Unilever Nigeria Plc (UNILEVER)

Not out of the woods

United Capital
The Intelligent Choice

Equity Research | Earnings Update

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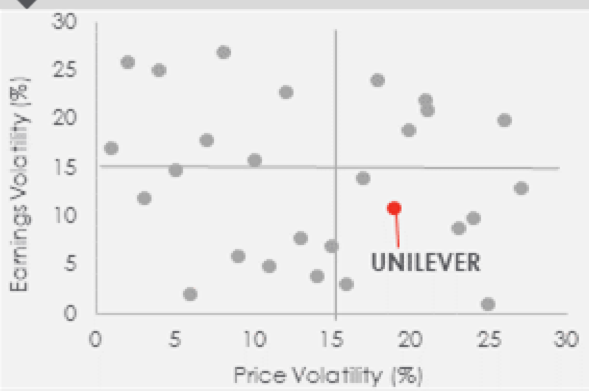
Risk Rating: Medium

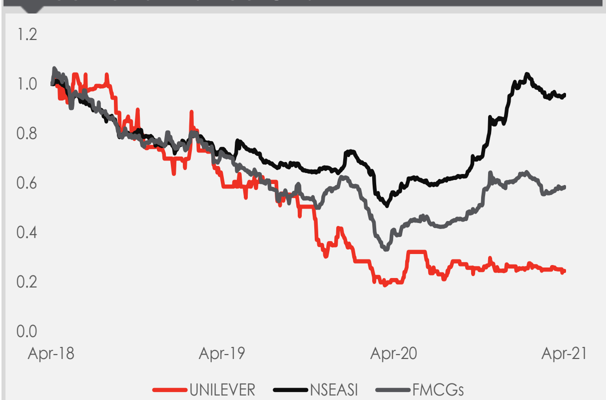


Note: Refer to appendix for complete description of risk rating

Key Data

Last Price (₦)	12.95
Last Price ($)	0.03
52 week High/Low (₦)	17.05/ 10.50
1M Price Change (%)	-2.3
3M Price Change (%)	-4.1
6M Price Change (%)	-1.5
YTD Change (%)	-6.8
Beta	0.8
Market Capitalization (₦'bn)	74.4
Market Capitalization ($'mn)	196.3
Shares Outstanding. (Units'bn)	5.7
Float (%)	24.0
Dividend Yield (%)	NM

Price Performance Chart



Sources: Bloomberg, United Capital Research

Stock Rating	Target Price	Expected Return
SELL	**Old: N15.00** **New: N11.46**	**-11.5%**

Recently, Unilever Nigeria Plc (UNILEVER) published its Audited FY-2020 and Unaudited Q1-2021 financial result. According to the reports, Revenue grew marginally in FY-2020, up 2.4% y/y to N62.0bn. In Q1-2021, Revenue surged 45.7% y/y to N19.4bn. However, the company's revenue improvement remains undermined by huge cost pressures and impairment booking. As a result, UNILEVER recorded a loss of N4.0bn in FY-2020 and N0.5bn in Q1-2021. Below, we update our model estimates for UNILEVER, based on the recently published numbers and provide our expectations for the rest of the year.

Revenue resurgence continues: According to the recently released financials, UNILEVER's recent Revenue resurgence continued in Q4-2020 and Q1-2021. Overall, while FY-2020 Revenue grew marginally by 2.4% y/y to N62.0bn, Q4-2020 Revenue surged 94.5% y/y to N17.2bn. Similarly, Q1-2021 Revenue grew 45.7% y/y to N19.4bn. Across business segments, FY-2020 Revenue was driven by decent growth in Food Revenue (up 18.8% y/y) while Home & Personal Care (down 12.4% y/y) disappointed. The weakness in the HPC business segment reflects severe competition from lower priced brands amidst tight consumer wallets. That said, the impressive growth in Q1-2021 was driven by growth in both business segments as HPC (up 52.6% y/y) and Food (up 40.3% y/y) recorded strong growth. However, we note that the surge in Revenue was largely price-driven as Unilever (in line with industry trend) raised prices on several of its products amidst climbing cost pressures.

Cost pressures remain sticking point: While UNILEVER's revenue has continued to recover, recent cost pressures have refused to taper. In its FY-2020 financials, the company reported an 11.8% y/y decline in Cost of Sales which puts Cost margin at 79.3%. This remains high compared to pre-2019 five-year average of 67.3%. Thus, while decent improvements were recorded in FY-2020, the company remains a long way off prior cost efficiency levels. The cost pressures have been exacerbated by resurgence in commodity prices, particularly crude

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(price of Linear Alkyl Benzene, a key material in Detergent & soap production is tied to crude price movements) and palm oil. Furthermore, the recent currency devaluations coupled with FX scarcity has raised the company's naira cost of production. This has informed recent price increase across the company's brands.

The price increase appears to be driving some improvements as Cost margin printed at 77.0% in Q1-2021, lower than FY-2020's 79.3% and recent three-quarter average of 80.7%. Overall, Q1-2021 Cost of Sales grew 51.0% y/y (compared to a 45.7% y/y growth in Revenue) to N15.0bn. Gross profit grew 30.6% y/y to N4.5bn in Q1-2021.

Pressure from Opex and impairments drag operating performance: In FY-2020, although Opex declined 7.5% y/y to N15.2bn, the company booked Impairments worth N3.8bn on receivables. As a result, UNILEVER recorded Operating loss of N6.1bn in FY-2020, albeit lower than Operating loss of N11.9bn in FY-2019. In Q1-2021, Opex climbed 54.9% y/y to N4.6bn from N3.0bn in Q1-2020, pressuring Operating performance. The surge in Opex reflects broad based increases in Brand & Marketing cost (up 63.3% y/y), Overheads (up 53.3% y/y) and Service Fees (up 124.5% y/y). As a result, UNILEVER recorded Operating loss of N82.7m in Q1-2021, compared to Operating profit of N431.7m IN Q1-2020.

...UNILEVER continues to battle stubborn cost pressures, undermining recent Revenue recovery.

Still stuck in the woods: The company's cost pressures continue to derail gains from improving revenue. Finance income (now an important revenue item due to the company's huge cash balance), declined 26.1% y/y to N1.5bn in FY-2020 as a result of the lower yield environment. However, it was inadequate in keeping the company from making a loss, as Loss before Tax and Loss after Tax printed at N4.6bn and N4.0bn, respectively. In Q1-2021, the company also recorded a Loss after Tax of N492.0m, compared to Net Profit of N1.1bn in Q1-2020.

Outlook & Valuation: Looking ahead, we expect the company's revenue to continue its upward trajectory. Our expectation is premised on the company's recent price increases on several of its products, which we believe would support price-driven growth. Our viewpoint is further bolstered by the fact that price increments in the FMCG space have been industry-wide and thus we do not expect a dramatic fall in UNILEVER's volumes. That said, we note competition among brands in the FMCG space (particularly among players in Home and Personal Care segment) remains tough. Overall, we forecast Revenue growth of 24.5% y/y to N77.1bn as we expect the high base effect of H2-2020 to smoothen growth rates.

However, we anticipate that the company will continue to face cost pressures. Thus, while we model a lower Cost margin of 78.0% (driven by improved pass-through effect of recent price increment), we do not expect cost efficiency to return to pre-2019 levels. In addition, we expect the company's high operating leverage (driven by huge fixed costs) to further weigh on operating performance. We forecast Operating loss of N0.8bn (lower

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than FY-2020 actual of N6.1bn) in FY-2021. That said, we expect the resurgence in the yield environment to revive Finance income which feeds into our 38.5% y/y forecast increase in Finance income to N2.1bn. We expect this to help return the company back to profitability for the first time in three years. We forecast a Net income of N0.9bn in FY-2021.

Following adjustments made to our forecasts as well as updating our valuation inputs to reflect the changing yield environment as well as increased macroeconomic risks, we lower our target price to N11.46/s which implies an 11.5% downside to current price of N12.95. In light of this, we have changed our recommendation from a BUY to a **SELL**.

... we review our year-end target price to N11.46/share on the back of slower than expected profit recovery.

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Financial Highlights (N'Mn)

Earnings Flash | Unilever Nigeria Plc Q1-2021 **Unaudited Result**

Financial Highlights (N'Mn)			
Headlines	Q1 - 2021	Q1 - 2020	Change
Revenue	**19,426**	**13,329**	45.7%
Cost of sales	-14,951	-9,902	51.0%
Gross Profit	**4,475.2**	**3,426.9**	**30.6%**
Operating Expenses	-4,640.7	-2,995.1	54.9%
Finance income	187	496	-62.3%
Finance costs	-34	-1	5497.9%
Other Income	0	22	-100.0%
Profit/Loss Before Tax	**-13**	**948**	NM
Taxation	-479	166	NM
Profit/Loss for the period	**-492.0**	**1,114**	NM
	Q1 - 2021	FY-2020	
Cash and Bank Balances	38,809	37,101	4.6%
Trade & Other Receivables	**13,914**	**12,957**	**7.4%**
Trade & Other Payables	**29,433**	**27,422**	**7.3%**
Borrowings	**239**	**211**	**13.4%**
Total Assets	**93,269**	**91,518**	**1.9%**
Net Assets	61,637	62,129	-0.8%
Gross Margin	23.0%	25.7%	**-2.7%**
Net Margin	NM	8.4%	**NM**
Cost to Sales	77.0%	74.3%	**2.7%**
Leverage (Debt/Equity)	0.4%	0.3%	**0.0%**
Price(N)	13.0		
Trailing 12M EPS(N)	NM		
BVPS(N)	10.7		
P/E (x)	NM		
P/BV (x)	1.2		
Trailing 12M ROAE	NM		

Sources: Company Financials, United Capital Research

Disclosure Appendix

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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.

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

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Fidelity Bank Plc	h
Flour Mills of Nigeria Plc	h
Forte Oil Plc	g
International Breweries Plc	a,h
Nigerian Breweries Plc	h
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Total Nigeria Plc	h
UAC of Nigeria Plc	h
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