



Unilever Nigeria Plc. (UNILEVER.NL)

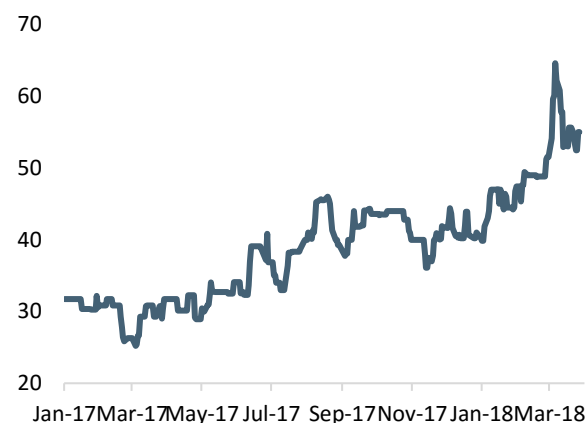
Stock report

Is Unilever topping out?

Rating	SELL
Price	₦53.00
FVE	₦34.30
52-week range	₦28.73-₦65.00
Market Cap. (₦'bn)	304
1-month Avg. Vol	1,850,724
Current PE	25.8x

Quarterly EPS	Q1	Q2	Q3	Q4
2016 A	0.28	0.01	0.12	0.37
2017 A	0.42	0.55	0.30	0.50
2018 A*(E)	0.50*	0.49	0.51	0.55

UNILEVER:NL - Share Price Trend



Analyst(s)

Feyisike Ilemore

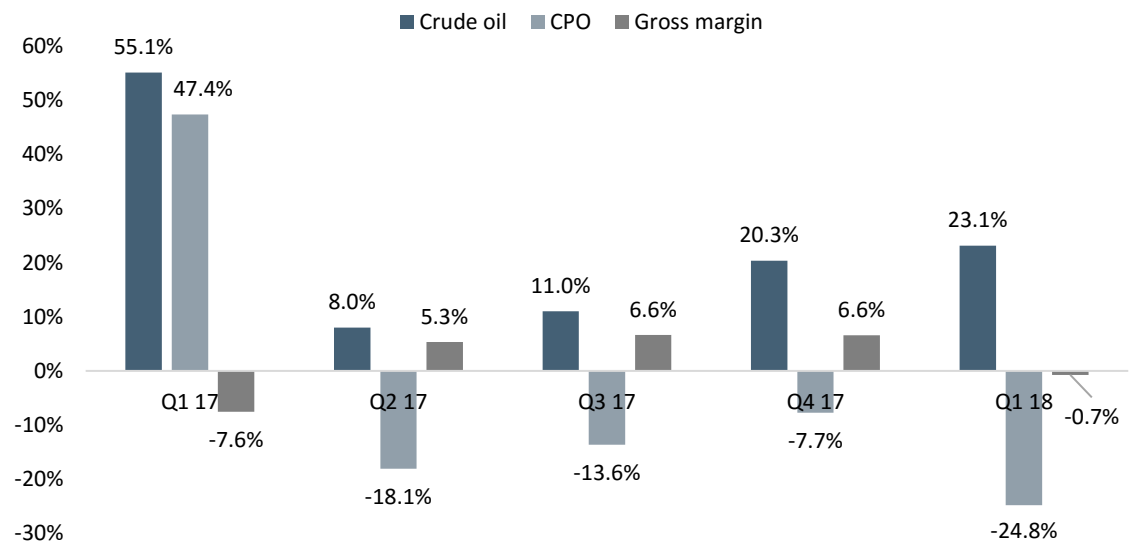
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- Unilever Nigeria Plc (Unilever) began the 2018 financial year positive reporting impressive EPS of ₦0.50 (+19.1% YoY) which was largely in line with our expectation (ARM forecast: ₦0.49). Broadly, earnings growth reflected volume-led revenue growth (+16.4% YoY to ₦25.8 billion) and lower operating expenses to sales ratio (-199bps to 14%) which offset higher cost of sales (+17.6% YoY to ₦18.7 billion) – a reflection of higher petrochemical prices, in our view.
- Going forward, we retain our view that higher petrochemical prices from the sustained rise in Brent price would pose downside risk to Unilever's core earnings. Nevertheless, we see higher finance income and tamer finance expense providing support for earnings and forecast FY 18E after-tax earnings to rise 58.7% YoY to ₦11.8 billion. However, due to the dilutive impact of the additional shares (1.96 billion ordinary shares) from the rights issue in Q3, our EPS translates to ₦2.06 which represents a 15.4% YoY increase from FY 17.
- From all indications, Unilever Nigeria is poised for further earnings recovery in FY 18. However, from a valuation standpoint, we believe the stock is expensive with the company trading at a forward P/E of 25.8x vs. 18.9x average for MENA peers. Additionally, on our FY 18 earnings, we expect 2018 ROE to print at 13%, lower than 27% average in the last 5 years which speaks to the idle cash – from the rights issue – on its books that is yet to translate to substantial improvement in earnings. Hence, with our FVE of **₦34.30**, we retain our **SELL** rating on the stock.

Margin expansion and finance income underpins Q1 earnings

- Over Q1 18, Unilever's revenue rose 16.4% YoY to ₦25.8 billion, faster than Q4 17 YoY growth of 8.7%. By our price checks, average product pricing was higher ~4% YoY, as such, we attribute the growth in revenue to higher volumes. In our view, the growth in volumes speaks to the company's sustained investment in its route-to-market strategy to drive volumes amidst slow recovery in consumer wallets. According to provided breakdown, much of the growth came from the Home and Personal Care (HPC) segment which rose 16.8% YoY to ₦13.6 billion and contributed 52.9% to aggregate revenue while the food segment rose 16% YoY to ₦12.2 billion.
- In our report on Unilever Nigeria following the release of its FY 17 results, we explained that the company is set to face input cost pressures in 2018 on the back of rising Brent price which would impact prices of petrochemicals (key input) with an attendant negative impact on Cost of Goods Sold (COGS). In line with our prognosis, despite the recent stability in the Naira and declines in the price of domestic Crude Palm Oil, COGS rose at a faster pace than sales, 17.6% YoY to ₦18.7 billion, most likely reflecting the rise in petrochemicals. Consequently, gross margin contracted 72bps YoY to 27.7% (Q3: 31.3%, Q4: 34.7%) with related profit at ₦7.1 billion. Irrespective, aided by a soft increase in operating expenses owing to lower admin expenses, operating margin firmed up, rising 124bps to 13.7% above the 5-year trend level of 10%.

Figure 1: YoY changes in crude oil, Crude Palm Oil (CPO) and gross margin



Source: Company financial, Bloomberg, World Bank

- Extending what played out in Q4 17, Unilever's earnings enjoyed gains of a rich cash position and tamed leverage. Pertinently, with cash of ₦47.4 billion (Cash at bank: ₦22.6 billion and Fixed deposit: ₦24.9 billion), the company reported finance income of ₦494 million (vs. ₦150 million in Q1 17). Also, given the lower debt position of ₦457 million (vs. ₦25.4 billion as at Q1 17), interest expense declined markedly by 86.4% YoY to ₦98.5 million. Against this backdrop, net finance income over the quarter printed at ₦396 million compared to a net finance expense of ₦575 million in Q1 18.
- Given the above mentioned, before and after-tax earnings printed at ₦3.9 billion (+80% YoY) and ₦2.9 billion (+80.9% YoY). However, EPS printed at ₦0.50 representing a 19.1% YoY increase from ₦0.42 in Q1 17, due to share dilution.

Further earnings improvement anticipated in FY 18

- Over the rest of the year, we expect revenue to come in stronger relative to 2017 largely driven by volumes. As such, we have revised our FY 18E revenue higher by 6.5% to ₦104.5 billion (+15.1% YoY). Despite the downturn in the price of CPO, the sustained upsurge in the price of crude oil guides to further pressures on COGS. Hence, we have revised our FY 18E cost of sales higher by 9.7% to ₦72.3 billion (+17.0% YoY). Accordingly, we project gross profit to rise 11.2% YoY to ₦32.2 billion with a 109bps contraction in related margin to 30.8% (vs. 5-year average of 35%).
- We have revised our operating expenses higher by 10.6% to ₦17.0 billion to capture expected increases in selling, distribution and admin expenses. Against this backdrop, we forecast operating margin to expand 25bps to 14.5% which is higher than 5-year average level of 10.4%.
- With the company's cash position remaining buoyant, we expect finance income for the year to print at ₦2.5 billion, representing a 51% YoY increase from the prior year. Similarly, given the company's soft leverage, we forecast finance expense to print at ₦305 million (vs. ₦3.4 billion in FY 17). The combination of our forecast finance income and expense translate to a net finance income of ₦2.2 billion (vs. ₦1.7 billion net finance expense). Overall, net impact of our model revisions translates to a PBT and PAT of ₦17.4 billion (+55% YoY) and ₦11.8 billion (+58.7% YoY) respectively.
- From all indications, Unilever Nigeria is poised for further earnings recovery in FY 18 although, stemming more from moderated finance expense. However, from a valuation standpoint, we believe the stock remains expensive with the company trading a P/E of 25.8x

vs. 18.9x average for MENA peers. Additionally, on our FY 18 earnings, we expect 2018 return on equity to print at 13%, lower than 27% average in the last 5 years which speaks to the idle cash on its books that is yet to translate to substantial improvement in earnings. Hence, with our FVE of ~~₦34.30~~, we retain our **SELL** rating on the stock.

Summary of Results and Forecasts - Naira (₦)

ANNUAL					
Income Statement (₦' m) *	2016A	2017A	2018E	2019F	2020F
Revenue	69,777	90,771	104,513	108,412	112,457
COGS	49,481	61,828	72,323	72,094	74,222
Gross Profit	20,296	28,943	32,190	36,318	38,236
Operating Cost	14,615	15,976	17,036	19,948	21,142
Operating Profit	5,805	12,950	15,175	16,424	17,150
Net finance Cost	(1,699)	(1,743)	2,213	2,626	2,382
PBT	4,106	11,207	17,389	19,050	19,532
Tax	1,035	3,757	5,564	6,096	6,250
PAT	3,072	7,450	11,824	12,954	13,282
Balance Sheet (₦ '000) *					
Fixed Assets	29,272	29,881	31,448	35,768	40,139
Stocks	9,878	11,479	14,465	14,419	14,844
Trade debtors	18,946	27,621	31,354	32,524	33,737
Cash & other bank balances	12,474	50,494	58,551	63,917	70,290
Total Assets	72,491	121,084	137,428	148,238	160,621
Liabilities					
Trade Creditors	32,477	33,409	39,778	39,652	40,822
Non-current Liabilities	7,288	8,481	9,006	9,581	10,170
Total liabilities	53,513	36,695	43,054	42,926	44,094
Shareholders' fund	11,690	75,908	85,368	95,731	106,357
Key Ratios	2016A	2017A	2018E	2019F	2020F
Gross Margin	29.1%	31.9%	30.8%	33.5%	34.0%
EBIT Margin	5.9%	12.3%	16.6%	17.6%	17.4%
PBT Margin	8.3%	14.3%	14.5%	15.2%	15.3%
Net Margin	4.4%	8.2%	11.3%	11.9%	11.8%
EPS	0.81	1.78	2.06	2.25	2.31
P/E	67.74	30.85	26.72	24.39	23.79
EV/EBITDA	26.67	10.56	15.91	14.42	13.39
ROA	5.0%	7.7%	9.1%	9.1%	8.6%
ROE	26.3%	9.8%	13.9%	13.5%	12.5%

Source: ARM Research *unless otherwise stated

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