

Brighter prospects but pricey valuation

8th March, 2021

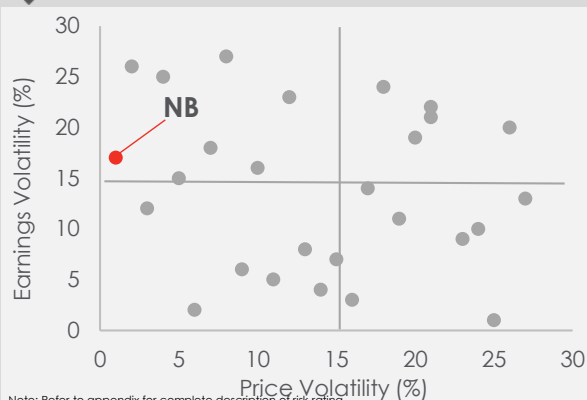
Research Analyst:

Akinloye Ayorinde

+234-(0)802-818-0822

ayorinde.akinloye@unitedcapitalplcgroup.com

Risk Rating: Low



Key Data

Last Price (₦)	49.5
Last Price (\$)	0.12
52 week High/Low (₦)	63.25/ 22.00
1M Price Change (%)	-18.9
3M Price Change (%)	-11.6
6M Price Change (%)	+23.8
YTD Change (%)	-11.6
Beta	1.34
Market Capitalization (₦'bn)	395.8
Market Capitalization (\$'mn)	965.5
Shares Outstanding. (Units'm)	7,996.9
Float (%)	46.76
Dividend Yield (%)	1.4

Price Performance Chart



Sources: Bloomberg, United Capital Research

Stock Rating
SELL

Target Price
Old: N45.3
New: N39.7

Expected Return
-19.8%

In its recently released FY-2020 scorecard, NB reported a 4.3% y/y growth in Revenue, printing at N337.0bn, from N323.0bn in FY-2019. The growth in Revenue was driven by a solid recovery in H2-2020 where Revenue grew 21.2% y/y compared to 10.8% y/y decline in H1-2020. The company faced significant cost pressures during the year, emanating from inflationary pressures and naira devaluation impact on raw material costs. As a result, Gross profit fell 9.6% y/y to N118.7bn. Despite controlled Operating expenses, higher Finance costs (up 50.8% y/y) pressured profitability during the year as Pre-Tax profits and Net income plunged 50.4% and 54.3% to N11.6bn and N7.4bn, respectively. We review our forecasts for the company and present our outlook below.

Strong recovery in H2-2020 rescues FY-2020 revenue: In H1-2020, Covid-linked pressures which led to the closure of on-trade channels (clubs & bars) as well as a ban on social gatherings pressured Revenue, which declined 10.8% y/y in H1-2020. However, in H2-2020, the relaxation of Covid-19 restrictions and gradual return to normality supported recovery in Revenue. In addition, prior price increment in Nov-2019 and Feb-2020 crystalized. As a result, Revenue in H2-2020 grew 21.2% y/y. Overall, FY-2020 Revenue grew 4.3% y/y to N337.0bn from N323.0bn in FY-2019. Across product segments, the premium beer segment recorded the most impressive growth, growing double-digit, led by gains in Heineken and Tiger. In addition, NB impressively grew ahead of the market, garnering a stronger market share in FY-2020.

Devaluation and inflationary pressures impact costs: In FY-2020, Cost of Sales grew, faster than Revenue, up 13.9% y/y to N218.4bn from N191.8bn in FY-2019. Consequently, cost margin grew 542bps y/y to 64.8% in FY-2020. The increase in Cost of sales was driven by the increase in the naira cost of imported raw materials (Barley & Hops) due to the devaluation of the naira as well as inflationary pressures on locally sourced materials (Sorghum, Cassava & Packaging Materials).

Brighter prospects but pricey valuation

Consequently, Gross profit fell 9.6% y/y to N118.7bn in FY-2020 from N131.3bn in FY-2019 while Gross margin fell 542bps to 35.2% in FY-2020.

Reduced commercial activity & controlled personnel cost keeps Opex in check:

Operating expenses declined 7.4% y/y to N89.9bn in FY-2020 from N97.1bn in FY-2019. The decline in Opex was driven by a synchronized decline in Marketing & Distribution expenses (down 9.0% y/y) and Administrative expenses (down 0.7% y/y). The decline in Marketing & Distribution expenses was driven by reduced commercial and promotional activities evident in the 13.8% decline in Advertising & Sales promotion. Also, Personnel expenses was kept in check, supporting the flattish decline in Administrative expenses. Nevertheless, Operating profit declined 15.9% y/y to N29.6bn in FY-2020.

Surge in debt level drives Finance cost higher...pressures profits: In FY-2020, NB actively raised short term debt finance from the capital market, exploiting the low yield environment. Thus, the company's aggregate debt level surged, climbing higher by 64.1% y/y to N91.4bn at the end of FY-2020. Consequently, Interest expense grew 50.8% y/y to N18.3bn in FY-2020. Meanwhile, Interest income fell 5.5% y/y and consequently pulled Net Finance cost higher by 52.1% y/y. This pressured Pre-Tax profits, which declined 50.4% y/y to N11.6bn for FY-2020, from N23.4bn in FY-2019. Piling further pressure, Effective tax rate jumped by 532bps to 36.4% for FY-2020, pushing Net Profit further lower, down 54.3% y/y to N7.4bn at the end of FY-2020.

Volume and price growth to support Revenue recovery: Looking ahead, we anticipate sustained recovery in Revenue supported by volume growth as well as expected price increments by the company. Volume growth will be supported by improved market acceptance of recently introduced brands and flavours in the premium and malt segment of the company's product lines. Sustained investment in market channels as well as sustained return to normality would support demand from on-trade channels. Also, we note that the beer industry is in steep losses as it has struggled to pass on cost increases to consumers. However, with the recent surge in costs due to the naira devaluation, brewers are expected to implement more price increments in FY-2021. We expect this to further support Revenue. We forecast a Revenue growth of 11.3% y/y to N375.1bn for FY-2021e.

Price increase to support margins and profit growth: Following the significant cost pressures in FY-2020, we expect further price increases in FY-2021e. We expect these increases to strengthen the company's margins and consequently improve profitability. Also, we expect the cost pressures of FY-2020 to dissipate through the course of the year as the FX situation improves. We project Gross margin and Operating margin to edge higher by 178bps y/y and 147bps y/y. We forecast Net income growth of 74.8% y/y to N12.9bn in FY 2021e.

...we anticipate a significantly improved performance in FY-2021e as price and volume growth will support improved Revenue and Profit.

Brighter prospects but pricey valuation

Brighter prospects but pricey valuation: We recognize the improved outlook for NB due to improved pricing, volume growth and controlled cost pressures. However, we consider the current price of the stock expensive. NB trades at a PE ratio of 53.8x, a significant premium of 87.8% over our peer average as well as a 35.2% premium over NB's historical average. Following the updates to our forecasts for FY-2021e, we set a target price of N39.72/s and place a SELL recommendation on the stock due to the 19.8% downside on the stock.

**...we set our year-end
Target Price at N39.72/
share with a SELL rating
on the stock.**

Brighter prospects but pricey valuation

Financial Highlights (N'Mn)			
Headlines	FY - 2020	FY- 2019	Change
Revenue	337,046	323,006	4.3%
Cost of Sales	-218,355	-191,757	13.9%
Gross Profit	118,691	131,250	-9.6%
Other Income	828	1,005	-17.6%
Operating Expense	-89,914	-97,051	-7.4%
Operating Profit	29,605	35,204	-15.9%
Finance Income	246	261	-5.5%
Finance Costs	-18,275	-12,115	50.8%
Profit Before Tax	11,577	23,351	-50.4%
Taxation	-4,208	-7,246	-41.9%
Profit After Tax	7,368	16,105	-54.2%
	FY - 2020	FY - 2019	
Cash and Cash Equivalents	30,370	6,361	377.4%
Trade & Other Receivables	11,417	21,307	-46.4%
Trade & Other Payables	139,201	102,783	35.4%
Total Debt	91,447	55,720	64.1%
Total Assets	445,857	382,778	16.5%
Net Assets	161,179	167,750	-3.9%
Gross Margin	35.2%	40.6%	-5.4%
Cost to Sales	64.8%	59.4%	5.4%
Net Margin	2.2%	5.0%	-2.8%
Leverage (Debt/Equity)	56.7%	33.2%	23.5%
Leverage (Net Debt/Equity)	37.9%	29.4%	8.5%
Price(N)	49.5		
Trailing 12M EPS(N)	0.92		
BVPS(N)	20.2		
Trailing 12M P/E (x)	53.7		
P/BV (x)	2.5		
Trailing 12M ROAE	4.5%		
Proposed Dividend (N)	0.69		
Dividend Yield	1.4%		
Qualification Date	March 10, 2021		
Closure of Register	March 11-17, 2021 (both dates inclusive)		
Payment Date	April 22, 2021		

Disclosure Appendix

Investment Rating Criteria and Disclosure

United Capital Research adopts a 3-tier recommendation system for assets under our coverage: Buy, Hold and Sell. These generic ratings are defined below:

Buy: Based on our valuation and subjective view (if any), the expected upside on the stock's close price as at 31st December is greater than the Asymmetric Corridor around the MPR of the Central Bank of Nigeria (which is currently MPR – 500bps; i.e 9%). We consider this as the minimum return that may deserve our holding of a risk asset, like equity.

Hold: Based on our valuation and subjective view (if any), the expected upside on the stock's close price as at 31st December is greater zero but less than the Asymmetric Corridor around the MPR of the Central Bank of Nigeria (which is currently MPR – 500bps; i.e 9%).

Sell: Based on our valuation and subjective view (if any), the expected upside on the stock's close price as at December 31st is less than zero.

NR*: Please note that in addition to our three rating heads, we indicate stocks that we do not rate with NR; meaning Not-Rated. We may not rate a stock due to investment banking relationships, other sources of conflict of interests and other reasons which may from time to time prevent us from issuing a rating on the shares (or other instruments) of a company.

Please note that we sometimes give concessional rating on stocks, which may be informed by technical factors and market sentiments.

Conflict of interest: It is the policy of United Capital Plc and all its subsidiaries/affiliates (hereafter collectively referred to as "UCAP") that research analysts may not be involved in activities that suggest that they are representing the interests of UCAP in a way likely to appear to be inconsistent with providing independent investment research. In addition, research analysts' reporting lines are structured so as to avoid any conflict of interests. Precisely, research analysts are not subject to the supervision or control of anyone in UCAP's Investment Banking or Sales and Trading departments. However, such sales and trading departments may trade, as principal, on the basis of the research analyst's published research. Therefore, the proprietary interests of those Sales and Trading departments may conflict with your interests as clients. Overall, the Group protects clients from probable conflicts of interest that may arise in the course of its business relationships.

Risk Rating

Our Risk rating assesses the likelihood of market price deviating significantly from valuation fair prices. Risk factors limit gravitation of market prices towards target prices or result in significant decline in current price and thus swing buy/sell rating from positive to negative or vice versa. Risk factors are broadly grouped into systematic and unsystematic risk. Systematic risk (also called market risk or un-diversifiable risk) captures uncertainties or volatilities inherent to the entire market. This also includes macroeconomic shocks emanating from government actions or inactions, unanticipated policy pronouncements, external shocks and socio-political tensions which may swing market prices significantly away from targets. Unsystematic risk (specific risk, diversifiable risk or residual risk) on the other hand captures company or sector specific uncertainties which can mostly be reduced by diversification. These include labour union/industrial actions, corporate governance/management inefficiency, litigation, possible liquidation/winding-down of operation, internal labour unrest, government action, policy missteps as well as disruptions resulting from innovation, technology and technical progress etc.

United Capital Research adopts a 3-tier risk rating for assets under our coverage: High, Medium and Low. The rating scale is ordinal and captures the diverse risks that we deem applicable the company of focus. The ratings are defined below:

High: High probability of an imminent systematic risk or/and unsystematic risk

Medium: Slightly high (but lower compared to 'High') probability of an imminent systematic risk or/and unsystematic risk

Low: Low probability of an imminent systematic risk or/and unsystematic risk

Analyst Certification

The research analysts who prepared this report certify as follows:

1. That all of the views expressed in this report articulate the research analyst(s) independent views/opinions regarding the companies, securities, industries or markets discussed in this report.
2. That the research analyst(s) compensation or remuneration is in no way connected (either directly or indirectly) to the specific recommendations, estimates or opinions expressed in this report.

Other Disclosures

United Capital Plc or any of its affiliates (hereafter collectively referred to as "UCAP") may have financial or beneficial interest in securities or related investments discussed in this report, potentially giving rise to a conflict of interest which could affect the objectivity of this report. Material interests which UCAP may have in companies or securities discussed in this report are disclosed:

- UCAP may own shares of the company/subject covered in this research report.
- UCAP does or may seek to do business with the company/subject of this research report
- UCAP may be or may seek to be a market maker for the company which is the subject of this research report
- UCAP or any of its officers may be or may seek to be a director in the company(ies) covered in this research report
- UCAP may be likely recipient of financial or other material benefits from the company/subject of this research report

Company	Disclosure
Dangote Cement Plc	a,h
Fidelity Bank Plc	h
Flour Mills of Nigeria Plc	h
Forte Oil Plc	g
International Breweries Plc	a,h
Nigerian Breweries Plc	h
PZ Nigeria Plc	h
Stanbic IBTC Plc	g
Total Nigeria Plc	h
UAC of Nigeria Plc	h
Zenith Nigeria Plc	a

Disclosure keys

- a. The analyst holds personal positions (directly or indirectly) in one or more of the stocks covered in this report
- b. The analyst(s) responsible for this report (whose name(s) appear(s) on the front page of this report is a Board member, Officer or Director of the Company or has influence on the company's operating decision directly or through proxy arrangements
- c. UCAP is a market maker in the publicly traded equities of the Company
- d. UCAP has been lead arranger or co-lead arranger over the past 12 months of any offer of securities of the Company
- e. UCAP beneficially own 1% or more of the equity securities of the Company
- f. UCAP holds a major interest in the debt of the Company
- g. UCAP has received compensation for investment banking activities from the Company within the last 12 months
- h. UCAP intends to seek, or anticipates compensation for investment banking services from the Company in the next 6 months
- i. The content of this research report has been communicated with the Company, following which this research report has been materially amended before its distribution
- j. The Company is a client of UCAP
- k. The Company owns more than 5% of the issued share capital of UCAP

Disclaimer

United Capital Plc Research (UCR) notes are prepared with due care and diligence based on publicly available information as well as analysts' knowledge and opinion on the markets and companies covered; albeit UCR neither guarantees its accuracy nor completeness as the sole investment guidance for the readership. Therefore, neither United Capital (UCAP) nor any of its associates or subsidiary companies and employees thereof can be held responsible for any loss suffered from the reliance on this report as it is not an offer to buy or sell securities herein discussed. Please note this report is a proprietary work of UCR and should not be reproduced (in any form) without the prior written consent of Management. UCAP is registered with the Securities and Exchange Commission and its subsidiary, United Capital Securities Limited is a dealing member of the Nigerian Stock Exchange. For enquiries, contact United Capital Plc, Afriland Towers (3rd Floor), 97/105, Broad Street, Lagos. ©United Capital Plc 2019.