

PZ Cussons Nigeria Plc

Nigeria | Equities | Consumer Goods | August 27, 2015

PAC RESEARCH

Upward movement in finance costs restraint profitability

Full year 2014/15 revenue improves marginally by 0.3% y/y. In its full year audited results to May 2015, PZ Cussons recorded revenue of ₦73.13billion, up marginally by 0.3% compared with ₦72.91billion in the previous year. The weak increase in the revenue is typical of companies operating in the fast moving consumer goods sector in Nigeria in the current period, which is a reflection of factors such as weak consumer spending, undue competition with imported products and security challenges in the north-eastern part of the country. On a quarterly basis, the company reported revenue of ₦20.24billion in the fourth quarter to May 2015, a decline of 4.7% and 0.4% against ₦21.23billion and ₦20.31billion respectively in the third quarter to February 2015 and the fourth quarter to May 2014.

A 1.9% year-on-year decline in input costs improves gross profit margin. For the review period, PZ Cussons' cost of sales (COS) of ₦52.67billion declined by 1.9% compared with ₦53.71billion in the corresponding period of the previous year. The decline in the input costs despite a marginal increase in revenue resulted in a lower COS/revenue ratio of 72.0% relative to 73.7% in the previous period. On a quarterly basis, the company's COS of ₦14.13billion in the last quarter of the review period was down by 8.7% and 9.1%, compared with ₦15.47billion and ₦15.55billion accordingly in the third quarter of the review period and the fourth quarter of the previous period. On the contrary, the latest quarter's COS is higher than 8-quarter average of ₦13.30billion by 6.3%.

Furthermore, the company's COS/revenue ratio of 69.8% in the fourth quarter of the period is lower than 72.9% and 76.5% in the third quarter of 2014/15 and the fourth quarter of the preceding period. Similarly, the latest quarter's COS/revenue ratio is lower than 8-quarter average of 72.9%. Therefore, gross profit increased by 6.6% to ₦20.45billion compared with ₦19.20billion in the previous year, and gross profit margin improved to 28.0% relative to 26.3% in the previous period.

Fig. 1: Quarterly results highlights

	4Q2014/15	3Q2014/15	4Q2013/14	Q/q Δ	Y/y Δ
Revenue (₦mn)	20,236	21,230	20,312	-4.68%	-0.37%
Operating profit (₦mn)	2,767	2,121	1,696	30.46%	63.15%
Net profit (₦mn)	1,784	1,346	1,217	32.54%	46.59%

Source: NSE, PAC Research

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Price:

- Current	₦23.11*
- Target	₦18.80
Recommendation:	SELL

* As at Thursday August 27, 2015

Fig. 2: Stock data

FYE	May
Price Mov't: YtD / 52wk	+7.52%/-28.92%
52-week range	₦17.50 - ₦36.00
Average daily vol./val.	1,024,752 / ₦29.501mn
Shares Outstanding (₦mn)	3,971
Market Cap. (₦mn)	101,604 (US\$508.02mn)
EPS, ₦- 12months trailing	1.15
DPS, ₦- FY2014/15	0.81
FCF, ₦- FY2014/15	n/a

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

Fig. 3: Key ratios

	FY2014/15	FY2013/14
Gross profit margin	27.97%	26.33%
Net profit margin	6.25%	6.97%
Equity multiplier	1.54x	1.67x
Asset turnover	1.09x	1.03x

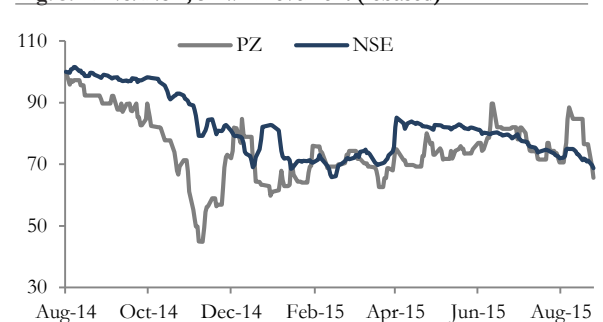
Source: NSE, PAC Research

Fig. 4: Valuations

	FY2015	FY2016E	FY2017F	FY2018F
P/Sales	1.62x	1.61x	1.59x	1.57x
P/E	25.91x	25.21x	26.38x	25.56x
PEG	n/a	25.21	2.20	6.39
EV/EBITDA	1.59x	1.57x	1.55x	1.52x
P/B	2.71x	2.62x	2.52x	2.44x
ROE	10.47%	10.41%	9.54%	9.55%
ROA	6.78%	6.80%	6.25%	6.38%
Div. Yield	2.72%	2.72%	2.18%	2.68%

Source: NSE, PAC Research

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



Source: Bloomberg, PAC Research

Operating profit improves despite an increase in running costs. For FY2014/15, the company posted operating expenses of ₦13.80billion, up by 7.1% y/y compared with ₦12.89billion in the preceding period. In the fourth quarter to May 2015, PZ Cussons posted operating expenses of ₦3.45billion, down by 17.1% compared with ₦3.69billion in the third quarter but it increased by 6.2% against ₦3.25billion in the fourth quarter of the prior year. Also, the operating expenses is higher than 8-quarter average of ₦3.34billion by 3.5%. Further analysis revealed that operating expenses/revenue ratio of 17.1% in the last quarter of the review period is lower than 17.4% in the third quarter but higher than 16.0% in the fourth quarter of the preceding year; it is also lower than 8-quarter average of 18.5%.

Overall, total costs declined marginally by 0.2% to ₦66.48billion against ₦66.60billion in 2013/14, and total costs/revenue ratio fell to 90.9% relative to 91.4% in the previous year. Consequently, operating profit increased by 2.9% to ₦6.77billion compared with ₦6.58billion in the previous period, and operating profit margin improved marginally to 9.3% relative to 9.0% in 2014/15. Moreover, we are keen to highlight an increase of 215.6% in finance costs to ₦445million against ₦141million in the previous year despite the fact that there is no loans and borrowings in the company's books in the review period. Also, interest income declined by 54.9% y/y to ₦229million against ₦508million. Therefore, net profit declined by 10.1% to ₦4.57billion compared with ₦5.08billion in the preceding period.

PZ Cussons out-performs the broad equity market in the review period.

In the 52-week period to August 2015, the company recorded total shareholders' returns (TSR) of -19.3% relative to -24.6% recorded by the equity market as measured by the All Share Index. On the contrary, the company under-performed the market in the same period of the previous year with TSR of +9.6% compared with the market returns of +20.4%. Similarly, PZ Cussons recorded year-to-date (YTD) returns of +16.6% against returns of -10.0% posted by the broad market in the same period.

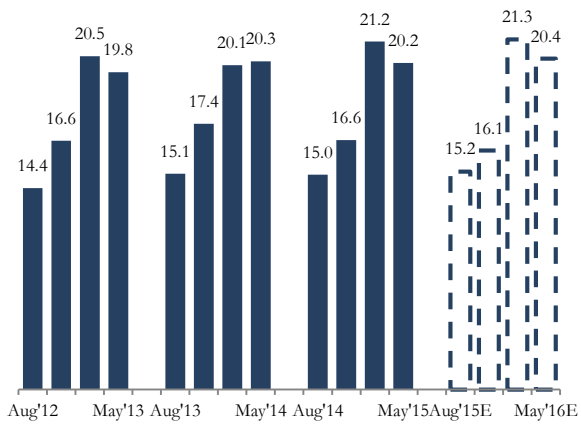
Valuation

Our Valuation puts the target price of the stock of PZ Cussons Nigeria Plc at ₦18.80. 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 SELL 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, insecurity challenges in the northern part of the country, demographic factor, the strength of consumer spending and the intensity of competition in the market.

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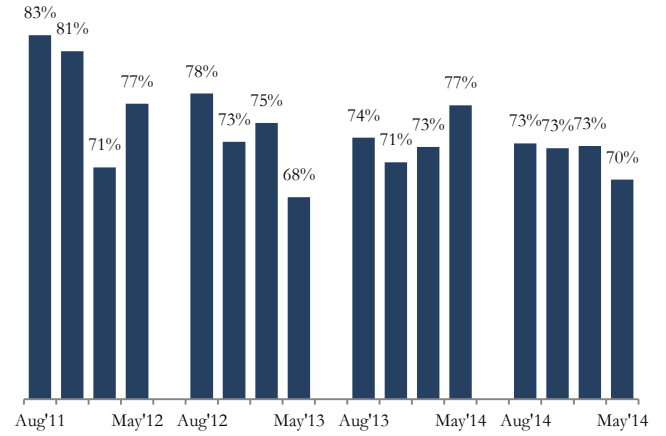
“ Our Valuation puts the target price of the stock of PZ Cussons Nigeria Plc at ₦18.80. ”

Fig. 6: Quarterly sales revenue (₦billion)



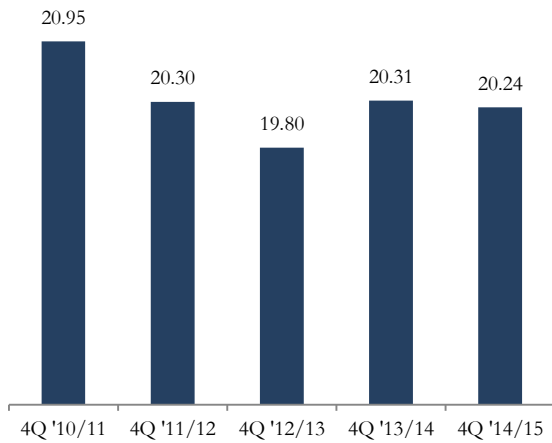
Source: NSE, PAC Research

Fig. 7: Quarterly COS/revenue ratio



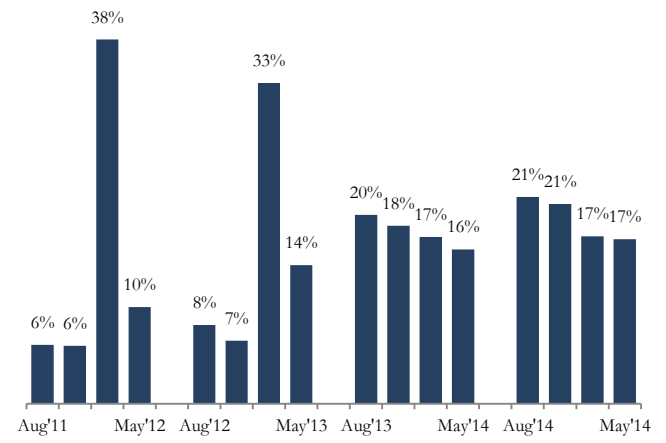
Source: NSE, PAC Research

Fig. 8: Fourth quarter sales revenue (₦billion)



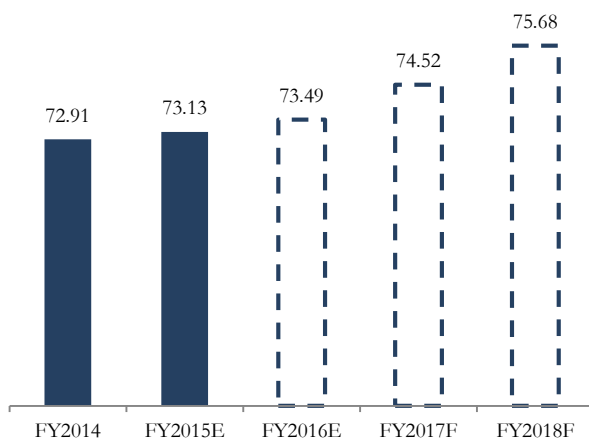
Source: NSE, PAC Research

Fig. 9: Quarterly operating expenses/revenue ratio



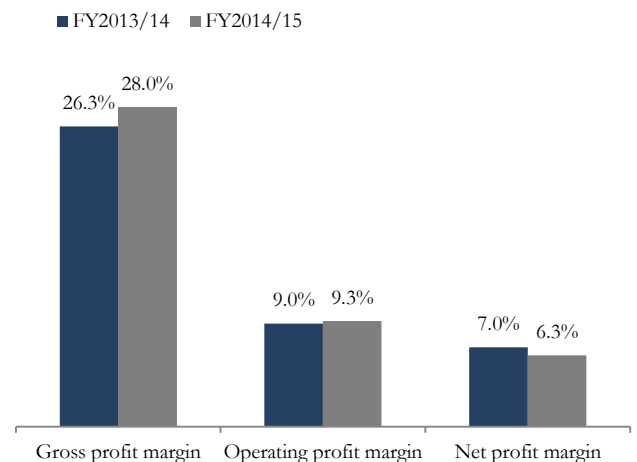
Source: NSE, PAC Research

Fig. 10: Annual sales revenue (₦billion)



Source: NSE, PAC Research

Fig. 11: Profit margins



Source: NSE, PAC Research

Fig. 12: Statement of Profit or Loss, ₦mn

	FY2015	FY2016E	FY2017F	FY2018F
Revenue	73,126	73,492	74,521	75,638
Change		0.50%	1.40%	1.50%
Cost of sales	52,672	53,061	54,102	54,838
Change		0.74%	1.96%	1.36%
Gross profit	20,454	20,431	20,419	20,801
Change		-0.11%	-0.06%	1.87%
Operating expenses	13,803	13,596	13,935	14,296
Change		-1.50%	2.50%	2.59%
Other operating income	122	117	107	128
Change		-4.10%	-8.55%	20.00%
Operating profit	6,773	6,952	6,590	6,633
Change		2.64%	-5.20%	0.65%
Interest income	229	234	259	311
Change		2.00%	11.00%	20.00%
Interest expenses	445	472	434	417
Change		6.00%	-8.00%	-4.00%
Profit before tax	6,557	6,714	6,416	6,528
Change		2.39%	-4.44%	1.75%
Income tax expenses	1,986	2,014	1,925	1,893
Change		1.41%	-4.44%	-1.64%
Profit for the year	4,571	4,700	4,491	4,635
Change		-2.81%	-4.44%	3.20%

Fig. 13: Statement of Financial Position, ₦mn

	FY2015	FY2016E	FY2017F	FY2018F
Non-Current Assets				
Property, plant & equipment	25,218	25,975	27,178	27,722
Total non-current assets	25,218	25,975	27,178	27,722
Current Assets				
Inventories	21,013	20,803	21,219	20,795
Trade & other receivables	18,829	19,582	20,757	20,342
Cash & cash equivalents	2,328	2,782	2,680	3,749
Total Current assets	42,170	43,167	44,656	44,885
Total assets	67,388	69,142	71,834	72,607
Equity	43,672	45,155	47,065	48,523
Non-Current Liabilities				
Deferred tax	3,904	4,339	4,165	3,957
Provisions	249	183	183	183
Loans and borrowings				
Total non-current fin. liab.	4,153	4,522	4,348	4,140
Current Liabilities				
Trade & other payables	17,835	17,389	18,432	17,972
Current tax liabilities	1,671	2,014	1,925	1,893
Total current liabilities	19,506	19,403	20,357	19,865
Total equity and liabilities	67,388	69,142	71,834	72,607

Fig. 14: Profitability & return

	FY2015	FY2016E	FY2017F	FY2018F
Gross profit margin	27.97%	27.80%	27.40%	27.50%
Operating profit margin	9.269%	9.46%	8.84%	8.77%
Net profit margin	6.25%	6.39%	6.03%	6.13%
ROCE	15.51%	15.40%	14.00%	13.67%
ROE	10.47%	10.41%	9.54%	9.55%
ROA	6.78%	6.80%	6.25%	6.38%

Source: Company's Annual Reports, PAC Research

Fig. 15: DuPont Analysis

	FY2015	FY2016E	FY2017F	FY2018F
Total assets turnover	1.67x	1.63x	1.58x	1.56x
Operating profit margin	9.269%	9.46%	8.84%	8.77%
Equity multiplier	1.54x	1.53x	1.53x	1.50x
ROCE	15.51%	15.40%	14.00%	13.67%

Fig. 16: Efficiency ratios

	FY2015	FY2016E	FY2017F	FY2018F
Fixed assets turnover	2.90x	2.83x	2.74x	2.73x
Current assets turnover	1.73x	1.70x	1.67x	1.69x
Total assets turnover	1.67x	1.63x	1.58x	1.56x
Inventory turnover	2.70x	2.54x	2.57x	2.61x
Receivables turnover	n/a	n/a	n/a	n/a
Payables turnover	n/a	n/a	n/a	n/a
Days inventory outstanding	135	144	142	140
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. 17: Liquidity ratios

	FY2015	FY2016E	FY2017F	FY2018F
Working capital (₦millions)	22,607	23,702	24,235	24,941
Current ratio	2.16	2.22	2.19	2.25
Quick ratio	1.08	1.15	1.15	1.21
Cash ratio	0.12	0.14	0.13	0.19

Fig. 18: Long-term solvency & stability ratios

	FY2015	FY2016E	FY2017F	FY2018F
Gearing	0.00%	0.00%	0.00%	0.00%
Equity multiplier	1.54x	1.53x	1.53x	1.50x
Total debt-to-equity	0.35x	0.35x	0.34x	0.33x
Total debt-to-assets	54.30%	53.12%	52.63%	49.64%
Proprietary	64.81%	65.31%	65.52%	66.83%
Interest coverage	15.22x	14.74x	15.19x	15.12x
Cash coverage	n/a	n/a	n/a	n/a

Fig. 19: Shareholders' investment ratios

	FY2015	FY2016E	FY2017F	FY2018F
EPS, ₦	1.15	1.18	1.13	1.17
DPS, ₦	0.81	0.81	0.65	0.80
Payout	70.37%	68.44%	57.47%	68.54%
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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