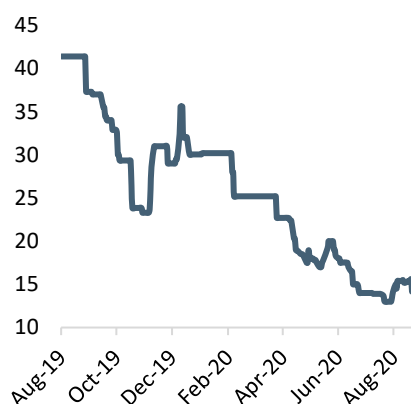




Rating	BUY
Price	₦14.15
FVE	₦18.94
52-week range	₦12.85 – ₦41.40
Market Cap. (₦'bn)	30.99
1-month Avg. Vol	3,544,291
Curr. PE	22.6x

GUINNESS .NL –Price Trend



Analyst(s)

Temitayo Peters

temitayo.peters@arm.com.ng

Guinness Nigeria Plc. (GUINNESS.NL)

Stock Report

Impairments push Guinness deep into the red

Guinness' Q420 result showed a higher than expected hit to their revenue numbers (-72% YoY) which led to a steep contraction of 71%YoY in their gross profit to ₦2.53 billion. Further aggravating the pressure on earnings was the ₦16.5 billion impairment charge booked over the period, resulting in an operating loss of ₦18.05 billion. However, tax credit received helped mitigate the loss in the quarter to ₦13.94 billion. Ex-impairment, Guinness' loss would have been much lower at ~₦2 billion before the tax credit which points to the impact the impairments had. While we expect a swift bounce back for Guinness as economy gradually re-opens the risk from its FCY loan and an adjustment to our revenue projections necessitated a cut in our FVE to ₦18.94 (previously: ₦26.63). Relative to the last closing price, this represents a 33% upside which translates to a BUY recommendation for the stock.

- Revenue decline exacerbated by spirits' performance:** Over Q420, Guinness' revenue declined sharply by 72% YoY to ₦8.36 billion (Q419: ₦30.61 billion) which is much sharper than the average 23%YoY decline suffered by their peers over the same period. Aside from the lockdown induced decline in volumes that was felt across the whole industry, Guinness' revenue was also hit by an implementation of a strict credit policy to minimise their credit risk. Receivables went as high as ₦31.56 billion at the end of Q220 but following this policy it declined to ₦18.72 billion at the end of Q4. This policy involved call-backs of stocks from distributors they were no longer partnering with which meant a reversal of revenue had to be recorded on their books. The effect of this was more keenly felt in the premium spirits segment which declined 92%YoY over H220. Additionally, spirits, which makes up a more significant part of total revenue for Guinness compared to the others, has had to face higher excise duties.
- Cost of sales declined 73%YoY to ₦5.83 billion (Q419: ₦24.17 billion) which was partly due to the decline in the cost of raw materials which aligned with what we saw for both Nigerian Breweries and International Breweries. Consequently, gross profit dropped sharply by 71%YoY to ₦2.53 billion and, since cost declined faster than revenue, the related margin came in higher at 30.2% compared to 28.7% in Q419.**

- **Impairments worsen the picture:** Away from the top line, the ubiquitous nature of impairments worsened the company's performance. This largely stemmed from the ₦11.72 billion impairment of PPE that the company has either deemed no longer a part of its current strategy or too old and idle to be viable. Additionally, there was a ₦2.7 billion impairment of Customer Deposit Liability (CDL) recognized as part of admin expenses which led those expenses higher by 154% YoY. A 94%YoY decline in sales and distribution, however, meant that overall increase in OPEX was only 0.5% to ₦6.85 billion (Q419: ₦6.82 billion). Finally, there was a ₦2.09 billion impairment loss recognized that relates to the Export Expansion Grant (EEG) that Guinness has discontinued.
- These impairments resulted in an operating loss of ₦18.05 billion (vs profit of ₦1.97 billion in Q419). Net finance costs rose 32%YoY to ₦1.03 billion (Q419: ₦782million) stemming from a 21%YoY increase in finance costs which in turn was a result of higher interest payments on loans and borrowings. Short term borrowings climbed 89%QoQ to ₦22.8 billion (Q320: ₦12.1 billion) following the issuance of a ₦5 billion commercial paper and the upward revaluation of a \$23million loan from parent company Diageo (by ₦580m) following the depreciation of the Naira. The loss before tax printed at ₦19.08 billion while a tax credit of ₦5.14 billion meant that the overall loss for the business was slightly lower at ₦13.94 billion.
- **Outlook:** Guinness' stock, down 52% YTD, has been much sold this year but looking ahead we see opportunities that could make this an attractive buy. Management confirmed their intention to keep focusing on RTDs and spirits which have grown in recent times and whose combined contribution to overall revenue has almost doubled from 22% at the end of FY17 to 43% at the end of FY20. These segments recorded growth in the first half of the year before the lockdown measures and strict credit policy and we expect them to gradually return to pre-covid sales levels following the reopening of the economy. Also, the decline in the premium spirits segment in FY20 was largely a result of a one-off event which we do not see continuing into FY21. Additionally, Guinness can set prices in the spirits segment, unlike the beer segment where they're price takers, which should give them more room for maneuvering should there be a further increase in excise duty.
- Management also highlighted plans to continue to reduce their presence in the lager segment which suffers from low margins, but they do intend to make a comeback via the premium beer segment with their Guinness Gold brand. Lager recorded a 45% decline over FY20 but the contribution of that segment has declined from 20% in FY17 to 2% in FY20 while the brand Guinness segment has seen its contribution increase from 29% to 36% over the same period.
- A major risk to consider is Guinness' foreign currency intercompany loan of \$23million that is due next May. The company has made it known that they would like to refinance the loan, but the scarcity of FX is making that difficult. Further depreciation of the naira would only serve to increase the burden of that loan, the impact of which would be felt in the form of higher finance costs
- Based on the aforementioned risk, and an adjustment in our revenue projections to reflect a slower rate of increase than initially expected, we have reduced our FVE by 30% to **₦18.94** which, based on current market price, represents a **BUY** rating.

Summary of Results and Forecasts - ₪'000

ANNUAL

Income Statement (₪'m) *	2019A	2020A	2021F	2022F	2023F
Revenue	131,498,373	104,376,015	106,022,507	110,282,452	115,255,161
COGS	(91,369,145)	(71,045,954)	(69,974,854)	(72,786,418)	(76,068,406)
Gross Profit	40,129,228	33,330,061	36,047,652	37,496,034	39,186,755
Operating Cost	(31,608,803)	(32,855,024)	(28,626,077)	(29,335,132)	(30,542,618)
Operating Profit	8,966,036	(12,832,256)	8,001,156	8,792,881	9,296,457
Net finance Cost	(1,862,406)	(4,241,385)	(4,428,039)	(4,366,207)	(4,630,610)
PBT	7,103,630	(17,073,641)	3,573,117	4,426,674	4,665,847
Tax	(1,619,898)	4,494,823	(1,071,935)	(1,328,002)	(1,399,754)
PAT	5,483,732	(12,578,818)	2,501,182	3,098,672	3,266,093
Balance Sheet (₪ '000) *					
Fixed Assets	100,801,064	88,919,044	101,456,742	100,715,798	99,898,146
Inventory	25,180,431	26,426,253	21,342,331	21,835,925	22,059,838
Receivables & payables	25,180,431	26,426,253	21,342,331	21,835,925	22,059,838
Cash & other bank balances	4,756,561	5,271,224	11,072,619	15,312,462	18,168,006
Total Assets	160,792,627	144,145,581	157,205,829	161,914,753	166,173,485
Liabilities					
Trade Creditors	31,921,108	31,944,466	30,089,187	30,570,296	30,427,362
Non-current Liabilities	22,875,691	10,509,465	18,410,807	18,753,015	19,108,911
Total liabilities	71,732,165	71,107,441	66,510,039	68,290,763	69,492,243
Shareholders' fund	89,060,462	73,038,140	78,590,854	80,358,923	82,222,522
Key Ratios					
	2019A	2020A	2021F	2022F	2023F
Gross Margin	30.5%	31.9%	34.0%	34.0%	34.0%
EBIT Margin	6.8%	-12.3%	7.5%	8.0%	8.1%
PBT Margin	5%	-16%	3.4%	4.0%	4.0%
PATt Margin	4%	-12%	2.4%	2.8%	2.8%
EPS	2.50	- 5.74	1.14	1.41	1.49

ARM ratings and recommendations

ARM now employs a two-tier rating system which is based on systemic importance of the security under review and the deviation of our target price for the stock from current market price. We characterize systemic importance as a function of a stock's ranking among the group of top 20 stocks by NSE market capitalization over a trailing 6-month period (minimum) to the review date. We adopt a 5-point rating system for this category of stocks and a 3-point rating system for stocks outside this group. The choice of top 20 stocks arises from the consideration that this group of stocks constitutes >75% of overall market capitalization and stocks outside this group are generally less liquid and individually account for <<1% of market capitalization. For stocks in both categories, the basis for ratings subject to target price deviation is outlined below:

TOP 20		NON-TOP 20	
Rating	Deviation	Rating	Deviation
STRONG BUY	>20%	BUY	>20%
OVERWEIGHT	10% — 20 %	NEUTRAL	5% — 20 %
NEUTRAL	0% — 10 %	SELL	<5%
UNDERWEIGHT	-5% — 0%		
SELL	<-5%		

RECOMMENDATION KEY	
Rating	Recommendation
BUY	Accumulate security to a substantial extent constrained only by portfolio diversification considerations
OVERWEIGHT	Accumulate security to an extent moderated by cognizance of its benchmark weight
NEUTRAL	Maintain status quo for security with respect to current holding—i.e. keep if already holding and don't buy otherwise—subject to reasonable portfolio constraints
UNDERWEIGHT	Minimize exposure to security taking cognizance of its index weighting
SELL	Sell-off security completely from portfolio

Copyright © 2020 ARM Securities Limited (“ARMS”).

All rights reserved. Unauthorised use, reproduction, distribution, or disclosure of this document is strictly prohibited.

This material has been issued by ARM Securities Limited, a member of the Asset and Resource Management (“ARM”) Group, and a Company regulated by the Nigerian Securities & Exchange Commission. The analyst(s) primarily responsible for preparing this research report, in whole or in part, certifies that with respect to each security or issuer covered; all of the views expressed accurately reflect his/her personal views about the subject securities and issuers and no part of his/her compensation was, is, or will be, directly or indirectly, related to the inclusion of specific recommendations or views in the report.

This research report is based on information from sources that ARMS and its analysts believe to be reliable. Neither ARMS nor any of its research analysts, nor any member of the ARM Group, gives any representation or warranty, express or implied, or undertaking of any kind or assumes responsibility or liability of any kind with respect to the accuracy or completeness of the information set out in this report or any third party’s use (or the results of such use) of such information. This report is provided solely for informational purposes and is not to be construed as providing advice, recommendations, or endorsements of any kind whatsoever. The investments and strategies discussed here may not be suitable for all investors; counsel of investment advisor should be obtained with regard to such investments and or strategies. This research report is not a replacement for advice from an accountant, lawyer, personal finance advisor or other category of investment advisor. The investments discussed in this report may oscillate in price or value. Opinions and information provided are made as of the date of the report issue and are subject to change without notice. This research report is not intended as an offer or solicitation for the purchase or sale of any financial instrument. Reference herein to any specific security or financial instrument does not necessarily constitute or imply its endorsement or recommendation by ARMS, its directors, officers, employees or designated agents. Members of ARM may act as broker, advisor or lender, or make a market in any investments or issuers referenced in this report. Further information on any of the securities discussed herein may be obtained upon request to ARMS. By accepting this document, you agree to be bound by the foregoing limitations.