

Guinness Nigeria Plc

Nigeria | Equities | Breweries | September 16, 2015

PAC RESEARCH

New product innovation boosts revenue

Revenue improves by 8.5% year-on-year and 14.5% quarter-on-quarter. In its audited results for full year to June 2015, Guinness Nigeria recorded revenue of ₦118.50billion, up by 8.5% compared with ₦109.20billion in the previous period. In our view, the improvement in revenue was due to the benefits of successful products innovations launched by the company in the previous year such as **Orijin Bitters** and **Orijin Ready-to-Drink**. On a quarterly basis, the company's revenue of ₦33.75billion in the fourth quarter to June 2015 improved by 14.5% and 8.2% compared with ₦29.48billion and ₦31.18billion respectively in the third quarter to March 2015 and the fourth quarter to June 2014.

Gross profit improves on the back of lower increase in input costs.

The company's cost of sales (COS) of ₦62.60billion in the review period increased by 8.2% against ₦57.87billion in the previous year. The lower increase in the COS relative to the increase in revenue resulted in a lower COS/revenue ratio of 52.8% compared with 53.0% in the previous year. Furthermore, the COS of ₦17.59billion posted in 4Q2014/15 was higher by 13.5% and 8.6% compared with ₦15.50billion and ₦16.19billion respectively in 3Q2014/15 and 4Q2013/14; also the latest quarter's COS is higher than 8-quarter average of ₦15.06billion by 16.8%. In addition, our analysis revealed that the COS/revenue ratio of 52.1% in the latest quarter is lower than both 52.6% in 3Q2014/15 and the 8-quarter average of 52.8% but higher than 51.9% in 4Q2013/14. Therefore, gross profit increased by 8.9% y/y to ₦55.89billion against ₦51.33billion in the previous period, and gross profit margin improved marginally to 47.2% relative to 47.0% in the preceding year.

Estimated decline in the prices of grains is expected to improve gross profit margins. Moreover, the prices of grains which are major input in the processing of both alcoholic and non-alcoholic beverages have been on a downward trend in the past two years in line with the prices of other agricultural commodities.

Fig. 1: Quarterly results highlights

	4Q2015	3Q2015	4Q2014	Q/q Δ	Y/y Δ
Revenue (₦mn)	33,746	29,483	31,183	+14.46%	+8.22%
Operating profit (₦mn)	4,905	3,061	5,284	+60.24%	-7.17%
Net profit (₦mn)	2,579	1,817	3,630	+41.94%	-28.95%

Source: NSE, PAC Research

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Price:

- Current	₦155.23*
- Target	₦155.45
Recommendation:	HOLD

* As at Wednesday September 16, 2015

Fig. 2: Stock data

FYE	June
Price Mov't: YtD / 52wk	-3.39%/-5.55%
52-week range	₦106.00 - ₦214.98
Average daily vol./val.	543,719 / ₦80.429mn
Shares Outstanding (mn)	1,506
Market Cap. (₦mn)	244,631 (\$1,241mn)
EPS, ₦- 12months trailing	5.18
DPS, ₦- FY2014/15	3.20
FCFPS, ₦- FY2014/15	n/a

Source: NSE, Company's Annual Reports, PAC Research

Fig. 3: Key ratios

	FY2015	FY2014
Gross profit margin	47.17%	47.01%
Net profit margin	6.58%	8.77%
Equity multiplier	2.53x	2.94x
Asset turnover	0.97x	0.82x

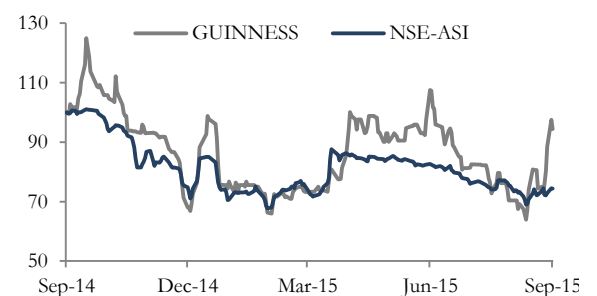
Source: NSE, PAC Research

Fig. 4: Valuations

	FY2015	FY2016E	FY2017F	FY2018F
P/Sales	1.93x	1.88x	1.84x	1.82x
P/E	29.40x	22.71x	22.76x	22.65x
PEG	n/a	n/a	5.69	11.33
EV/Sales	1.93x	1.88x	1.84x	1.82x
P/B	4.74x	4.37x	4.06x	3.81x
ROE	16.13%	19.25%	17.84%	16.84%
ROA	6.38%	8.15%	8.00%	7.91%
Div. Yield	2.10%	2.63%	2.63%	2.83%

Source: NSE, PAC Research

Fig. 5: Guinness vs. NSE, 52-wk movement (rebased)

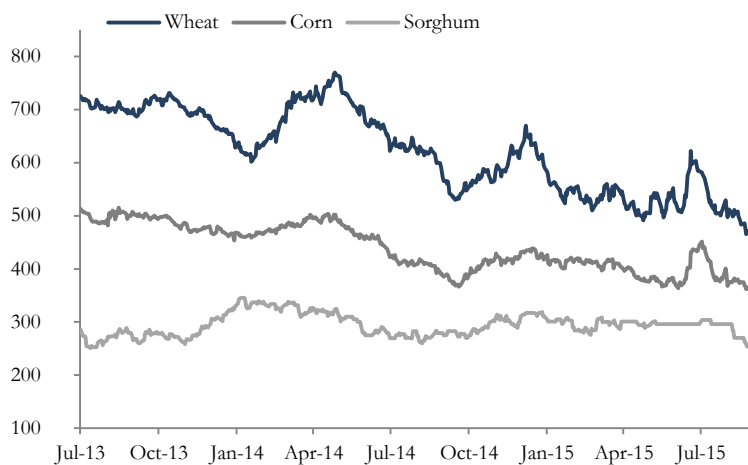


Source: Bloomberg, PAC Research

For example, in the review period the average prices of wheat and corn declined by 18.0% and 16.3% respectively to US\$569/bsh and US\$404/bsh compared with US\$695/bsh and US\$482/bsh in the previous period. Also, the average prices of sorghum declined by 2.0% to US\$291/bsh against US\$297/bsh in the preceding period. Significant decline in prices in the grain market is expected in the remaining part of 2015 due to bumper harvests in the U.S. and the E.U. for wheat and maize, and strong exports for rice from Thailand are expected to keep downward pressure on prices. However, the underline risk to the forecast of bumper harvests is the likelihood of unfavourable weather that could undermine the output of several agricultural commodities. Regardless, the Economic Intelligence Unit (EIU) projected an average decline of 17.7% in the prices of grains in 2015 relative to the previous year. Therefore, profit margins of Guinness Nigeria are expected to improve in the quarters ahead if the management can restrain the growth of running costs.

“ Significant decline in prices in the grain market is expected in the remaining part of 2015 due to bumper harvests in the U.S. and the E.U.... ”

Fig. 6: Prices of grains (US\$/bsh)



Source: Bloomberg, PAC Research

Operating profit margin fell on the back of increase in running costs.

For the review year, the company's operating expenses of ₦40.95billion was up by 13.9% compared with ₦35.94billion in the preceding year. The higher increase in the operating expenses relative to revenue resulted in a higher operating expenses/revenue ratio of 34.6% relative to 32.9% in the previous year. On a quarterly basis, Guinness Nigeria's operating expenses of ₦11.25billion in the fourth quarter to June 2015 was up by 6.9% and 19.1%, compared with ₦10.53billion and ₦9.45billion accordingly in the third quarter to March 2015 and the fourth quarter to June 2014. Also, it is higher than 8-quarter average of ₦9.61billion by 17.1%. Furthermore, the company's operating expenses/revenue ratio of 33.3% in the latest quarter is lower than both 35.7% in 3Q2014/15 and 8-quarter average of 34.0% but higher than 30.3% in 4Q2013/14.

Overall, total costs increased by 10.4% y/y to ₦103.55billion compared with ₦93.81billion in the corresponding period of the preceding year, and total cost/revenue ratio increased to 87.4% relative to 85.9% in the immediate past year. Therefore, operating profit declined by 2.9% to ₦14.95billion compared with ₦15.39billion in 2014/15, and operating profit margin fell to 12.6% relative to 14.1% in the previous year. Contrary to expectation, interest expenses rose by 9.7% to ₦4.87billion against ₦4.44billion in the past year, despite the fact that total financial liabilities declined by 37.5% to ₦24.59billion compared with ₦39.37billion in the preceding year. Further analysis revealed that bank overdraft stood at ₦12.34billion in June 2015, up by 3.4% y/y against ₦11.94billion while non-current financial liabilities declined by 55.3% to ₦12.25billion compared with ₦27.43billion in 2013/14. Consequently, net profit declined by 18.6% to ₦7.79billion compared with ₦9.57billion in the previous year and net profit margin dipped to 6.6% relative to 8.8% in 2013/14.

Guinness Nigeria out-performs the broad market in the review period.

For the 12 months period to June 2015, the company recorded total shareholders' returns (TSR) of -14.9% relative to -17.5% posted by the equity market in the same period. However, Guinness Nigeria under-performed the market in the corresponding period of the previous year with TSR of -16.1% compared with +16.3% achieved by the market. Also, the company recorded TSR of -3.4% year-to-date compared with -9.2% achieved by the equity market; overall the company under-performed the equity market in a 5-year period with TSR of +12.5% relative to +58.0% recorded by the market.

Fig. 7: Total shareholders' returns

	Guinness Nigeria	Equity market
Year-to-Date	-3.4%	-9.2%
1-year to Jun. '15	-14.9%	-17.5%
1-year to Jun. '14	-16.1%	+16.3%
5-year to Aug. '15	+12.5%	+58.0%

Source: Bloomberg, PAC Research

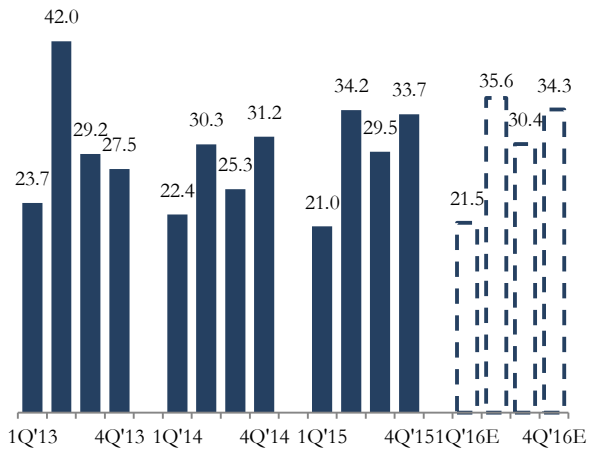
Our valuation puts the target price of the stock of Guinness Nigeria Plc at ₦155.45. In arriving at the target price, we employed multiples of price/earnings, price/sales, price/book, and EV/sales. We also employed the discounted cashflow valuation methodology. Consequently, we recommend a HOLD on the stock of the company.

Our valuation and forecasts considered several factors (both quantitative and qualitative) among which are; the challenging operating environment in Nigeria, the trends in the price of commodities in the global market, insecurity challenges in the northern part of the country, the strength of consumer spending and the intensity of competition in the market.

“ Contrary to expectation, interest expenses rose by 9.7% to ₦4.87billion against ₦4.44billion in the past year...”

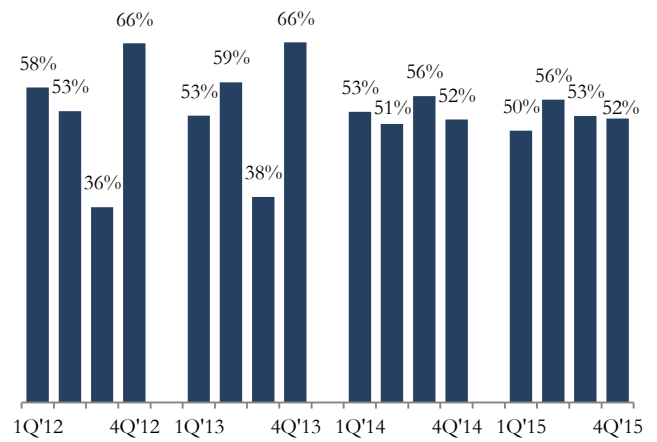
“ Our valuation puts the target price of the stock of Guinness Nigeria Plc at ₦155.45. ”

Fig. 8: Quarterly revenue (₦billion)



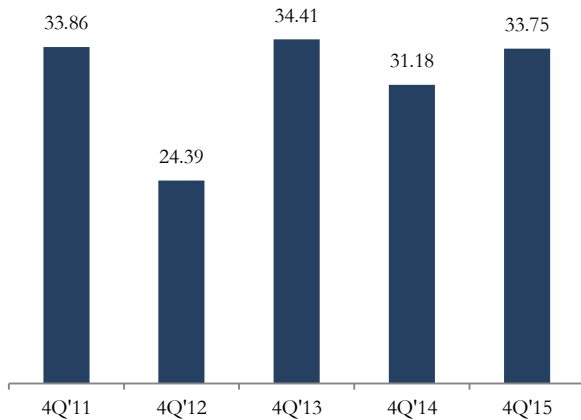
Source: NSE, PAC Research

Fig. 9: Quarterly COS/revenue ratio



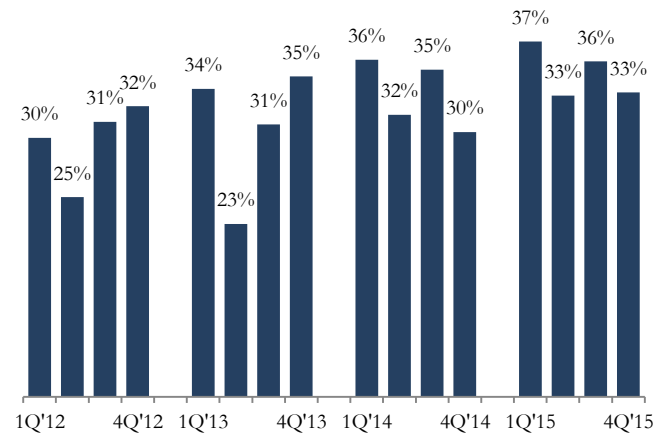
Source: NSE, PAC Research

Fig. 10: Fourth quarter revenue (₦billion)



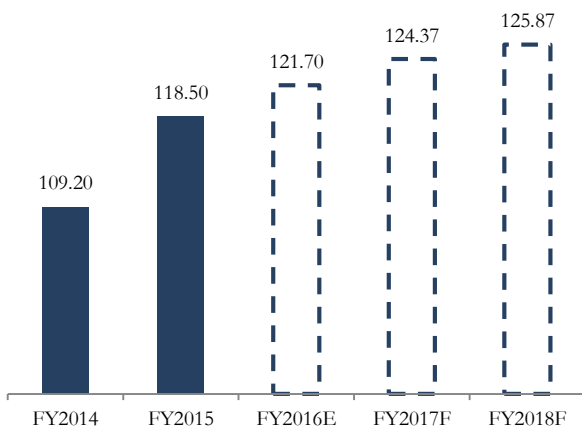
Source: NSE, PAC Research

Fig. 11: Quarterly operating expenses/revenue ratio



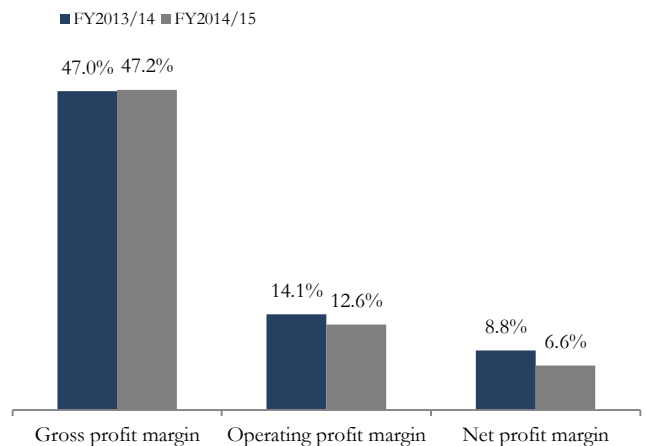
Source: NSE, PAC Research

Fig. 12: Annual sales revenue (₦billion)



Source: NSE, PAC Research

Fig. 13: Profit margins



Source: NSE, PAC Research

Fig. 14: Statement of Profit or Loss, ₦mn

	FY2015	FY2016E	FY2017F	FY2018F
Revenue	118,496	121,695	124,373	125,865
Change		2.70%	2.20%	1.20%
Cost of sales	62,604	64,499	66,539	66,960
Change		3.03%	3.16%	0.63%
Gross profit	55,892	57,197	57,833	58,905
Change		2.33%	1.11%	1.85%
Operating expenses	40,947	39,551	40,048	40,906
Change		-3.41%	1.26%	2.14%
Other operating income	505	540	421	329
Change		7.00%	-22.00%	-22.00%
Operating profit	15,450	18,186	18,207	18,327
Change		17.71%	0.11%	0.66%
Interest income	217	310	282	257
Change		43.00%	-9.00%	-9.00%
Interest expenses	4,872	4,482	4,303	4,131
Change		-8.00%	-4.00%	-4.00%
Profit before tax	10,795	14,014	14,186	14,454
Change		29.82%	1.23%	1.88%
Income tax expenses	3,000	3,924	4,114	4,336
Change		30.80%	4.84%	5.40%
Profit for the year	7,795	10,090	10,072	10,118
Change		29.45%	-0.18%	0.45%

Fig. 15: Statement of Financial Position, ₦mn

	FY2015	FY2016E	FY2017F	FY2018F
Non-Current Assets				
Property, plant & equipment	87,754	90,979	93,182	95,626
Intangible assets	943	830	722	628
Prepayments & other recv.	38	34	33	33
Total non-current assets	88,738	91,843	93,938	96,287
Current Assets				
Inventories	10,750	11,288	11,513	12,204
Trade & other receivables	16,956	16,447	15,296	14,225
Cash & cash equivalents	5,805	4,233	5,080	5,122
Total Current assets	33,511	31,968	31,889	31,551
Total assets	122,246	123,811	125,827	127,838
Equity	23,233	24,421	25,554	26,656
Non-Current Liabilities				
Deferred tax	3,085	2,869	2,955	3,014
Employee benefits	496	546	562	590
Total non-current liabilities	4,589	4,536	5,269	5,870
Current Liabilities				
Trade & other payables	1,237	1,361	1,551	1,737
Short-term borrowings	2,286	1,943	2,235	2,451
Dividend payable	63	286	382	477
Current tax liabilities	1,003	946	1,102	1,205
Total current liabilities	4,589	4,536	5,269	5,870
Total equity and liabilities	28,820	30,158	30,879	31,331

Fig. 16: Profitability & return

	FY2015	FY2016E	FY2017F	FY2018F
Gross profit margin	47.17%	47.00%	46.50%	46.80%
Operating profit margin	13.04%	14.94%	14.64%	14.56%
Net profit margin	6.58%	8.29%	8.10%	8.04%
ROCE	25.50%	26.22%	25.58%	24.82%
ROE	16.13%	19.25%	17.84%	16.84%
ROA	6.38%	8.15%	8.00%	7.91%

Source: Company's Annual Reports, PAC Research

Fig. 17: DuPont Analysis

	FY2015	FY2016E	FY2017F	FY2018F
Total assets turnover	1.96x	1.75x	1.75x	1.70x
Operating profit margin	13.04%	14.94%	14.64%	14.56%
Equity multiplier	2.53x	2.36x	2.23x	2.13x
ROCE	25.50%	26.22%	25.58%	24.82%

Fig. 18: Efficiency ratios

	FY2015	FY2016E	FY2017F	FY2018F
Fixed assets turnover	1.34x	1.33xx	1.32x	1.31x
Current assets turnover	3.54x	3.81x	3.90x	3.99x
Total assets turnover	1.96x	1.75x	1.75x	1.70x
Inventory turnover	5.41x	5.85x	5.84x	5.65x
Receivables turnover	n/a	n/a	n/a	n/a
Payables turnover	n/a	n/a	n/a	n/a
Days inventory outstanding	67	62	63	65
Days collection outstanding	n/a	n/a	n/a	n/a
Days payable outstanding	n/a	n/a	n/a	n/a
Operating cycle (days)	n/a	n/a	n/a	n/a

Fig. 19: Liquidity ratios

	FY2015	FY2016E	FY2017F	FY2018F
Working capital (₦millions)	-12,589	-13,324	-13,032	-14,408
Current ratio	0.73	0.71	0.71	0.69
Quick ratio	0.49	0.46	0.45	0.69
Cash ratio	0.13	0.09	0.11	0.11

Fig. 20: Long-term solvency & stability ratios

	FY2015	FY2016E	FY2017F	FY2018F
Gearing	20.22%	24.44%	20.68%	18.61%
Equity multiplier	2.53x	2.36x	2.23x	2.13x
Total debt-to-equity	1.53x	1.49x	1.31x	1.21x
Total debt-to-assets	60.46%	62.91%	58.74%	56.69%
Proprietary	39.54%	42.33%	44.87%	47.01%
Interest coverage	3.17x	4.06x	4.23x	4.44x
Cash coverage	6.68x	6.82x	6.26x	5.73x

Fig. 21: Shareholders' investment ratios

	FY2015	FY2016E	FY2017F	FY2018F
EPS, ₦	5.18	6.70	6.69	6.72
DPS, ₦	3.20	4.00	4.00	4.30
Payout	61.82%	59.70%	59.81%	64.01%
FCFPS, ₦	n/a	n/a	n/a	n/a

Source: Company's Annual Reports, PAC Research

Equity research methodology employed in this report

Views documented in this equity research report stem from conclusions reached through the use of multiple valuation methodologies, industry-wide knowledge, company specific information and our near to medium term expectations of industry and company performance, as well as market outlook. Our forecasts are based on a combination of top down and bottom up analysis, alongside historical trends in industry and company financials. Where appropriate, we factored in available forecasts and business direction provided by company management.

Our recommendation tends towards value investing. Therefore, our investment rank gauge—a customized scale we use to judge how well a firm under coverage has performed—is determined using major value parameters as well as relevant ratios and multiples computed with figures from the company's most recent financials.

The variables used to arrive at the company's investment rank cover a wide range of measures which characterize liquidity, operational efficiency, profitability, profit margins, growth, economic viability, gearing, relative valuation ratios, capital structure and management performance. Our investment recommendation is underpinned by the upside or downside potential of a stock under coverage. This potential is estimated by comparing the stock's current market price to its price target and fair value, on a percentage increase or decrease basis as summarized below:

Deviation from current price	Recommendation
>30%	STRONG BUY
10% to < 30%	BUY
-10% to < 10%	HOLD
<-10%	SELL

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