

## Weaker Sales Reflects Strong Competition in the Market

### INVESTMENT SUMMARY

The 2019 unaudited first quarter results released by Unilever Nigeria Plc showed a disappointing figure in its top-line as revenue declined by 20.83% to ₦19.24 billion (vs. ₦24.30 billion in the first quarter of 2018). The disappointing result during the period can be attributed to weaker sales in Food Products segment and Home & Personal Care segment of the company. As a result of lower sales during the period, cost of sales declined by 12.55% to ₦15.34 billion (vs. ₦17.57 billion in Q1'18). However, the figure for the cost of sales in the first quarter of 2019 remains worrisome as cost-to-sales margin increased by 757bps to 79.89% in Q1'19 (vs. 72.32% in Q1'18). The company recorded lower operating expenses during the period, which reflected in a decline of 21.14% in selling & distribution expenses and 34.32% reduction in marketing & administrative expenses. Consequently, EBITDA fell by 25.88% to ₦2.96 billion in Q1'19 (vs. ₦3.99 billion in Q1'18).

Unilever Nigeria reported a significant improvement in its non-operating activities during the period as finance income increased by 72.87% to ₦0.80 billion in Q1'19 (vs. ₦0.47 billion in Q1'18). The company also recorded lower finance costs of ₦94.39 million in Q1'19 (₦92.72 million in Q1'18). Mainly as a result of poor operating performance, profit before tax fell significantly by 45.21% to ₦2.03 billion in Q1'19 (vs. ₦3.70 billion in Q1'18). During the review period, a provision of ₦0.51 billion was made for tax (vs. ₦0.96 billion in Q1'18). Consequently, Profit after tax declined by 44.43% to ₦1.52 billion in Q1'19 (vs. ₦2.74 billion in Q1'18). The disappointing bottom-line reflected on 12-month trailing EPS as it declined by 3.50% to ₦1.38, from ₦1.43 reported in the previous period. Based on the recent figures released by the company, we downgrade our target price per share and rating to **₦27.35** and **SELL** respectively.

Fig. 1: Quarterly results highlights

	1Q2019	4Q2018	1Q2018	Q/q Δ	Y/y Δ
Revenue (₦mn)	19,236	24,180	24,298	-20.45%	-20.83%
Operating profit (₦mn)	1,318	4,260	3,328	-69.06%	-60.40%
Net profit (₦mn)	1,521	3,846	2,737	-60.45%	-44.43%

Source: NSE, PAC Research

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Price:

- Current	<b>₦30.95</b>
- Target	<b>₦27.35</b>
<b>Recommendation:</b>	<b>SELL</b>

\* As at Friday June 7, 2019

Fig. 2: Stock data

FYE	December
Price Mov't: YtD / 52wk	-16.35%/-41.60%
52-week range	₦55.00 - ₦27.95
30-day Average vol.	5,738,670
Shares Outstanding ('mn)	5,745.01
Market Cap. (₦mn)	177,807.92
EPS, ₦- 12months trailing	1.38
DPS, ₦- FY2018	1.50

Source: NSE, Bloomberg, PAC Research

Fig. 3: Key ratios

	Q1'19	Q1'18
Gross profit margin	20.11%	27.68%
Net profit margin	7.91%	11.26%
Equity multiplier	1.60x	1.69x
Asset turnover	0.23x	0.31x

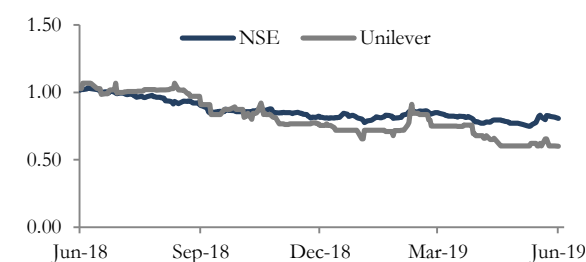
Source: NSE, PAC Research

Fig. 4: Valuations

	FY2017	FY2018	FY2019F	FY2020F
P/E	25.15x	19.47x	21.32x	15.62x
P/B	2.34x	2.15x	2.06x	1.91x
Sales Per Share	14.83	16.17	14.47	15.78
EV/EBITDA	7.83x	9.97x	11.23x	7.63x
P/Sales	2.09x	1.91x	2.14x	1.96x
ROE	9.31%	11.03%	9.68%	12.22%
ROA	5.84%	6.93%	6.35%	8.00%
Div. Yield	1.62%	4.85%	4.20%	5.49%

Source: NSE, PAC Research

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



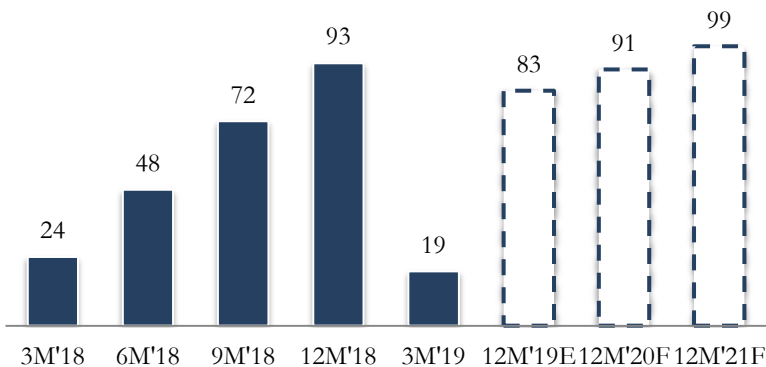
Source: NSE, PAC Research

**Due to weaker sales across board, revenue declines by 20.83% year-on-year.**

In three-month to March 2019, Unilever Nigeria reported a disappointing figure for total revenue as it fell significantly by 20.83% to ₦19.24 billion (vs. ₦24.30 billion in the three-month to March 2018). The reduction in the total revenue of the company can be attributed to the weak sales across board as revenue from Food Products segment and Home & Personal Care segment declined by 13.13% and 26.85% to ₦9.26 billion (vs. ₦10.65 billion in Q1'18) and ₦9.98 billion in Q1'19 (vs. ₦13.65 billion in Q1'18) respectively. Looking at the past trends, we are not surprised by the poor performance of the Home & Personal Care segment as the company always struggle to retain the market share of this segment. However, we are surprised with the performance of the Food Products segment as the company consistently recorded significant impressive performance in this segment over the past quarters. The decline in Food Products segment may be attributed to the intense competition in the seasoning businesses, which contributed the largest percentage to total sales. The rivals in Food products segment, particularly in the seasoning business, are NASCON and GB Foods who introduced Dan-Q Cubes and Gino Cubes respectively late last year. These newly introduced Dan-Q Cubes and Gino Cubes are also priced more competitively than Unilever's Knorr and Royco seasoning cubes in the market. Also, the sales of Spreads Business (Blueband margarine) in July 2018 may have contributed to the lower revenue in the Food Products segment of the company. Home and Personal Care segment remained the largest contributor to the company's revenue as it contributed 51.89% to the total revenue (Q1'18: 56.16%) while Food Products segment contributed 48.11% to total revenue in Q1'19 (Q1'18: 43.84%). Currently, the company has 135 customers, and no single customer accounted for more than 10% of the company's revenue.

*...we are not surprised by the poor performance of the Home & Personal Care segment as the company always struggle to retain the market share of this segment. However, we are surprised with the performance of the Food Products segment...*

**Fig. 6: Revenue – 3M'18 – 12M'21F (Billion NGN)**



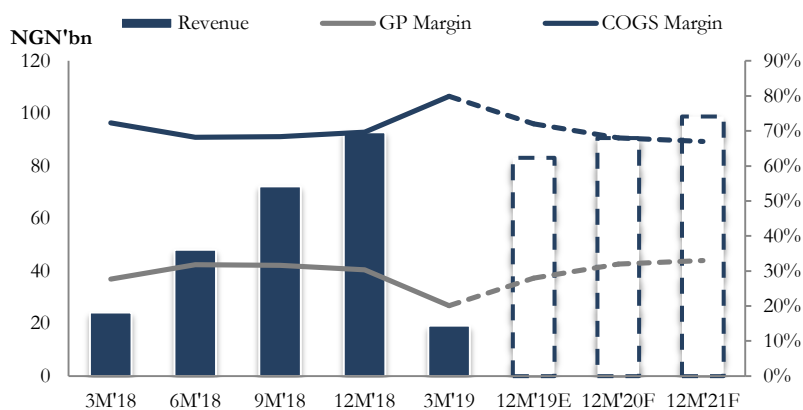
Source: NSE, PAC Research

**Unimpressive figure for cost of sales, reflected in higher cost of sales margin.** Due to lower sales during the review period, cost of sales declined by 12.55% to ₦15.37 billion, from ₦17.57 billion recorded in the corresponding quarter of the previous year. Although the company reported a lower figure for cost of sales during the period, cost-to-sales margin increased by 757bps to 79.89% in Q1'19 (vs. 72.32% in Q1'18). As witnessed in the previous quarters, the pressure on the cost of sales may be attributed to higher cost of raw materials and consumables. To achieve an impressive result, Unilever Nigeria Plc needs to improve in the area of local raw materials patronisation as the increase in the cost-to-sales margin may be largely attributed to high dependence on imported raw materials.

The company recorded a lower operating expenses during the period as administrative expenses and selling & distribution expenses fell during the period. Mainly as a result of lower overhead expenses in first quarter of 2019, total marketing & administrative expenses fell by 34.21% to ₦1.52 billion (vs. ₦2.31 billion reported in first quarter of 2018). Also, selling & distribution expenses declined by 34.21% to ₦0.86 billion in Q1'19 (vs. ₦1.09 billion in Q1'18). Consequently, EBITDA fell by 25.88% to ₦2.96 billion in three-month to March 2019 (vs. ₦3.99 billion in three-month to March 2018).

*To achieve an impressive result, Unilever Nigeria Plc needs to improve in the area of local raw materials patronisation as the increase in the cost-to-sales margin may be largely attributed to high dependence on imported raw materials.*

Fig. 7: Revenue, COS Margin & Gross Profit Margin – 3M'18 – 12M'21F (Billion NGN)



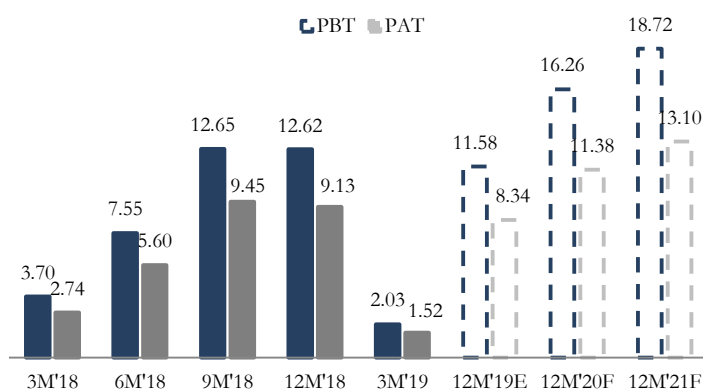
Source: NSE, PAC Research

**Weak operating performance outweighs impressive non-operating performance; profit before tax fell by 45.21% YoY.** Unilever Nigeria Plc recorded impressive performance in its non-operating activities as finance income increased significantly by 72.87% to ₦0.80 billion in Q1'19 (vs. ₦0.47 billion in Q1'18). The increase in finance income can be largely attributed to higher interest on call deposits and bank accounts as the company continues to benefit from the proceed of rights issue of 2017.

The benefit of proceeds from 2017 rights issue also reflected on lower finance cost of ₦94.39 million in Q1'19 (vs. ₦92.72 million in Q1'18) as the company had lower loans to service. The poor performance in the core operating activities of the company override the impressive figures of non-operating activities and as a result, profit before tax fell by 45.21% to ₦2.03 billion in Q1'19 (vs. ₦3.70 billion in Q1'18). The company made a provision of ₦0.51 billion for tax in Q1'19 (vs. ₦0.96 billion provision in Q1'18). Consequently, profit after tax declined significantly by 44.43% to ₦1.52 billion in three-month to March 2019 (vs. ₦2.74 billion achieved in three-month to March 2018).

*The benefit of proceeds from 2017 rights issue also reflected on lower finance cost of ₦94.39 million in Q1'19 (vs. ₦92.72 million in Q1'18) as the company had lower loans to service.*

Fig. 8: PBT and PAT– 3M'18 – 12M'21F (Billion NGN)

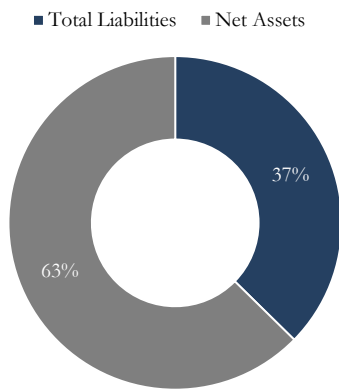


Source: NSE, PAC Research

**Balance sheet remains strong; expectation of lower final dividends in FY19.** Despite the poor performance in the income statement in the first quarter of 2019, the company continues to maintain a strong financial position. Due to higher inventories and trade & other receivables, total assets of the company increased by 1.21% to ₦134.57 billion in Q1'19 (vs. ₦132.96 billion reported in Q1'18). Impressively, total liabilities also declined by 7.19% to ₦50.26 billion in Q1'19 (vs. ₦54.15 billion in Q1'18), due to lower trade and other payables, reduced deferred tax liabilities and lower loans and borrowing during the period. Consequently, net assets rose by 6.98% to ₦84.31 billion (vs. ₦78.81 billion in Q1'18) and this translated to a higher net assets per share of ₦14.68 in Q1'19 (vs. ₦13.72 in Q1'18). With the unimpressive first quarter results, we do expect the company to pay a lower dividend per share of ₦1.30 in FY'19E, except there is a significant turnaround in the coming quarters of 2019.

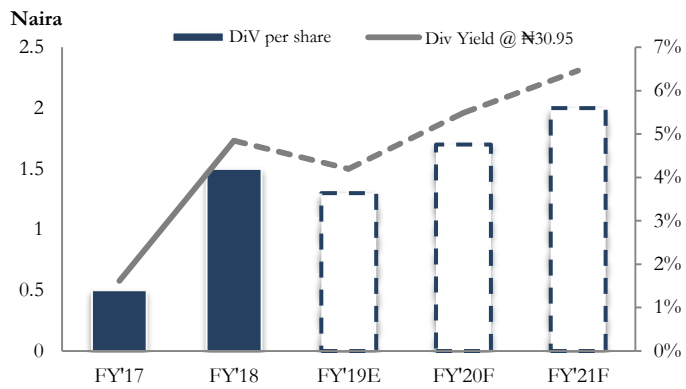
*With the unimpressive first quarter results, we do expect the company to pay a lower dividend per share of ₦1.30 in FY'19E, except there is a significant turnaround in the coming quarters of 2019.*

Fig. 9: Total Liabilities Vs Net Asset in Q1'19



Source: NSE, PAC Research

Fig. 10: Dividend Per Share and Dividend Yield (FY'17-FY'21F)



Source: NSE, PAC Research

**Valuation**

Our valuation puts the target price of the stock at ₦27.35, representing a decline of 11.64% from the current price of ₦30.95. In arriving at the target price, we employed discounted cashflow valuation methodology. Consequently, we downgrade to a **SELL** 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 and increase competition within the industry.

*Our valuation puts the target price of the stock at ₦27.35, representing a decline of 11.64% from the current price of ₦30.95*

**Fig. 11: Share Price History (Naira)**



Source: NSE, PAC Research

Fig. 12: Statement of Profit or Loss, N'mn

	2017	2018	2019E	2020F
Revenue	85,193	92,900	83,145	90,670
Change		9.05%	-10.50%	9.05%
Cost of Sales	(57,679)	(64,675)	(59,865)	(61,656)
Change		12.13%	-7.44%	2.99%
Gross Profit	27,514	28,225	23,281	29,014
Change		2.58%	-17.52%	24.63%
Selling and distribution exp.	(3,791)	(4,239)	(3,326)	(3,627)
Change		11.83%	-21.54%	9.05%
Marketing and admin. exp.	(11,476)	(14,713)	(11,640)	(12,694)
Change		28.20%	-20.88%	9.05%
Core Operating Profit	12,231	9,198	8,315	12,694
Change		-24.80%	-9.60%	52.67%
Finance Income	1,565	4,027	3,600	3,926
Change		157.27%	-10.60%	9.05%
Finance Cost	(3,201)	(603)	(540)	(589)
Change		-81.17%	-10.34%	9.05%
Profit Before Taxation	10,596	12,622	11,582	16,257
Change		19.12%	-8.24%	40.36%
Taxation	(3,526)	(3,490)	(3,243)	(4,877)
Change		-1.03%	-7.07%	50.39%
Profit After Taxation	7,070	9,132	8,339	11,380
Change		29.17%	-8.68%	36.46%

Fig. 13: Statement of Financial Position, N'mn

	2017	2018	2019E	2020F
Property, plant and equip.	29,881	29,678	29,517	31,281
Intangible assets	706	448	416	453
Other non- current assets	79	48	33	36
Inventories	11,479	13,929	14,135	15,414
Trade and other receivable	27,621	30,188	34,090	37,175
Cash and bank balances	50,494	57,144	52,797	57,576
Employee loan receivable	79	49	42	45
Total Assets	121,084	131,843	131,332	142,298
Trade and other payables	33,409	38,611	36,168	39,442
Income Tax	2,799	4,556	4,157	4,534
Deferred income	-	-	-	-
Deferred tax liabilities	4,485	3,652	2,910	3,173
Pension Obligations	3,660	2,231	1,912	2,040
Total Liabilities	45,176	49,054	45,149	49,189
Net Assets	75,908	82,790	86,184	93,108

Fig. 14: Profitability Ratio

	2017	2018	2019E	2020F
Return on Equity	9.31%	11.03%	9.68%	21.00%
Return on Assets	5.84%	6.93%	6.35%	8.00%
Gross margin	32.30%	30.38%	28.00%	32.00%
EBITDA margin	19.15%	13.03%	13.39%	17.39%
PBT margin	12.44%	13.59%	13.93%	17.93%
Net Profit Margin	8.30%	9.83%	10.03%	12.55%

Fig. 15: Asset Utilisation

	2017	2018	2019E	2020F
cash/.sales	0.59	0.62	0.64	0.64
Sales to inventory (x)	7.42	6.67	5.88	5.88
Sales to total assets (x)	0.70	0.70	0.63	0.64
Sales to total fixed assets	2.85	3.13	2.82	2.90
Equity multiplier	1.60	1.59	1.52	1.53
fixed asset turnover	2.85	3.13	2.82	2.90

Fig. 16: Liquidity Ratios

	2017	2018	2019E	2020F
Quick ratio	2.14	2.02	2.16	2.16
Current ratio	2.45	2.35	2.51	2.51
Cash ratio	1.38	1.32	1.31	1.31
Interest Coverage	3.82	15.26	15.77	21.92
Debt/net income	0.10	0.00	0.00	0.00
Debt to asset	0.01	0.00	0.00	0.00
Debt to equity	0.01	0.00	0.00	0.00
Total liabilities/equities	0.60	0.59	0.52	0.53
Inventory turnover	7.42	6.67	5.88	5.88
Inventory turnover days	49.18	54.73	62.05	62.05

Fig. 17: Shareholders' Investment Ratios

	2017	2018	2019E	2020F
EPS (₦)	1.23	1.59	1.45	1.98
DPS (₦)	0.50	1.50	1.30	1.70
NAVPS (₦)	13.21	14.41	15.00	16.21
Earnings yield (%)	3.98%	5.14%	4.69%	6.40%

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



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