

Rating	BUY
Price	₦28.35
FVE	₦35.81
52-week range	₦0.5- ₦ 39.03
Market Cap. (₦'bn)	7.201
1-month Avg. Vol	42,637
Curr. PE	5.20x

Quarterly EPS	Q1	Q2	Q3	Q4
2016 A	1.43	2.15	1.03	0.33
2017 A	3.51	-0.74	0.42	2.27

MRSOIL: NL - Share Price Trend



Analyst(s)

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MRS Nigeria Plc. (MRSOIL: NL)

Stock Report

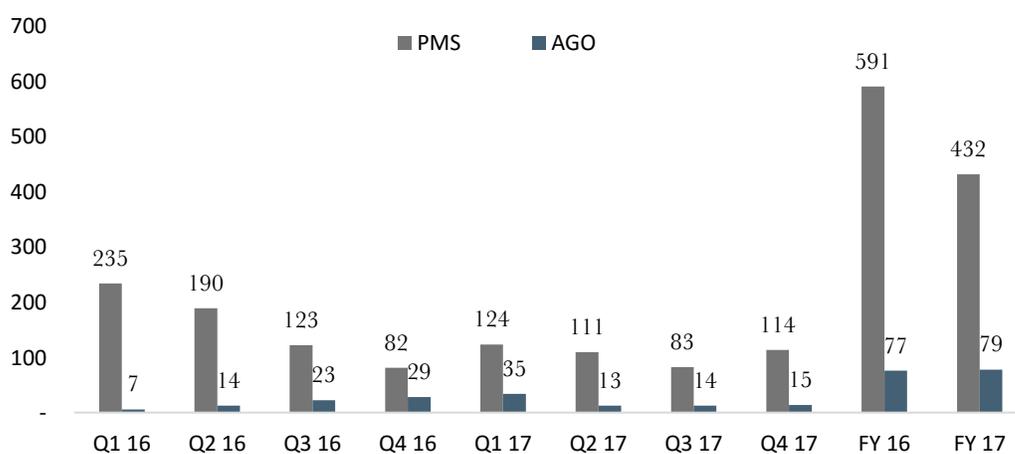
Core earnings yield to materially lower income

- In this note, we transfer primary coverage of MRS Nigeria Plc. (MRS) to Olamide Adeboboye.
- MRS Nigeria Plc (MRS) full-year result showed a 6% YoY increase in earnings with EPS printing at ₦5.45 (2016: ₦5.77). The board of directors proposed a bonus shares issuance in the ratio of 1 for every 5 shares held by shareholders, which implies newly issued share of 51 million to bring shares outstanding (SHO) to 305 million units.
- The positive earnings, when compared to other downstream players who reported lower earnings YoY¹, was solely driven by a surprise tax credit of ~₦2.4 billion which masked the loss before tax position of ₦997 million. Unlike its peers, MRS was quite resilience in defending its margins, with gross margin contracting by 80bps YoY to 7.2% relative to sector average of 266bps YoY decline to 12.06%. Lubricant business recorded a ~10pps expansion in gross margin, but margin pressure was expectedly evident in the fuel and aviation segment wherein gross margin contracted 120bps and 330bps YoY to 5.6% and 7.7% accordingly. In sync with sector-wide supply challenges, the decline in sales (-2.3% YoY to ₦107 billion) was largely due to lower volumes on PMS which our estimate puts at 432 million litres (2016: 591 million litres). On the flipside, AGO volumes increased slightly by 2.9% to 78 million litres.

¹ Except Forte Oil due to strong numbers from its power business

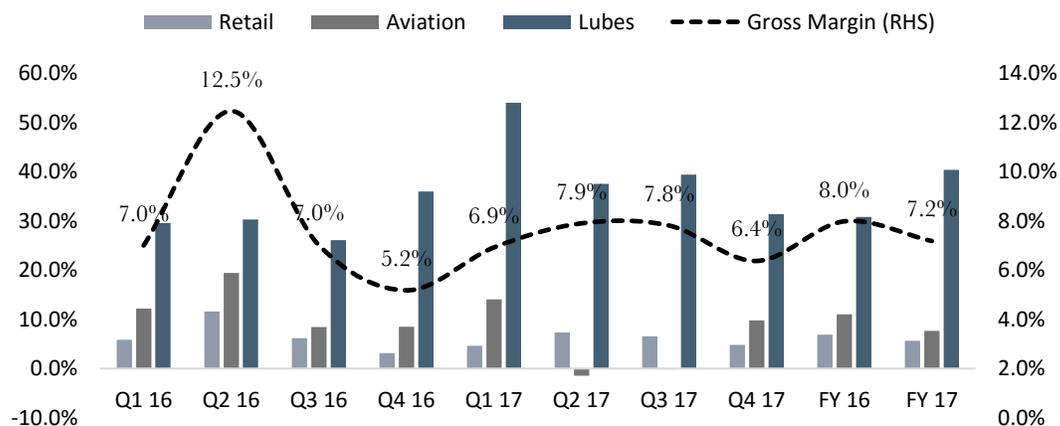
- The loss position at the PBT level reflected the material decline in other income as well as finance income. Other income printed at ₦150 million relative to ₦1.3 billion in 2016. The decline emanated from lower handling fees of ₦47 million (2016: ₦594 million) and income on storage services of ₦75 million (2016: ₦623 million). To our minds, the supply challenges, a reflection of sole reliance on NNPC for petrol supply as well as bottleneck in accessing Apapa terminal, impacted on the storage and handling services. On the finance income line which printed at ₦112 million (2016: ₦634 million), this was due to lower cash position of ₦3 billion (2016: ₦10.9 billion) as the company repaid ₦18 billion short term borrowings in the period. Consequently, total debt now prints at ₦9.6 billion relative to ₦18.5 billion in the prior year.

Figure 1: Diesel and Petrol volumes (million litres)



Source: Company Financials, ARM Research

Figure 2: Gross margin (Retail, Lubes, Aviation vs. Overall Gross Margin)



Source: Company Financials, ARM Research

2018 will be more of the same

- Going into 2018, we are of the view that performance will be largely like 2017 as supply challenges remain evident and continue to impact on volumes and margins. Furthermore, we think other income will remain depressed, albeit slightly higher than 2017 levels. On the positive, an improved debt position, given ₦18 billion short term debt repayment and fuel sourcing from NNPC guides to lower payables, which will provide some support. Elsewhere, given our view on stable currency, we rule out the possibility of further FX loss on its payables². Overall, the impact of a material decline in other income and finance income, as well as margin pressure, will drive a loss before tax position of ₦191 million in 2018. However, a possible recovery of ₦16 billion receivables from PPPRA may salvage earnings in 2018.
- Starting from top-line, we expect the effect of lower volumes to become more glaring as the price support for revenue seen in prior year fades. For the retail segment³, while we envisage no movement in prices for both diesel and PMS – the duo of sole reliance on NNPC in sourcing its products and suppressed industry wide demand for AGO would drive volumes lower. Consequently, we estimate a 10% decline in both PMS and Diesel volumes to 461 million litres. For lubricants, the relative naira stability would breed more competition and limit the prospect for significant growth in sales (+5% YoY to ₦4.6 billion). Overall, given that the retail business accounts for over 80% of total revenue, we expect total revenue to drop by 6.8% YoY to ₦101 billion (-5.8% YoY). Elsewhere, lower PMS and AGO volumes would drive cost lower by 5.6% to ₦93 billion which translates to a gross margin of 7% (-0.2pps YoY).
- Further down, given same persisting supply challenges which will pressure income from handling and storage services, we model other income to turnover of 0.30% (2017: 0.14%) which brings other income to ₦303 million. Reflecting lower cash and debt position, we forecast finance income of ₦79.6 million (-30% YoY) and finance cost of ₦678 million (-44% YoY), to bring net finance cost to ₦598 million (2017: ₦1.1 billion). Irrespective of the operating income which is expected to print at ₦408 million (3x YoY) - a reflection depressed income and 9% decline in gross profit - the net finance cost, though lower than 2017 guides to a loss before and after tax of ₦191 million and ₦258 million respectively.

² 2017 FX loss on payables – ₦784 million (2016: ₦1.2 billion)

³ Retail segment refers to the sale of PMS and AGO

- Farther out, beyond 2018, we expect the company to return to profitability, as improved supply picture and benign cost pressure is expected to drive earnings, wherein we forecast a 50% CAGR in earnings over 2019F – 2022F. Net Impact of our adjustment informs a **FVE** of ₦35.81 – a 26% upside from last closing price. MRS trades at a P/E of 5.2x compared to its industry peers of 9.79x.

Summary of Results and Forecasts - Naira (₦)

ANNUAL					
Income Statement (₦' m) *	2016A	2017A	2018F	2019F	2020F
Sales	109,635	107,088	100,854	107,904	111,809
COGS	-100,880	-99,394	-93,841	-99,702	-102,611
Gross profit	8,755	7,695	7,013	8,202	9,198
Operating cost	-6,753	-7,744	-6,908	-6,822	-6,628
Operating profit	3,290	101	408	2,385	3,611
Net finance cost	-1,002	-1,098	-599	-480	-352
PBT	2,287	-997	-191	1,905	3,259
Tax	-821	2,382	-67	-667	-1,141
PAT	1,466	1,385	-258	1,238	2,118
Balance Sheet (₦ '000) *					
Assets					
Investment property	18,402	17,338	15,511	13,401	11,301
Inventories	7,004	5,289	7,282	7,737	7,963
Trade debtors	43,245	34,235	23,761	25,422	26,341
Cash and other bank balances	10,911	3,981	10,235	12,039	16,047
Total Assets	81,365	62,190	58,092	59,923	62,987
Liabilities					
Trade Creditors	32,157	24,233	22,666	23,533	25,016
Interest bearing loans & borrowings	18,527	9,640	9,736	9,834	9,932
Total liabilities	76,234	60,024	55,970	57,800	60,864
Shareholders' fund	22,164	23,109	22,793	23,660	25,143
Key Ratios					
Gross margin	8.0%	7.2%	7.0%	7.6%	8.2%
Operating margin	4.4%	1.5%	1.9%	3.6%	4.5%
EBIT Margin	3.0%	0.1%	0.4%	2.2%	3.2%
Pre – tax margin	2.1%	-0.9%	-0.2%	1.8%	2.9%
Valuation multiples	1.3%	1.3%	-0.3%	1.1%	1.9%
EV/EBITDA					
P/CF	NA	NA	1.4	8.0	2.9
P/B	0.5	0.5	0.5	0.5	0.0
P/E	7.8	8.2	N/A	9.2	5.4

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