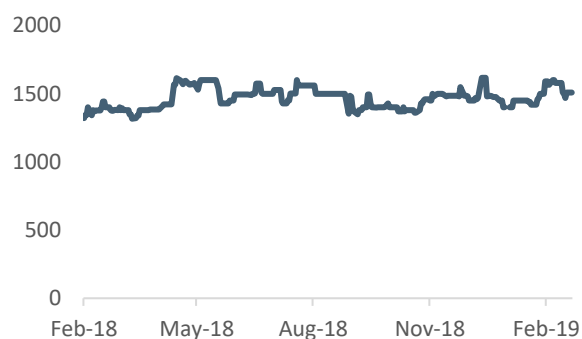




Rating	SELL
Price	₦1,510.00
52-week range	₦1317– ₦1645
Market Cap. (₦'bn)	1,197
1-month Avg. Vol	152,744
Current PE	27.8x

NESTLE: NL - Share Price Trend



Analyst(s)

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Nestle Nigeria Plc (NESTLE.NL)

Initial View

Topline gains eroded by operating cost pressures

- Nestle Nigeria Plc (Nestle) released Q4 18 results, reporting 7.9% YoY decrease in EPS to ₦12.48 stemming from an increase in operating cost following promotional offers during the period. Earnings reported in the period was, however, weaker than our estimate of ₦15.11 majorly due to lower than expected revenue. For context, given that Q4 happens to be the strongest quarter, we expected a double-digit growth from its food business – similar to the trend in the last two quarters. Based on the lower than expected Q4 performance, Nestle's EPS for FY 18 was up 27.5% YoY to ₦54.26, tracking below our estimate of ₦56.89. **Accordingly, the company declared a final dividend of ₦38.50 (+40% YoY), split into ₦34.20 from its FY 18 earnings and ₦4.30 from its FY 09 earnings. Based on current pricing, the dividend yield stands at 2.5%.**
- **Revenue improves on volume growth.** Revenue in the review quarter increased 7.2% YoY to ₦63.1 billion. On drivers, we note that a recovery in the beverage segment coupled with the improvement in food drove the increased revenue. Over Q4 18, revenue from the beverage segment expanded by 9.5% YoY to ₦24.0 billion (Q3 18: -1.3% YoY), while food grew by 5.8% YoY (below Q2 - Q3 YoY average growth of 11.7%) to ₦43.9 billion. For us, we believe the recovery in the beverage segment was largely supported by increased volumes as our price survey revealed a single digit decline in average product prices as the company embarked on promotional activities during the period. In the food segment, our survey revealed a 2.8% YoY price decline on flagship product “*maggi*”.

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- **Earnings drop, on higher operating expenses.** Over the period, Nestle reported 11% YoY increase in gross profit while gross margin expanded 156bps YoY to 44%, driven by a slower increase in cost of sales (+4.3% YoY) relative to topline growth. The improvement in margin reflects moderation in the prices of its major inputs¹ over Q4 18. Despite the positive outturn in gross margin, operating profit contracted by 11% to ₦11.3 billion, due to higher operating expense. For the period, opex to sales ratio increased by 510bps to 26.1% stemming from its selling and admin expenses as the company embarked on increased advertising and promotional offers during the period.
 - Further down, the company recorded a net finance income of ₦381.6 million, compared to a net finance expense of ₦263.5 million. The improved financing line largely reflects a reversal of prior quarters finance cost over Q4 of ₦54 million coupled with a finance income of ₦327 million. Notwithstanding, given the weak operating performance, earnings for the period came in lower with PAT at ₦9.9 billion (-7.9% YoY).
 - Overall, while EPS came in lower, we find the result decent as the company continues to grow its volumes amidst depressed consumer wallets. Our last communicated FVE on Nestle is ₦1,330.35 which translates to a **SELL** rating on the stock. NESTLE trades at a current P/E and EV/EBITDA of 27.8x and 18.4x relative to Bloomberg Mena peer average of 23.0x and 13.2x.
 - **More analysis to follow.**

¹ Maize (-6.2%), Sorghum (-11.1%) and Sugar (-15.7%)

Summary of Results and Forecast

Income statement – (¥ million)	Q4 18	YoY growth	QoQ growth	Deviation from forecast	FY 18	YoY growth
Revenue	63,140	7.20%	-6.90%	9.30%	266,275	9.06%
Cost of sales	35,370	4.30%	-5.10%	6.30%	-152,354	6.33%
Gross profit	27,770	11.00%	-9.20%	13.20%	113,920	12.94%
OPEX	16,489	33.20%	23.40%	-14.50%	-53,279	17.95%
Operating profit	11,281	-10.60%	-34.40%	53.50%	60,641	8.87%
Net finance expense	381.58	NA	NA	-113.70%	-890	
PBT	11,662	-5.60%	-28.10%	-28.10%	59,751	27.59%
PAT	9,890	-7.90%	-15.20%	-15.20%	43,008	27.53%

*N/M means not meaningful

Key Ratios	Q4 18	Q3 17	Change(pps)	FY 18	FY 17	Change(pps)
Gross margin	43.98%	45.07%	-1.08%	42.78%	41.31%	1.47%
EBIT margin	17.87%	25.36%	-0.50%	22.77%	22.81%	-0.04%
PBT margin	18.47%	23.90%	8.10%	22.44%	19.18%	3.26%
PAT margin	15.66%	17.19%	7.00%	16.15%	13.81%	2.34%
Effective tax rate	15.20%	28.09%	-7.70%	-28.02%	-27.98%	-0.04%

Source: ARM Research

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
RESTRICTED	In certain circumstances, Asset & Resource Management ("ARM") Group policy and/or applicable law and regulations preclude certain types of communications, including an investment recommendation, during the course of ARM Securities' and/or ARM Group's engagement in an investment banking transaction and in certain other circumstances.

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