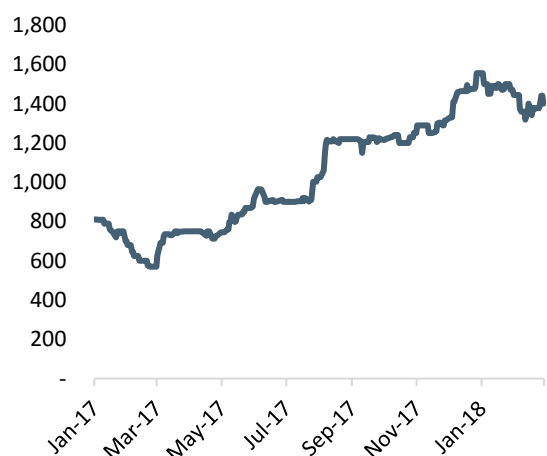




Rating	<b>SELL</b>
Price	₦1400.00
FVE	<b>₦948.01</b>
52-week range	₦691-1555.99
Market Cap. (₦'bn)	1,110
1-month Avg. Vol	998,049
Curr. PE	31.9x

Quarterly EPS	Q1	Q2	Q3	Q4
<b>2015 A</b>	3.73	7.48	10.53	8.20
<b>2016 A</b>	8.43	7.75	0.06	9.39
<b>2017 A</b>	10.55	10.33	8.11	13.55

#### NESTLE:NL - Share Price Trend



#### Analyst(s)

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## Nestle Nigeria Plc. (NESTLE.NL)

### Initial View

### Earnings rebound to its strongest level on record

- Nestle Nigeria Plc (Nestle) bounced back from 2016 tough time, coming out stronger, with its recently released full-year 2017 results revealing a solid growth in earnings of ₦33.7 billion – its highest absolute earnings on record. Earnings reported in FY 17 translates to an EPS of ₦42.55 (vs. ₦10.00 in FY 16), a four-fold increase from the prior year. Accordingly, the company declared a final dividend per share of ₦27.50 which in addition to the interim dividend of ₦15.00 amounts to a total dividend of ₦42.50 (vs. ₦10.00 DPS in FY 16). Final dividend implies a dividend yield of 2.0% based on last trading price.
- Much of the turnaround in Nestle's FY 17 earnings reflects improved operating profit margin (+181bps to 22.8%) and lower foreign exchange losses (-31.4% YoY to ₦11.2 billion). Isolating Q4 17 standalone result also reveals a 44.4% YoY increase in EPS to ₦13.55. However, the growth in earnings was primarily driven by a lower effective tax of 13% (vs. 54% in FY 16) with before-tax earnings declining 23.0% YoY to ₦12.3 billion. Subsisting input cost pressures and lower finance income were the key pressure points on Q4 PBT performance which offset a 12.8% YoY increase in revenue underpinned by higher product price. The Q4 revenue revealed a fallout from historical trend as the number was weaker than earlier quarters, with its contribution to aggregate turnover contracted to 24% (vs. 5-year average contribution of 28.3%).

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- As mentioned earlier, foreign exchange losses over 2017 amounted to ₦11.2 billion, 31.4% lower than ₦16.3 billion booked in 2016. The sizeable decline in FX losses reflected tamer depreciation following improved dollar liquidity as well as currency stability. Specifically, over 2017, the company paid around \$111 million worth of due related party loans on which it recorded FX losses of ₦7.3 billion – we estimate that the company settled its dollar obligations at an exchange rate around ₦370/\$, 16% higher than carrying value rate of ₦320/\$. The balance of FX losses (₦3.9 billion) booked most likely stemmed from the settlement of related party trade payables during the period. Further on dollar debt, Nestle Nigeria secured another \$30 million loan from its parent company – Nestle S.A – of which \$15.2 billion was drawn down in the review period. Given this, Nestle’s outstanding dollar loan currently stands at \$48.8 million (₦18 billion) valued at a rate around ₦369/\$ and accounting for 88% (vs. 92% as at FY 16) of its aggregate debt position.
  - Though, 2017 EPS is the strongest on record, Nestle Nigeria gross margin (41.3% in FY 17), is yet to recover to pre-recession average levels of 43%. The company sources 80% of its raw materials locally which exposed it to high domestic food inflation particularly for Maize (+25% YoY) and Sorghum (+38% YoY) following a deficit of these commodities in domestic markets. The foregoing applied upward pressure on COGS (+34.4% YoY) to which Nestle Nigeria effected price increases across its products portfolio in a bid to protect gross margin. The increase in product pricing largely explains the 34.2% YoY increase in FY 17 revenue, however, in our view, pricing came short of the surge in raw materials prices as gross margin contracted 9bps over 2017. Nevertheless, contraction (-190bps) in operating expenses to sales ratio underpinned by cost reduction initiatives neutered the weakness from gross margin to drive a 181bps expansion in operating margin to 22.8%.
  - Currently, NESTLE trades at a P/E of 32.9x compared to Bloomberg Middle and East Africa Peers at 36.9x. Our model is under review.
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## Summary of Results and Forecast

Income statement – (N'million)	Q4 17	Q4 16	YoY growth	QoQ growth	Deviation from forecast	FY 17	FY 16	YoY growth
<b>Revenue</b>	<b>58,909</b>	52,429	12.4%	-7.0%	<b>10.1%</b>	<b>244,151</b>	<b>181,911</b>	34.2%
<b>Cost of sales</b>	<b>33,918</b>	<b>29,034</b>	16.8%	-5.2%	<b>7.5%</b>	<b>143,280</b>	<b>106,583</b>	34.4%
<b>Gross profit</b>	<b>24,991</b>	23,394	6.8%	-9.2%	<b>13.7%</b>	<b>100,871</b>	75,328	33.9%
<b>Operating expenses</b>	<b>12,378</b>	<b>10,551</b>	17.3%	11.0%	<b>-6.5%</b>	<b>45,173</b>	<b>37,114</b>	21.7%
<b>Operating profit</b>	<b>12,613</b>	12,843	-1.8%	-23.0%	<b>33.5%</b>	<b>55,698</b>	38,213	45.8%
<b>Net interest expense</b>	<b>-263</b>	3,201	-108.2%	-95.9%	<b>532.8%</b>	<b>8,870</b>	<b>16,665</b>	-46.8%
<b>PBT</b>	<b>12,350</b>	16,044	-23.0%	23.3%	<b>22.9%</b>	<b>46,829</b>	13,623	243.7%
<b>PAT</b>	<b>10,744</b>	7,440	44.4%	67.0%	<b>0.4%</b>	<b>33,724</b>	7,925	325.5%

Key Ratios	Q4 17	Q4 16	Change(pps)	FY 17	FY 16	Change(pps)
<b>Gross margins</b>	42.4%	44.6%	-2.2%	41.3%	41.4%	-0.1%
<b>EBIT margins</b>	21.4%	24.5%	-3.1%	22.8%	21.0%	1.8%
<b>PBT margins</b>	21.0%	30.6%	-9.6%	19.2%	11.8%	7.3%
<b>PAT margins</b>	18.2%	14.2%	4.0%	13.8%	4.4%	9.5%
<b>Effective tax rates</b>	13.0%	53.6%	-40.6%	28.0%	63.2%	-35.2%

Source: ARM Research \*unless otherwise stated

**Ratings, Disclosure & Disclaimer** – [Click here](#)