



Rating	SELL
Price	₦12.55
FVE	₦10.12
52-week range	₦12.50-₦27.30
Market Cap. (₦'bn)	49.83
1-month Avg. Vol	171,288
Curr. PE	11.9x

Quarterly EPS	Q1	Q2	Q3	Q4
2017 A	0.40	0.33	0.48	0.53
2018 A	0.03	0.18	0.19	0.15
2019 A (E*)	0.05	0.13*	0.23*	0.19*

PZ:NL - Share Price Trend



Analyst(s)

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PZ Cussons Nigeria Plc. (PZ.NL)

Stock Report

Sluggish Outlook takes a toll on valuation

- PZ Cussons Nigeria (PZ) reported loss after tax of ₦204 million in its FQ1 19 numbers (FQ1 18: Loss after tax of ₦123 million). The dismal performance stemmed from weakness in its business operation, as the company reported a slump in revenue (-15.9% YoY to ₦15.9 billion), slower decline in cost of sales (-12% YoY to ₦11.4 billion) which combined led operating margin to contract 738bps to 2.4%. We highlight the positive of a 62.7% YoY decline in foreign exchange losses to ₦668 million.
- For the rest of FY 19, we expect the company to return to profit based on our expectation of sturdier revenues in subsequent quarters, as the company enters its peak seasons. However, overall FY 19 should come in weaker than the prior year, as we expect the company to continue to face volume pressures from weak consumer wallets and imported competition. Thus, we forecast revenue of ₦74.9 billion (-7% YoY). Additionally, we believe the company's product portfolio lacks sufficient products that are strong leaders in their category and thus see new exciting product innovations as an upside to revenue. Elsewhere, despite lower Crude Palm Oil (CPO) and stable foreign exchange, we forecast cost of sales to fall slower by 5.2% YoY due to rising Brent Crude price (+50.4% YoY) which should translate into higher petrochemical prices for the company and pressure cost of sales. Overall, we forecast FY 19 earnings at ₦1.95 billion, translating to an EPS of ₦0.49 (+1.3% YoY). Over our forecast horizon, we have cut our EPS forecast by an average of 22% owing to the slow recovery in topline. We have a FVE of ₦10.12 (previous: ₦16.57) which translates to a **SELL** rating based on PZ last trade price.

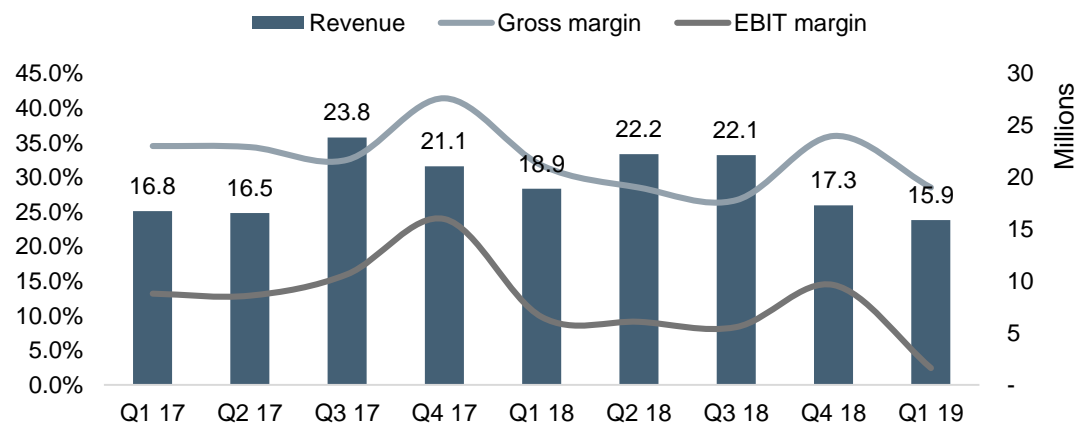
No respite yet for revenue

- On revenue, the parent company in its group's FQ1 18 trading statement attributed the decline in Nigerian sales to weak consumer disposable income and pressured prices. With foreign exchange more available than a year ago, we think PZ's volumes was pressured by imported competition which might have led the company to lower product prices in a bid to drive sales. Despite weaker revenue of 15.9%, cost sales declined slower by 12%, as the company continued to face cost inflation. With global and domestic Crude Palm Oil prices down 16% and 6% respectively, and FX more available and stable, we look to higher petrochemical prices as the probable pressure point on cost of sales. Precisely, over the review period, Brent crude was higher 50%, indicating higher petrochemical prices over the period. As a result, gross margin contracted 319bps to 28.5%. To add, we suspect a change in its product mix from higher margin to lower margin brands (due to repacking into smaller economy products) impacted on its gross margin.

FX losses moderates further

- Foreign exchange losses moderated further in FQ1 19, down 62.7% YoY to ₦668 million. As at FY 18 (ended May), the group moved from translating its balance sheets from the CBN rate (₦305/\$) to the NIFEX exchange rate – which averaged ₦337.84/\$ in its fourth quarter of the 2018 fiscal year. However, the NIFEX has depreciated 3.1% to ₦357.6/\$ between August and May which couple with the settlement of some of its FCY related party trade payables (₦4.3 billion equivalent) at the prevailing rate ~₦360/\$ prompted the FX losses reported in the review period.

Figure 1: Trend in historical gross and EBIT margin



Source: Company Report

Modest earnings growth driven by lower FX losses

- Although PZ started its fiscal year with a loss, we expect the company to return to profit based on our expectation of sturdier revenues in subsequent quarters, as the company enters into its peak seasons. On revenue, the parent company stated that the Nigerian division is focusing on optimizing price points and size across the key brands in its portfolio to support revenue. Irrespective, with tough market conditions and slow recovery in consumer wallets, we expect revenue to remain relatively weaker in FY 19 and thus, project a 4.8% YoY decline in revenue to ₦76.6 billion.
 - On cost of sales, despite lower CPO prices – which we expect to contract further on supply overhang in international markets – we expect input cost pressures to persist due to the sustained rise in Brent crude, and by extension, petrochemical prices. Owing to this, we forecast cost of sales to decline by 3% YoY to ₦54 billion. This combined with our FY 19 operating expenses forecast of ₦16.9 billion (+3.9% YoY) translates to an EBIT of ₦5.5 billion (-34% YoY) and related margin of 7.2% (-317bps). EBIT margin of 7.2% for FY 19 is lower than PZ's 5-year historical average of 11%.
 - On foreign exchange losses, we believe PZ's FCY liabilities was translated at an average NIFEX rate of ₦348.51/\$ as at FQ1 19. However, since the end of PZ's first quarter, the NIFEX rate has depreciated 3% to ₦359.61/\$ to converge with the NAFEX rate. Given this, as well as its outstanding related party payables of ₦27 billion (which we expect will be paid in FY 19), we foresee further FX losses in the subsequent quarter, although projected to slowdown in FH2 19 – as we expect the company's balance sheet to be translated at a rate of ~₦360/\$ over the second half of 2019. Overall, we forecast FX losses of ₦2.2 billion (-60% YoY) over FY 19.
 - Largely on account of lower foreign exchange losses, we project PZ's earnings in FY 19 to grow 5.7% YoY to ₦2.0 billion, translating to an EPS of ₦0.51. We have a FVE of ₦10.12 (previous: ₦16.57) which translates to a SELL rating based on PZ last trade price. On our numbers, PZ trades at a P/E and EV/EBITDA of 25.6x and 4.9x compared to Bloomberg MENA peer average of 19.8x and 10.8x respectively.
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Summary of Results and Forecasts - Naira (₦)

ANNUAL					
Income Statement (₦' m) *	2016A	2017A	2018A	2019E	2020E
Revenue	69,528	78,216	80,553	76,669	78,510
COGS	49,326	50,268	56,097	54,435	55,742
Gross Profit	20,201	27,948	24,456	22,234	22,768
Operating Cost	14,068	14,733	16,228	16,867	17,665
Operating Profit	6,419	13,414	8,357	5,520	5,260
Interest Income	598	290	832	470	508
Interest Expense	210	486	181	193	132
PBT	3,148	4,811	2,314	3,086	4,884
Tax	1,019	1,125	386	1,049	1,563
PAT	2,130	3,687	1,927	2,037	3,321
Balance Sheet (₦ '000) *					
Fixed Assets	26,505	28,514	28,430	29,223	30,025
Stocks	19,278	26,710	26,040	28,306	26,756
Trade debtors	15,587	17,222	15,053	14,567	14,917
Cash & other bank balances	12,868	8,022	14,260	12,041	16,506
Total Assets	74,430	90,088	88,616	88,948	91,538
Liabilities					
Trade Creditors	25,716	39,723	40,205	39,193	40,134
Non-current Liabilities	3,932	2,584	2,525	2,547	2,582
Total liabilities	31,027	44,950	43,507	42,903	43,832
Shareholders' fund	43,403	45,138	45,109	46,046	47,706
Key Ratios	2016A	2017A	2018A	2019E	2020E
Gross Margin	29.1%	35.7%	30.4%	29.0%	29.0%
EBIT Margin	9.2%	17.1%	10.4%	7.2%	6.7%
PBT Margin	4.5%	6.2%	2.9%	4.0%	6.2%
Net Margin	3.1%	4.7%	2.4%	2.7%	4.2%
EPS	0.47	0.84	0.49	0.51	0.73
P/E	46.16	22.34	46.36	43.86	30.92
EV/EBITDA	8.83	4.40	7.16	10.35	10.03
ROA	3.0%	4.5%	2.2%	2.3%	3.7%
ROE	4.9%	8.3%	4.3%	4.5%	7.1%

Source: ARM Research *unless otherwise stated

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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