's Annual Reports, PAC Research

**Equity research methodology employed in this report**

Views documented in this equity research report stem from conclusions reached through the use of multiple valuation methodologies, industry-wide knowledge, company specific information and our near to medium term expectations of industry and company performance, as well as market outlook. Our forecasts are based on a combination of top down and bottom up analysis, alongside historical trends in industry and company financials. Where appropriate, we factored in available forecasts and business direction provided by company management.

Our recommendation tends towards value investing. Therefore, our investment rank gauge—a customized scale we use to judge how well a firm under coverage has performed—is determined using major value parameters as well as relevant ratios and multiples computed with figures from the company's most recent financials.

The variables used to arrive at the company's investment rank cover a wide range of measures which characterize liquidity, operational efficiency, profitability, profit margins, growth, economic viability, gearing, relative valuation ratios, capital structure and management performance. Our investment recommendation is underpinned by the upside or downside potential of a stock under coverage. This potential is estimated by comparing the stock's current market price to its price target and fair value, on a percentage increase or decrease basis as summarized below:

Deviation from current price	Recommendation
>30%	STRONG BUY
10% to < 30%	BUY
-10% to < 10%	HOLD
<-10%	SELL

**IMPORTANT DISCLOSURES**

This research report has been prepared by the analyst(s), whose name(s) appear on the front page of this document, to provide background information about the issues which are the subject matter of this report. It is given for information purposes only.

Each analyst hereby certifies that with respect to the issues discussed herein, all the views expressed in this document are his or her own and reflect his or her personal views about any and all of such matters. These views are not necessarily held or shared by PanAfrican Capital or any of its affiliate companies. The analyst(s) views herein are expressed in good faith and every effort has been made to base our opinion on reliable comprehensive information but no representation is made as to its accuracy or completeness. The opinions and information contained in this report are subject to change and neither the analysts nor PanAfrican Capital is under any obligation to notify you or make public any announcement with respect to such change.

This report is produced independently of PanAfrican Capital and the recommendations (if any), forecasts, opinions, estimates, expectations and views contained herein are entirely those of the analysts. While all reasonable care has been taken to ensure that the facts stated herein are accurate and that the recommendations, forecasts, opinions, estimates, expectations and views contained herein are fair and reasonable, none of the analysts, PanAfrican Capital nor any of its directors, officers or employees has verified the contents hereof and accordingly, none of the analysts, PanAfrican Capital nor any of its respective directors, officers or employees, shall be in any way responsible for the contents hereof.

With the exception of information regarding PanAfrican Capital, reports prepared by PanAfrican Capital analysts are based on public information. Facts and views presented in this report have not been reviewed and may not reflect information known to professionals on other PanAfrican Capital business areas including investment banking. This report does not provide individually tailored investment advice. Reports are prepared without regard to individual financial circumstances and objectives of persons who receive it. The securities discussed in this report may not be suitable for all investors. It is recommended that investors independently evaluate particular investments and strategies. The appropriateness of a particular investment or strategy will depend on an investor's individual circumstances or objectives. Neither the analyst(s), PanAfrican Capital, any of its respective directors, officers nor employees accepts any liability whatsoever for any loss so ever arising from any use of this report or its contents or otherwise arising in connection therewith. Each analyst and/or any person connected with any analyst may have acted upon or used the information herein contained, or the research or analysis on which it is based prior to its publication date. This document may not be relied upon by any of its recipients or any other person in making investment decisions.

Each research analyst certifies that no part of his or her compensation was, or will be directly or indirectly related to the specific recommendations (if any), opinions, forecasts, estimates or views in this report. Analysts' compensation is based upon activities and services intended to benefit clients of PanAfrican Capital. As with other employees of PanAfrican Capital, analysts' compensation is impacted by the overall profitability of PanAfrican Capital, which includes revenues from all business areas of PanAfrican Capital.

**PanAfrican Capital Holdings Ltd**

8A, Elsie Femi Pearse Street

Victoria Island

Lagos, Nigeria

Tel: +234 (1) 2716899, 2718630

[www.panafricancapitalplc.com](http://www.panafricancapitalplc.com)