

Friday, June 26, 2015

Building Alliances for Growth

1.0 FY 2014 Performance Analysis:

The audited Full Year 2014 (FY 2014) result of GlaxoSmithKline Consumer Nigeria Plc (Glaxosmith) for the period ended December 31, 2014 shows that its Turnover (T/O) increased by 4.58% to N30.52bn, compared with N29.18bn recorded in the corresponding period of 2013. The improvement in revenue can be attributed to the increased income generated from consumer healthcare products, particularly Lucozade and Ribena. The revenue generated from this segment increased by 4.23% to N21.41bn in 2014. The cost of sales increased by 12.54% to N19.79bn in FY 2014 from N17.58bn recorded in FY 2013. The increase in the cost of sales can mostly be attributed to the rise in the cost of raw materials. The cost of raw materials, consumables and goods purchased for resale rose by 12.53% to N16.47bn in FY 2014. Cost of sales as a percentage of Turnover rose to 64.83% from 60.24% as at FY 2013. The administrative, selling and distribution expenses increased by 3.02% to N7.65bn. These expenses as a percentage of turnover decreased marginally to 25.06% in FY 2014 from 25.44% in FY 2013.

The other operating income stood at N81.11mn as at FY 2014, representing a decrease of 1.64%, compared with N82.46mn recorded in FY 2013. Other operating expenses rose significantly to N1.03bn in FY 2014 from N104.45mn in 2013, this increase was mostly due to unrealised exchange losses totalling N893.137mn. The company also recorded a significant increase of 895.14% in its finance cost of N5.12mn in FY 2014 from N0.51mn in 2013. The Profit Before Tax (PBT) fell to N2.75bn, a decrease of 36.21% from N4.31bn recorded in the corresponding period of 2013. The tax provision also decreased by 35.27% to N903.37mn from N1.40bn, leading to a Profit After Tax (PAT) of N1.85bn in FY 2014 from N2.92bn in the corresponding period of 2013, representing a decrease of 36.67%. The company's profit margins decreased significantly in FY 2014 compared with FY 2013. This is a reflection of the challenges the company is facing with regards to stiff competition rising cost of raw materials and increased foreign exchange loss.

Table 1:	HOLD
Current Price	N44.00
Fair Value	N48.19

The turnover in FY December 2014 increased by 4.58% to N30.52bn.

The improvement in revenue can be attributed to the increased income generated from consumer healthcare products, particularly Lucozade and Ribena.

The company's profit margins decreased significantly in FY 2014 compared with FY 2013.

Table 2: Financial Performance (N'bn)

	FY 2014	FY 2013	Change
T/O	30.52	29.18	4.58%
EBIT	2.69	4.15	(35.26%)
PBT	2.75	4.31	(36.21%)
PAT	1.85	2.92	(36.67%)

Table 3: Quarterly Result Highlights (N'bn)

	Q1 2015	Q4 2014	Q3 2014	Q2 2014	Q1 2014	Q4 2013
Turnover	7.46	7.31	7.54	7.87	7.80	7.85
PBT	0.42	0.69	0.81	0.36	0.89	1.53
PAT	0.30	0.37	0.62	0.25	0.62	0.99

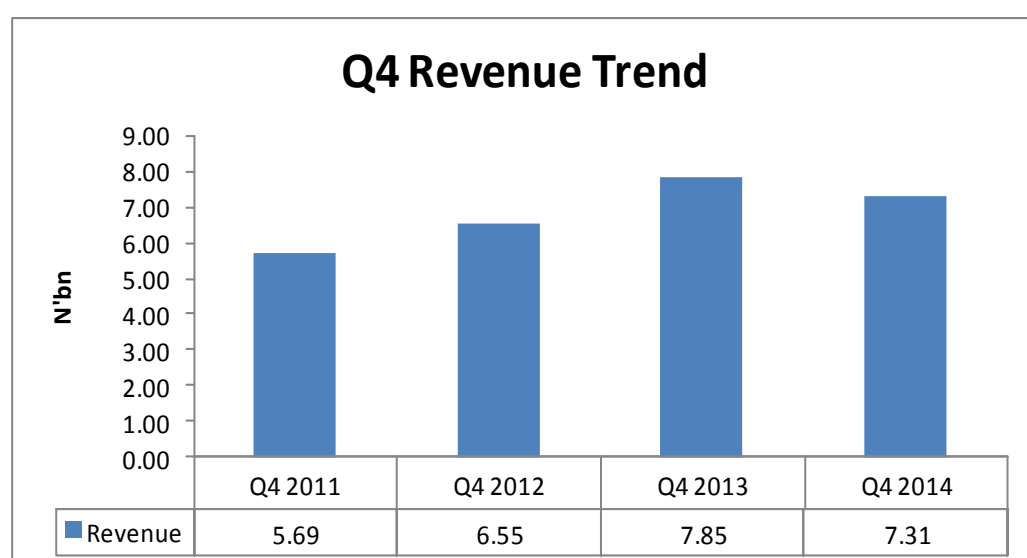
The Gross Profit Margin decreased to 35.17% in 2014 from 39.76% in 2013. The EBIT Margin decreased significantly in 2014 to 8.81% from 14.24% in 2013.

The company's profit margins decreased in 2014 compared with 2013. The Gross Profit Margin decreased to 35.17% in 2014 from 39.76% in 2013. The EBIT Margin decreased significantly in 2014 to 8.81% from 14.24% in 2013. The PBT margin decreased to 9.02% in 2014 from 14.79% in 2013, The PAT margin also decreased to 6.06% in 2014, down from 10% in 2013.

Table 4: Profitability Margins

	FY 2014	FY 2013	FY 2012
GP* Margin	35.17%	39.76%	40.41%
EBIT Margin	8.81%	14.24%	15.71%
PBT Margin	9.02%	14.79%	16.48%
PAT Margin	6.06%	10.00%	11.16%

*GP – Gross Profit

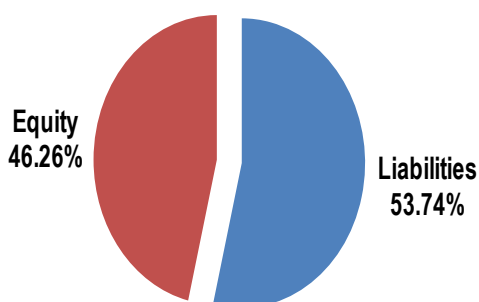


A cursory look at the balance sheet position as at FY 2014 compared with the position as at FY 2013 shows an increase in the company’s fixed assets. The total fixed assets increased by 10.70% to N13.42bn from N12.12bn in FY 2013. The inventory also increased to N7.59bn from N5.62bn in FY 2013. The cash and bank balances recorded a decrease of 56.70% from N3.92bn in FY 2013 to N1.70bn in FY 2014. Included in the Group’s cash balance is restricted cash of N256mn for unclaimed dividends of shareholders. The trade debtors and other receivables increased in FY 2014 by 22.75% to N4.98bn from N4.05bn in the FY 2013 period. The trade creditors and other payables also increased by 10.22% to N11.89bn from N10.79bn as at FY 2013. The working capital stood at N1.35bn from N2.31bn recorded in FY 2013, while net assets for the period increased by 4.88% to stand at N12.95bn from N12.35bn as at FY 2013.

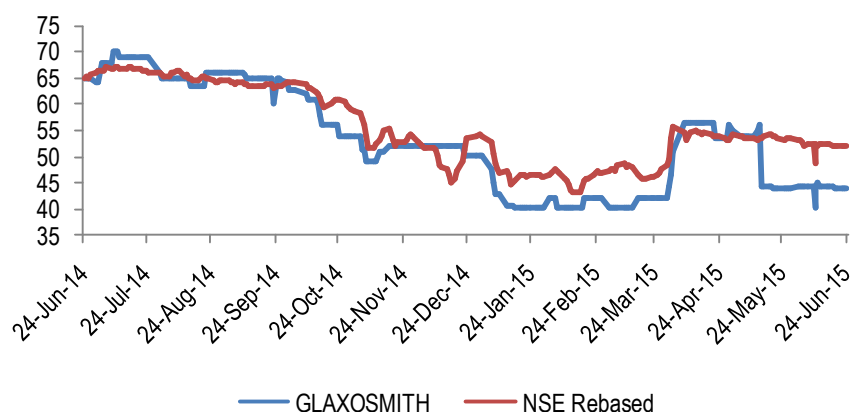
The total assets of the company which stood at N27.99bn as at FY 2014 were financed by a mix of equities and liabilities in the ratio of 46.26% and 53.74% respectively.

The total assets of the company which stood at N27.99bn as at FY 2014 were financed by a mix of equities and liabilities in the ratio of 46.26% and 53.74% respectively. Our analysis of the liabilities shows that the short-term liabilities stood at N13.22bn, accounting for 87.88% of the total liabilities, while the long-term liabilities stood at N1.82bn accounting for 12.12% of the total liabilities. The long-term liabilities constituted mainly of deferred tax liability, which stood at N1.69bn. The short-term liabilities constituted mainly of trade creditors and other payables.

Financing Mix



Glaxosmith VS NSE Rebased (Jun'14 - Jun'15)



1.1 Q1 Performance Analysis:

As at Q1 2015, turnover decreased by 4.45% to N7.46bn, compared with N7.80bn recorded in the corresponding period of 2014. The administrative, selling and distribution expenses increased by 8.86% to N2.15bn in Q1 2015. The company recorded a significant decrease of 77.63% in its net finance income of N4.50mn from N20.10mn in 2014. The PBT fell to N421.83mn, a decrease of 52.72% from N892.13mn recorded in the corresponding period of 2014. The tax provision decreased by 54.16% to N126.77mn from N276.56mn, leading to a PAT of N295.07mn in Q1 2015 from N615.57mn in the corresponding period of 2014, representing an decrease of 52.07%. We note that business activities were generally slow in Q1 2015 because of the general elections, the security issues in the country and the unfavourable macroeconomic situation in the country.

Given the run rate, the company is likely to meet its previous year's performance in turnover but unlikely to meet its previous performance in profit.

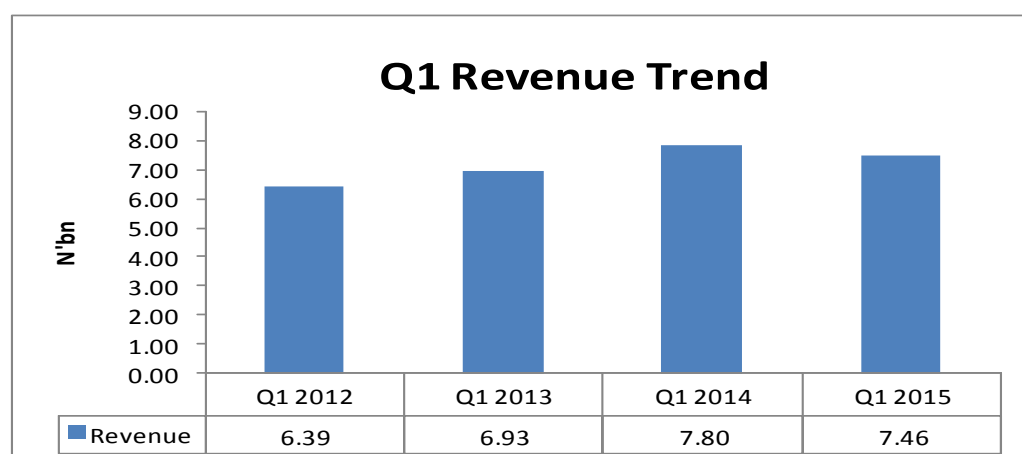
The PBT Margin decreased over the Q1 2014 and the Financial Year ended December (FY), 2014 figure. The PBT margin decreased to 5.66% in Q1 2015 from 11.43% as at Q1 2014 and 9.02% recorded at the end of FY 2014. Also, the PAT margin currently stands at 3.96%, down from 7.89% in the corresponding period of 2014, and also down from 6.06% as at FY 2014. The result also indicates that the percentage of T/O, PBT, and PAT in the Q1 2015 to the Audited T/O, PBT and PAT for the period ended December 2014 are: 24.43%, 15.33% and 15.96%, respectively. Given the run rate, the company is likely to meet its previous year's performance in turnover but unlikely to meet its previous performance in profit. However, given the strategic focus to advertisement, the company should gradually re-align on the profit margins.

Table 5: Profitability Margins (%)

	Q1 2015	Q1 2014	Q1 2013	Q1 2012
GP* Margin	39.21%	37.78%	39.13%	38.33%
EBIT Margin	5.60%	11.17%	12.07%	11.88%
PBT Margin	5.66%	11.43%	12.48%	12.28%
PAT Margin	3.96%	7.89%	8.61%	8.43%

Table 6: Financial Performance (N'bn)

	Q1 2015	Q1 2014	Change (%)
T/O	7.46	7.80	(4.45%)
EBIT	0.42	0.87	(52.14%)
PBT	0.42	0.89	(52.72%)
PAT	0.30	0.62	(52.07%)



2.0 Drivers of Performance:

Glaxosmith's earnings were impacted by the following:

Positive Factors:

- Large market size in Nigeria.
- Re-launch of Horlicks.
- Introduction of Panadol Suspension for children under the age of 12.
- Patronage received by Lucozade and Ribena.

Negative Factors:

- Stiff competition in the industry
- Outbreak of the Ebola Virus Disease (EVD) in West Africa.
- Counterfeit and parallel importation of drugs.
- Increased finance cost.
- Foreign exchange loss resulting in a rise in operating expenses.
- Security challenges in some parts of Nigeria

2.1 Strategic Focus:

Glaxosmith's current strategic priority is to focus on growing the new businesses and building the brand. For the coming years, the company's long term strategy is to redesign its Route-To-Market (RTM) with the focus to build momentum behind drinks and drive deeper and wider penetration and strengthen the non-drinks portfolio. The company will also focus on a commercial model that will ensure that distributor margins and investment are aligned to support growth. Glaxosmith will continue to make substantial investment in its Agbara factory in order to meet customer's demand and to maintain its edge over competition.

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The incidence of counterfeits and parallel imports continue to be a big challenge to the business, Glaxosmith has deployed strategies around appropriate supply chain capabilities route to market, consumer education and anti-counterfeiting technologies including the mobile authentication systems to arrest the trend and ensure that quality products are available to its customers.

We think the recent foreign exchange restrictions announced by the Central Bank of Nigeria (CBN) will also have a positive impact on the company's business as it will discourage some imports into the country.

3.0 Business:

GSK UK controls Glaxosmith's Nigeria through Setfirst Limited and Smithkline Beecham Limited who jointly own 46.42% of the shares of Glaxosmith Nigeria.

The principal activities of Glaxosmith are manufacturing, marketing and distribution of consumer healthcare and pharmaceutical products. The ultimate parent and controlling party is GlaxoSmithKline Plc, United Kingdom (GSK UK). GSK UK controls Glaxosmith Nigeria through Setfirst Limited and Smithkline Beecham Limited who together have a 46.42% stake in Glaxosmith Nigeria. The other 53.54% of Glaxosmith Nigeria shares are owned by Nigerian Shareholders. The registered office of the company is located in Ilupeju with regional sales teams across Nigeria. It also operates from warehouses in Ijanikin and Isolo Lagos. Global Manufacturing and Supply (GMS) is the manufacturing unit of the company and is located in Agbara, Ogun State. The site provides for the Nigerian market and now exports to Ghana. Glaxosmith has made substantial investments in the expansion of the Agbara factory to manufacture Oral Healthcare and Wellness products.

Table 7: Directors' Shareholding as at February 28, 2015

Director	Position	Holdings
Mr. Edmund C.Onuzo	Chairman	203,504
Mr. Thandalam Dayanand Sriram	Managing Director	Nil
Mr. Jonathan Murray	Executive Director	Nil
Mr Jonathan Girling	Non-Executive	Nil
Mr. Justin Korte	Non-Executive	Nil
Mr. Chinedum Okereke	Non-Executive	Nil
Mr. Samuel Kuye*	Independent Non-Executive	75,739
Mr. Lekan Asuni	Non-Executive	Nil
Mr. Babatunde Lemo	Independent Non-Executive	Nil
Mrs. Lubabatu Bello	Independent Non-Executive	Nil

*Joint beneficial holder of the 75,000 ordinary shares held by Stanbic IBTC Asset Management. Holds only 739 shares directly

Table 8: Shareholding Structure as at December 31, 2014

Shareholders	No. of Shares Held	% of Shareholding
Setfirst Limited	261,725,035	27.31%
Smithkline Beecham Limited	182,790,506	19.11%
Stanbic Nominees Limited	96,486,569	10.08%
Nigerian Public and Institutions	415,699,080	43.45%
Total	956,701,190	100%

Table 9: Company Summary

Ticker	GLAXOSMITH
Sector	Healthcare
Sub-sector	Pharmaceuticals
Date of Incorporation	June 23rd 1971
Date of Listing	1977
Financial Year End	December
Number of Fully Paid Share	1,195,876,488
Current Capitalization(NGN)	52,618,565,472
NSE Capitalization (NGN)	11,356,179,876,971.50
% of NSE Capitalisation	0.46%
52 Week high NGN	70.00
52 Week low NGN	40.00
YTD Return (%)	11.50%
52 Weeks Average Volume Traded	338,180
Trailing EPS NGN	1.20
Trailing P/E Ratio (X)	36.72x
<i>*As at the June, 24, 2015</i>	

4.0 Product Analysis:

Glaxosmith is one of Africa's largest consumer healthcare companies. Its portfolio consists of many well known brands, most of which are leaders in each of their respective product categories. It has two major reporting segments namely; Consumer Healthcare and Pharmaceuticals. Consumer Healthcare consists of oral care, over-the-counter (OTC) medicines and nutritional healthcare. Pharmaceuticals consist of prescription, pharmaceuticals and vaccines.

Glaxosmith is one of Africa's largest consumer healthcare companies.

4.1 Consumer Healthcare:

Consumer Healthcare is the largest contributor to Glaxosmith's revenue, contributing 70.14% in FY 2014. This segment contributed 37.20% to operating profit in FY 2014. About 95% of the Consumer Healthcare products are manufactured in Nigeria from the GMS site in Agbara, Ogun state.

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As at November 2014, the brands in the three sectors under the Consumer Healthcare segment are:

- **Oral Care:** Macleans range (Complete Care, Herbal, Intense Whitening, Fresh Mint and Milk Teeth), Sensodyne range (Daily Care, Gentle Whitening, Extra Fresh Mint and Rapid Action) and Parodontax Regular. Competitors in this segment include Close Up, Dabur Herbal, and foreign brands like Crest, Colgate and Listerine.
- **OTC Medicines (Wellness):** Panadol range (Regular, Extra, Suspension and Cold & Catarrh), Andrews Liver Salt (Lemon and Orange), Actifed (Syrup and Tablets) and Scotts Emulsion Cod Liver Oil (orange flavour). Competitors include Emzor's Paracetamol range, Fidson Healthcare Tuxil and Avipol range.
- **Nutritional Healthcare:** Lucozade range (Boost, Sparkling, Sports and HydroPure), Ribena range (Blackcurrant, Blackcurrant & Pineapple, Blackcurrant & Orange, Blackcurrant & Strawberry,

Consumer health is the largest contributor to Revenue contributing 70.14% in FY 2014.

Blackcurrant & Peach and Concentrate) and Horlicks (including Horlicks Malt (UK), Original and Chocolate). Competitors in this segment include Bournvita, Ovaltine, Milo, Rich Chocó, Capri- Sun, Apple & Eve, Bobo drink, Welch's juice, Kool-Aid and La Casera.

4.2 Pharmaceuticals:

Pharmaceuticals contributed 29.86% and 62.80% in FY 2014 to Glaxosmith's revenue and operating profit respectively. All pharmaceutical products are imported. The products under pharmaceuticals include:

- Antibiotics: Ampiclox, Amoxil Augmentin,
- Anthelmintic: Zentel
- Anti-Malaria: Halfan.

Competitors in pharmaceuticals include Emzor Pharmaceutical Industries with its range of anti-malaria drugs: Lokmal, Chloroquine and Maldox, range of antibiotics called: Emgyl, Emmox, Emcillin and Kezitol, range of Haematinics namely: Emzoron and Ferrous and Fidson Healthcare with products like Arthemed and E-mal (anti-malaria).

Pharmaceuticals contributed 29.86% and 62.80% in FY 2014 to revenue and operating profit respectively.

5.0 SWOT Analysis:

<p>5.1 Strengths:</p> <ul style="list-style-type: none"> ○ Strong brand name ○ Good knowledge of domestic market ○ Quality products in the market ○ Long standing reputation and reliability ○ Strong support from the parent company 	<p>5.2 Weaknesses:</p> <ul style="list-style-type: none"> ○ Rising finance costs ○ Declining margins ○ Rising input costs ○ Key customer risk
<p>5.3 Opportunities:</p> <ul style="list-style-type: none"> ○ Large market size in Nigeria ○ The passage of the National Health Bill in December 2014. ○ Foreign exchange restrictions on some items 	<p>5.4 Threats:</p> <ul style="list-style-type: none"> ○ Security challenges in the Northern region ○ Inadequate physical infrastructure in the country ○ Increasing cost of raw materials ○ Foreign exchange risk ○ Counterfeit and parallel imports

6.0 Forecast: Our Forecast Drivers

We considered the following factors in arriving at our 5-year forecasts:

Positive Factors:

- The company's good knowledge and expertise of domestic market.
- The passage of the National Health Bill.
- The management initiatives on product innovation.
- Drive to ensure operational efficiencies, leading to cost reduction.
- Growing local demand.

Negative Factors:

- Foreign exchange exposure and risk.
- The weak consumers spending power.
- Rising cost of raw materials.

Our forecast final dividend for the FY 2015 is N0.75 per share.

Looking at the medium to long term outlook of the company and the impact of the aforementioned factors, we are of the opinion that the impact of the positive factors would be higher on both the revenue and the profitability of the company than the negative factors. We therefore estimate a Turnover of N30.61bn, N33.00bn, N37.39bn, N42.36bn and N47.78bn for the periods ending December 2015, 2016, 2017, 2018 and 2019. We estimate EBIT of N2.71bn, N3.60bn, N4.11bn, N5.53bn and N6.34bn, and EBITDA of N3.98bn, N5.02bn, N5.69bn, N7.29bn and N8.32bn for the same period using EBIT margins of 8.86%, 10.92%, 10.99%, 13.04% and 13.28% respectively. Our PBT forecasts for the periods are: N2.82bn, N3.71bn, N4.22bn, N5.63bn and N6.46bn. Adjusting for tax, our PAT forecasts are N1.89bn, N2.49bn, N2.83bn, N3.78bn and N4.33bn. PAT Margin for the period are 6.18%, 7.54%, 7.57%, 8.92% and 9.06%. Our forecast final dividend for the FY 2015 is N0.75 per share.

Profit and Loss =N='bn	Dec-15	Dec-16	Dec-17	Dec-18	Dec-19
Turnover (Net Sales)	30.61	33.00	37.39	42.36	47.78
Cost of Sales	(20.06)	(20.97)	(23.76)	(26.07)	(29.31)
Gross Profit	10.55	12.03	13.63	16.29	18.48
Admin, Selling & Distribution Expenses	(6.68)	(7.13)	(8.08)	(9.15)	(10.33)
Depreciation	(1.27)	(1.42)	(1.58)	(1.77)	(1.98)
Other Operating Income	0.111	0.119	0.135	0.153	0.173
EBIT	2.71	3.60	4.11	5.53	6.34
EBITDA	3.98	5.02	5.69	7.29	8.32
Net Finance Cost	0.11	0.11	0.11	0.11	0.11
PBT	2.82	3.71	4.22	5.63	6.46
Taxation	(0.93)	(1.22)	(1.39)	(1.86)	(2.13)
PAT	1.89	2.49	2.83	3.78	4.33

	Dec-15	Dec-16	Dec-17	Dec-18	Dec-19
EBITDA Margin	13.02%	15.22%	15.22%	17.22%	17.42%
EBIT Margin	8.86%	10.92%	10.99%	13.04%	13.28%
PBT Margin	9.22%	11.24%	11.28%	13.30%	13.51%
PAT Margin	6.18%	7.54%	7.57%	8.92%	9.06%
EPS(N)	1.58	2.08	2.37	3.16	3.62
DPS(N)	0.75	0.99	1.13	1.50	1.72
Dividend Payout	47.58%	47.58%	47.58%	47.58%	47.58%
Earnings Yield *	3.28%	4.32%	4.91%	6.56%	7.52%
Dividend Yield *	1.56%	2.05%	2.34%	3.12%	3.58%
P/E Ratio*	30.45	23.16	20.37	15.25	13.31
Number of Shares ('bn)	1.20	1.20	1.20	1.20	1.20
ROE	13.40%	17.11%	19.39%	24.57%	27.97%
Inventory Turnover	2.73	2.73	2.73	2.73	2.73

**At Our Fair Value of N48.19*

Company	Glaxosmith	May & Baker	Fidson
Turnover (Net Sales)	30.52	7.02	9.72
Gross Profit	10.74	2.56	5.43
EBIT	2.69	0.74	1.43
PBT	2.75	0.10	0.87
PAT	1.85	0.06	0.63
GP Margin	35.17%	36.47%	55.91%
EBIT Margin	8.81%	10.49%	14.73%
PBT Margin	9.02%	1.44%	8.96%
PAT Margin	6.06%	0.90%	6.50%
ROE	14.28%	2.05%	10.96%
Net Assets	12.95	3.09	5.77
Net Assets Per Share	13.53	3.16	3.84
PE Ratio	34.38x	23.33x	10.15x
Earnings Yield	2.91%	4.29%	9.85%
<i>*As at June, 25, 2015</i>			

7.0 Valuation

We employed relative valuation method using Enterprise Value (EV) to Earnings Before Interest Tax Depreciation and Amortization (EBITDA) multiple. The assumptions and results of the valuation are:

Assumptions:

- EV/EBITDA Multiple: 14.04x
- Debt: Nil
- Cash: N1.70bn
- Number of shares in issue: 1.20bn

Applying the EV/EBITDA multiple of **14.04x**, we arrived at **N48.19** per share as the fair value.

The current market value of Glaxosmith share is N44.00, the highest and the lowest closing prices in the last 52 weeks are N70.00 and N40.00 respectively. The forward earnings yield and dividend yield of the company at our fair value is 3.28% and 1.56% respectively. The total return, a combination of the capital appreciation and the dividend, generates 11.23%. This is lower than the current yield on the FGN Bond of 13.98%. We therefore place a **HOLD** on the shares of GlaxoSmithKline Consumer Nigeria Plc at the price of N44.00 as of June 25, 2015.

The fair value for GlaxoSmithKline Consumer Nigeria Plc is N48.19.

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