

NASCON ALLIED INDUSTRIES PLC

...Cost Pressures Remain a Bottleneck



April 27, 2022

Earnings Note

Event

Nascon's ('the Company') challenges worsened into the new financial year, as reflected in her Q1 2022 financial performance. The Company continued to face rising cost pressures, amid an intense competitive environment. This resulted in significant margin erosion for the Company in Q1 2022. Revenue grew by 29% YoY to N10.76bn. We believe that the revenue growth was driven by higher volume growth and marginal price increase. However, cost of sales grew by a marked 62% YoY to N7.99bn, on the back of higher raw material costs – we link this to the continued impact of the covid-induced global supply chain bottlenecks, as well as the impact of the recent geopolitical conflict in the Eastern Europe. As a result of the higher cost of sales incurred during the period, gross margin shrank to 26% from 41% in Q1 2021, thus leading to a 19% YoY decline in gross profit.

Operating profit recorded a steeper decline (-83% YoY to N176mn), which was due to a 10% YoY rise in operating expense to N2.60bn. Selling and distribution expense was 12% higher than Q1 2021, resulting from higher logistics expense. We believe that the higher inflationary environment was responsible for this. Therefore, the rise in operating expense relative to the decline in gross profit translated to the significant dip in operating profit (-83% YoY to N176mn).

Partly supported by a N411mn foreign exchange gain, the decline in profit before tax moderated to 47% YoY. Profit after tax declined by 47% YoY as well to N386mn.

Financial Performance

Income Statement (N'mn)	Q1 2022	Q1 2021	% Change
Revenue	10,760	8,337	29%
Cost of sales	(7,995)	(4,925)	62%
Gross profit	2,765	3,413	-19%
Other income	10	4	161%
Operating income	2,775	3,416	-19%
Selling and distribution expense	(1,888)	(1,683)	12%
Admin expense	(712)	(671)	6%
Operating expense	(2,599)	(2,353)	10%
Operating profit	176	1,063	-83%
Interest income	58	14	321%
Interest expense	(76)	(13)	473%
Gains or losses	411	0	100%
Profit before tax	569	1,064	-47%
Income tax	(182)	(340)	-46%
Profit after tax	386	723	-47%
Balance Sheet Information (N'mn)	Q1 2022	FY 2021	% Change
Assets			
Non-current assets			
Property, plant and equipment	13,569	14,063	-4%
Right of use assets	3,800	3,838	-1%
Total non-current assets	17,369	17,901	-3%
Current assets			
Inventories	5,675	4,292	32%
Trade and other receivables	10,679	9,794	9%
Other assets	1,027	1,490	-31%
Cash and bank	9,662	7,044	37%
Total current assets	27,044	22,620	20%
Total Assets	44,413	40,521	10%
Liabilities			
Non-current liabilities			
Borrowings	39	39	0%
Lease liabilities	3,293	3,139	5%
Other non-current liabilities	2,493	2,495	0%
Total non-current liabilities	5,825	5,673	3%
Current liabilities			
Trade and other payables	18,052	14,090	28%
Lease liabilities	272	501	-46%
Other current liabilities	5,246	5,627	-7%
Total current liabilities	23,570	20,218	17%
Total liabilities	29,396	25,891	
Net Assets	15,017	14,631	3%

Source: Company Accounts, WSTC Research

SELL

Fair Value Estimate:
N8.83

Stock Data

Current price (N)	12.00
Shares Outstanding (mn)	2,649
Market Cap (N'mn)	31,793
52-week high (N)	16.00
52-week low (N)	12.90
Trailing EPS (N)	1.12
Forward EPS (N)	0.46
Forward PE (X)	25.82
Justified PE Multiple (X)	19.01

Price Movement



Stock Data

	FY 2020	FY 2021	FY 2022F
P/E	11.82x	0.70x	25.82x
P/BV	2.50x	2.17x	2.15x
PBT Margin	14%	12%	4%
PAT Margin	10%	9%	3%
RoE	23%	22%	8%
Dividend Yield	3%	3%	3%

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Outlook

We anticipated higher cost pressures in our previous report. Over the subsequent quarters of the year, we expect the pressures to persist. However, we believe that it will get to the point where the Company will effectively raise prices to protect margins. Based on our projection, we expect to see the impact of higher pricing in Q4 2022.

On the heels of the material decline in earnings level in Q1 2022, our revised earnings per share for the Company for FY 2022 is N0.46 ([previous](#): N0.79). That is, we now expect the Company to report significantly lower net profit in FY 2022 due to higher operating costs.

Despite our downward earnings revision, we estimate an N8.83 fair value for the stock (previous: N8.34). We modelled higher price increases beyond FY 2022 to protect margins. In our view, we posit that the current challenges leading to higher raw material costs are temporary.

Nonetheless, our recommendation for the stock is a SELL. At the current market price, the stock trades at a 27.75x forward price-to-earnings (P/E) ratio. We think that the fundamentals of the business and growth expectations of the Company do not justify the multiple. Using a blend of discounted dividend, discounted cash flow, and enterprise valuation methodologies, we believe that a 19.01x justified P/E captures the growth of the Company. Hence, we see a 32% price downside on the stock.

Financial Projections

Income statement (NGN mn)	FY 2021	FY 2022F	FY 2023F	FY 2024F	FY 2025F	FY 2025F
Revenue	33,280	44,647	54,470	59,368	64,711	70,540
EBITDA	5,102	5,011	7,989	10,073	11,949	13,554
EBIT	2,534	1,868	3,444	5,089	6,854	7,972
Profit before taxation (PBT)	4,238	1,811	3,364	5,011	6,790	7,917
Net profit (PAT)	2,971	1,231	2,288	3,408	4,617	5,383
EPS (₦)	1.12	0.46	0.86	1.29	1.74	2.03
DPS (₦)	0.40	0.40	0.43	0.64	0.87	1.02
Balance sheet (NGN mn)	FY 2021	FY 2022F	FY 2023F	FY 2024F	FY 2025F	FY 2025F
Current assets	22,620	33,702	37,791	41,026	45,122	50,303
Non-current assets	17,901	17,912	19,016	19,391	20,137	20,922
Total assets	40,521	51,614	56,807	60,416	65,258	71,225
Current liabilities	20,218	30,332	33,608	35,125	37,312	40,030
Non-current liabilities	5,673	6,480	7,169	6,998	6,739	6,914
Long-term debt	39	39	39	39	39	39
Shareholders' equity	14,631	14,802	16,030	18,294	21,207	24,282
Book value per share (₦)	5.52	5.59	6.05	6.90	8.00	9.16
Cash flow statement (NGN mn)	FY 2021	FY 2022F	FY 2023F	FY 2024F	FY 2025F	FY 2025F
Cash from operating activities	4,996	3,440	4,519	8,900	9,261	12,054
Cash from investing activities	1,098	(3,071)	(5,555)	(5,253)	(5,726)	(6,243)
Cash from financing activities	(1,676)	(344)	(349)	(1,473)	(2,050)	(2,249)
Net increase/ (decrease) in cash	4,418	25	(1,384)	2,174	1,485	3,562
Ratio analysis (%)	FY 2021	FY 2022F	FY 2023F	FY 2024F	FY 2025F	FY 2025F
EBITDA margin	15.33	11.22	14.67	16.97	18.47	19.22
Operating margin	7.61	4.18	6.32	8.57	10.59	11.30
ROAE	24.96	9.00	15.55	22.10	26.90	27.26
ROA	7.33	2.39	4.03	5.64	7.08	7.56
Dividend payout ratio	35.67	86.06	50.00	50.00	50.00	50.00

Source: Company Accounts, WSTC Research



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- Buy Rating: estimated fair value is $\geq 15\%$ above current market price.
- Hold Rating: estimated change in price is between -10% and 15% of current market price.
- Sell Rating: estimated change in price is $\leq -10\%$ of current market price.

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