

Unilever Nigeria Plc. (Unilever.NL)

Stock Report

We downgrade to an “Overweight” rating

• Unilever performance over 2018, largely reflected the intense cross product competition in the home and personal care (HPC) segment, coupled with pressure from its input cost and operating expenses. For context, while revenue grew 9% YoY, input cost rose 12% YoY to necessitate gross margin contraction by 191bps YoY to 30.4%. Furthermore, with operating expense surging 24% YoY, emanating from higher marketing and distribution spend, EBIT margin contracted to 9.9% (-450bps YoY). Nonetheless, following strong net finance income of ₦3.4 billion (+157% YoY) booked during the year compared to net expense of ₦1.6 billion in FY 17, the company was able to grow its earnings by 29% YoY to ₦9.1 billion (excl. spread business). Mirroring the impact of the additional shares issued during the year, EPS came in lower by 6% YoY to ₦1.59. Adjusted for the discontinued operation (wherein the company recorded gain after tax of ₦1.4 billion on the sale of its spread business), total FY 18 EPS expanded 9% YoY to ₦1.84. The company declared dividend of ₦1.50 (FY 17: ₦0.50), which on current pricing translates to dividend yield of 4.2%.

• With the subsisting competition in the HPC segment, we cut our FY 19E revenue estimate to ₦99.4 billion (prior: ₦110.9 billion) with average growth estimate over 2019F to 2023F revised lower to 6% (previously: 9%). Reflecting the higher marketing spend in FY 19, we leave our expectation on operating expense (Opex to sales at 20%) unchanged. With the still strong cash position as at FY 18 of ₦57.1 billion, we model strong gains on finance income over FY 19. On the bright side, our expectation of a downward movement in petrochemical prices guides our view of an expansion in gross margin to 31.5% (FY 18: 30.4%).

Rating	OVERWEIGHT
Price	₦35.70
FVE	₦41.94
52-week range	₦33.5-₦59.8
Market Cap. (₦'bn)	300,562
1-month Avg. Vol	468,367
Curr. PE	19.2x

Quarterly EPS	Q1	Q2	Q3	Q4
2017 A	0.42	0.55	0.31	0.27
2018 A	0.50	0.49	0.32	0.33
2019 (E*)	0.45	0.41	0.38	0.49

Unilever: NL - Share Price Trend



Analyst(s)

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- Following the above revisions, we downgrade our rating on Unilever to **OVERWEIGHT** (Previously: BUY), with a revised FVE of **₹41.94** (previously: ₹49.19).
 - **Impressive growth in its Food business:** Over 2018, revenue expanded 9% YoY to ₹92.9 billion with support largely stemming from the food business – which recorded double digit growth. The HPC segment however dragged, expanding by just 1% YoY following incessant competition from “**So klin**”, “**Good Mama**” and “**Ariel**” brand. From our interactions with market stakeholders, we were made to understand that demand for Unilever’s “**Sunlight and OMO**” **brand** dropped over the review period, with competing products gathering more market share in recent times. Over 2019, while growth in the food segment is expected to remain strong with double-digit growth, we remain pessimistic on the HPC segment as competition is likely to persist through the year. That said, we expect moderate revenue growth of 7% YoY to ₹99.4 billion.
 - **Cost pressures to moderate:** Over 2019, our expectation of moderation in petrochemical prices guides to expansion in gross margin by 112bps YoY to 31.5%, albeit lower than the five-year historical average of 32.7%. Furthermore, given the increase in operating expense over 2018 emanated from recurring items (staff expense: +32% YoY, IT: +3.3x and marketing: +23% YoY), we left our opex to sales ratio unchanged at 20%. Nonetheless, we expect the stronger gross margin to support expansion in FY 19E EBIT margin by 220bps YoY to 12.1%.
 - Elsewhere, the company ended the year with a cash balance of ₹57.1 billion (+13.2% YoY) which guides our expectation of strong finance income over 2019. Amidst low leverage, with equity multiplier at historical low levels (FY 18: 1.6x), we expect stronger net finance income which translates to higher PBT of ₹16.3 billion (+29.4% YoY) and PAT settling at ₹11.3 billion (+23.4% YoY). That said 2019 EPS is expected to print at ₹1.96.
 - Unilever trades at a FY 19E P/E of 21.2x, compared to Bloomberg MENA peer average of 20.4x. At current price, our expected dividend of ₹1.57 (with a payout ratio of 80%) over FY 19E translates to a dividend yield of 4.5%.
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Summary of Results and Forecasts - Naira (₦)

ANNUAL					
Income Statement (₦'m) *	2017A	2018E	2019F	2020F	2021F
Revenue	85,193	92,900	99,377	106,004	110,805
COGS	57,679	64,675	68,073	72,613	74,240
Gross Profit	27,514	28,225	31,304	33,391	36,566
Operating Cost	15,267	18,952	19,447	20,744	21,780
Operating Profit	12,231	9,198	12,056	12,701	14,848
Interest Income	1,565	4,027	4,902	4,692	1,980
Interest Expense	-3,201	-603	-183	-183	-238
PBT	10,596	12,622	16,775	17,210	16,590
Tax	3,526	3,490	5,200	5,335	5,143
PAT	7,070	9,132	11,575	11,875	11,447
Balance Sheet (₦ '000) *					
Fixed Assets	29,881	29,678	29,944	69,052	68,104
Stocks	11,479	13,929	13,681	14,593	14,920
Trade debtors	27,621	30,188	41,738	50,882	53,187
Liabilities					
Trade Creditors	33,409	38,611	34,037	36,307	37,120
Non-current Liabilities	8,481	5,887	8,506	9,026	9,527
Total liabilities	36,695	43,167	39,034	41,302	42,113
Shareholders' fund	75,908	82,790	84,707	87,082	89,372
Key Ratios	2017A	2018E	2019F	2020F	2021F
Gross Margin	32%	30%	32%	32%	33%
EBIT Margin	14%	10%	12%	12%	13%
PBT Margin	12%	14%	17%	16%	15%
Net Margin	8%	10%	12%	11%	10%
EPS	1.69	1.59	2.01	2.07	1.99
P/E	24.23	23.28	20.63	20.11	20.86
EV/EBITDA	7.44	13.15	12.68	14.85	10.50
ROA	7.30%	7.22%	8.77%	8.81%	8.23%
ROE	9.31%	9.31%	11.03%	13.66%	13.64%

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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