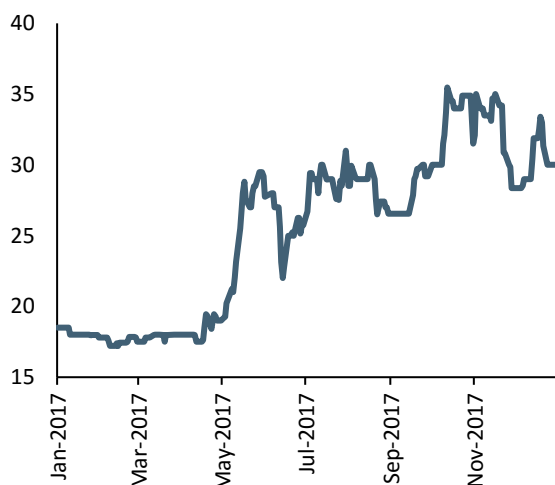


Rating	SELL
Price	₦128
FVE	₦121.30
52-week range	₦112- ₦193
Market Cap. (₦bn)	1,014
1-month Avg. Vol	341,399
Curr. PE	28.4x

Quarterly EPS	Q1	Q2	Q3	Q4
2016 A	1.32	1.09	0.13	1.05
2017 A	1.44	1.55	0.03	1.13
2018 F	1.41	1.64	0.61	1.69

NB:NL - Share Price Trend



Analyst(s)

Feyisike Ilemore
oluwafeyisike.ilemore@arm.com.ng

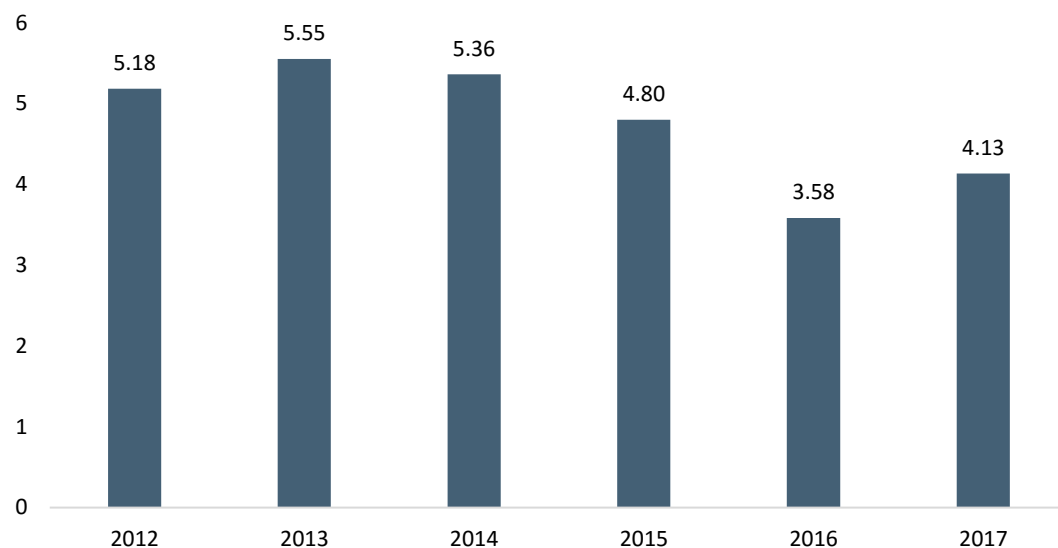
Nigerian Breweries Plc. (NB.NL)

Stock Report

Stock is expensive right now

- Last week, Management of Nigerian Breweries (NB) hosted a conference call to discuss its FY 2017 results as well as provide its outlook for 2018. In this note, we update our views on NB following the FY 2017 results and revise our 2018 forecasts to ascertain if there is still any upside potential for the stock.
- After touching a seven-month low in 2016 (~~₦28.4~~ billion), earnings recovered in 2017, rising 16.2% YoY to ~~₦33~~ billion underpinned by an improvement in the operating environment relative to the prior year. However, earnings remained below pre-2016 trend level due to sustained weak consumer income and increased industry competition.
- Notably, constrained consumer income adversely impacted on volumes with the company reporting a mid-single digit decline in sales volume over 2017. Precisely, management noted slight loss of market share in the review period on the back of strong price increases at the tail end of 2016 which was not implemented immediately by competition. In addition, NB's parent company – Heineken – noted that consumer downtrading impacted negatively on sales for its premium brands while value brands continued to outperform the broader portfolio. Irrespective, revenue over 2017 rose 9.8% YoY to ~~₦344.5~~ billion, underpinned by higher YoY prices.

Figure1: Trend in Nigerian Breweries EPS



Source: Company Financials, ARM Research

- **Cost pressures prevail in the quarter:** Input cost pressures lingered in 2017 which drove a faster increase (+12.8% YoY) in Cost of Goods Sold (COGS) than revenue (+9.8% YoY). At the conference call, management explained that the pressure on COGS reflected higher domestic inflation. NB sources around 50% of its raw materials locally (Sorghum, Sugar and Cassava starch) which exposed the company to rising local prices. Precisely, the price of Sorghum rose 32% YoY which, we believe, impacted on COGS. Against this backdrop, gross margin contracted 153bps to 41.7%. In our view, the switch in FX sourcing to the NAFEX window from NIFEX also impacted on COGS. Irrespective, lower net finance expense (-21.9% YoY to ₦10.7 billion) masked the impact of top-line pressures on core earnings. The decline in finance expense stemmed from a substantial drop (-33.4% YoY to ₦5.0 billion) in foreign exchange losses due to currency stability over 2017.

Other key highlights from the call

- **Consumer downtrading:** Management stated that the pace of consumer downtrading slowed in the second half of 2017. Consequently, volumes were better in the second half when compared to the first with its international premium brand – Heineken – returning back to growth.
- **New product:** In December 2017, Nigerian Breweries introduced a new lager brand – Stella beer – in a 60cl bottle across four key regions in Nigeria. Stella Beer is an international brand at a price point in the premium segment. According to management, initial feedback on the product was encouraging.

-
- ***Changes to the excise duty rate:*** Management acknowledged that the government is proposing to make changes to the excise duty rate. NB mentioned that the government plans to change the structure of excise duties to a specific model (wherein tax is levied on volumes sold) from an ad valorem tax model which basically charges a rate (currently 20%) on production costs. According to management, the policy decision is positive for the brewery industry as the specific model is more efficient, transparent and easily administered. However, the company further stated that the implementation would have a negative impact on COGS and looks to pass on the increase to consumers in a more efficient manner.
 - ***Sales growth momentum set to moderate:*** In 2018, strategies to drive volume induced revenue growth seems to be the focus of management even as we envisage limited price increases in the year. Management plans to achieve volume growth via leveraging on its strong distribution network as well as increasing availability of products amidst rising industry competition. While we acknowledge these initiatives, we do not expect to see a sharp increase in revenue given that the operating environment remains challenging. In addition, the country's exit from recession is yet to translate to a sizeable improvement in consumer wallets which also guides to a slow rebound in sales volume. Against these backdrop, we forecast a modest increase in revenue (+3.5% YoY to ₦356.6 billion) in 2018.
 - We forecast COGS to rise 3.8% YoY to ₦208.6 billion to capture the impact of increasing cost of key raw materials including Sorghum and Barley. This, combined with our revenue expectation translates to a 3.1% YoY increase in gross profit to ₦148 billion which should see gross margin decline 16bps YoY to 41.5% (FY 17: 41.7%). Similarly, we forecast operating costs to rise modestly by 2.6% YoY to ₦90.9 billion, driven by a slight increase in marketing and distribution expenses (+2.9% YoY) to capture the company's plan to drive visibility and availability of its products. The foregoing translates to EBIT of ₦57.1 billion (+3.9% YoY) with related margin forecasted to increase 7bps to 16.0%.
 - In view of our expectations for ongoing currency stability, we foresee lower FX losses in 2018. This, coupled with the low yield environment underpins our forecast of 2018 finance expense at ₦6.5 billion (-38.9% YoY). Net impact of our model revisions translates to PBT and PAT of ₦51.5 billion (+10.5% YoY) and ₦36.1 billion (+9.12% YoY) respectively.
 - Nigerian Breweries trades at a forward P/E of 28.4x vs. 32.9x for Bloomberg Middle East and Africa. NB has declined 5.1% YTD relative to a positive return of 10.2% for the NGSE INDX. We retain our SELL recommendation on the stock with a FVE of ₦121.30.
-

Summary of Results and Forecasts - Naira (₦)

ANNUAL					
Income Statement (₦'m) *	2016A	2017A	2018F	2019F	2020F
Revenue	313,743	344,563	356,622	374,453	393,176
COGS	178,219	201,013	208,624	213,438	216,247
Gross Profit	135,525	143,549	147,998	161,015	176,929
Operating Cost	83,237	88,647	90,939	91,741	96,328
Operating Profit	52,903	57,121	57,773	71,146	81,781
Interest Expense	13,229	10,491	6,232	1,483	1,622
PBT	39,675	46,630	51,541	69,663	80,158
Tax	11,258	13,581	15,462	21,595	25,651
PAT	28,417	33,049	36,079	48,067	54,508
Balance Sheet (₦ '000) *					
Fixed Assets	191,182	195,230	198,352	199,217	199,660
Stocks	31,245	42,729	40,682	41,620	38,924
Trade debtors	19,974	20,384	21,041	22,093	19,659
Cash & other bank balances	12,156	15,867	12,813	14,660	14,350
Total Assets	367,146	382,228	380,910	385,636	380,654
Liabilities					
Trade Creditors	111,184	127,947	125,174	128,063	121,098
Non-current Liabilities	56,978	47,877	49,308	51,121	53,077
Total liabilities	201,233	203,930	202,611	207,338	202,355
Shareholders' fund	165,914	178,298	178,298	178,298	178,298
Key Ratios	2014A	2015A	2016A	2017E	2018E
Gross Margin	43%	42%	42%	43%	45%
EBIT Margin	17%	17%	16%	19%	21%
PBT Margin	13%	14%	14%	19%	20%
Net Margin	9%	10%	10%	13%	14%
EPS	3.6	4.13	4.5	6.0	6.8
P/E	42.4	31.7	29.0	21.8	19.2
P/B	7.3	5.8	5.9	5.9	5.9
EV/EBITDA	14.9	11.6	12.3	10.6	9.4
ROA	8%	9%	9%	13%	14%
ROE	17%	19%	20%	27%	30%

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