UAC of Nigeria PLC: FY 2023 Results Conference Call Transcript

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Presenters:

- Mr. Fola Aiyesimoju (Group Managing Director)
- Mrs. Funke Ijaiya-Oladipo (Group Finance Director)

Moderator:

- Mrs. Temitope Omodele (Senior Vice-President)

1. Presentation

Moderator: Good morning and good afternoon, ladies, and gentlemen. Welcome to UAC of Nigeria PLC's full year 2023 results conference call. Please note that this call is being recorded.

This conference call will be hosted by Fola Aiyesimoju, the Group Managing Director of UAC of Nigeria PLC and Funke Ijaiya-Oladipo, the Group Finance Director. Following prepared remarks by UAC's management team, there will be an interactive Q & A session. I will now hand the call over to Fola Aiyesimoju, please go ahead.

Fola Aiyesimoju *(UAC Group Managing Director)*

Introductory remarks

Thank you Temitope and good day all. I have lost my voice at the most inopportune time, but I will do my best to be audible. Please turn to page 5.

For the financial year 2023, UAC recorded revenues and profit before tax of ₦120 billion and ₦12.3 billion respectively. Our profit included one-off gains from asset divestments and our treasury portfolio. Over the course of today's presentation, we will provide colour on the operating environment in 2023, discuss initiatives we executed over the course of the year, share insights on our financial performance and talk a bit about the outlook for 2024.

Our performance in 2023, in spite of challenging conditions, reflected the strength of our brands and distribution, management teams, risk management initiatives, and capital allocation decisions. Please turn to page 7.

Macroeconomic review

Operating conditions in 2023 were very difficult with low growth, currency devaluation, foreign exchange scarcity and high inflation. In addition to these, I am sure we all recall the very challenging first quarter of the year during which the effects of the attempted currency redesign program and election related uncertainty where most acutely felt. The elections were thankfully successful and while we are by no means out of the woods as an economy, we are encouraged by the current policy direction.

Page 8 reflects the impact of inflation on our businesses, with continued escalation of raw material prices as well as distribution and energy costs. Please turn to page 10.

2023 Strategic initiatives

Our primary focus in 2023 was on driving performance in spite of economic conditions. In addition, we executed a number of important initiatives.

We merged and integrated Spring Waters Nigeria Limited, producer of Swan Water with its parent company, UAC Foods, such that the businesses now operate as a single entity.

We unlocked ₦9.2 billion via the sale of non-core assets to bolster the group liquidity which we feel is important given the current economic conditions.

We have appointed Yemi Oloyede as Managing Director of UAC Foods, and he has had a very good first year. Debola Badejo returned to the holding company to drive our investment efforts, with Ufuoma Ogeleka being appointed General Manager at UAC Restaurants.

We streamlined Group governance and I now chair the boards of directors of our businesses, CAP, Grand Cereals, UAC Foods, and UAC Restaurants.

UAC brands and manufacturing footprint

On page 11, we reflect our brands. We are firmly of the view that our performance, under what were very difficult conditions, is directly related to the strength of these brands in our portfolio. We had a very successful launch of a new successful brand, Kingsway, which is trading strongly.

Page 12 reflects our nationwide manufacturing footprint and distribution that supports our brands, and these contributed to the improvement in key metrics reflected on page 13.

We recorded revenue growth, gross margin expansion, improvement in operating margins across all our key segments. We will take the business-specific updates on page 14 as read and Funke will run us through details on our financial performance.

Funke Ijaiya-Oladipo *(UAC Group Finance Director)*

Group financial performance

Good afternoon, ladies, and gentlemen. Please turn to Slide 16, which provides an overview of the Group's financial performance.

UAC Group recorded consolidated revenue of ₦121 billion in 2023, which is 10% higher year on year from the ₦110 billion recorded in 2022. Performance in the first half of the year was characterized by slower topline growth, which was impacted by limited trading during the general elections and scarcity of cash which affected consumer demand. In the second half of the year, we recorded stronger performance across all operating segments and delivered double digit growth in revenue, gross profit, and operating profit.

From the segmental perspective, our Animal Feeds and other Edibles segment, comprised of Grand Cereals and Livestock Feeds PLC, recorded revenue of ₦67 billion and this increased by a modest 2% year on year and was largely driven by price increases to offset rising raw material costs.

Our Packaged Food and Beverages business, UAC Foods, revenue was ₦29 billion, which is 23% higher year on year. The growth was on account of higher volumes recorded in the snacks category, which was supported by existing brands as well as the launch of a new brand, Kingsway Pastry Roll. It was also supported by volume growth in the Swan Spring water category as well as price reviews across board.

The revenue from our Paints business, CAP PLC, was ₦24 billion in 2023. This is 24% higher year on year and was achieved as a result of the positive impact of the company's growth strategy on volumes as well as price increases.

At a Quick Service Restaurants segment, we recorded a 21% revenue growth year on year, and this was driven by increase in sales from our company-owned restaurants.

In terms of operating profit, UAC Group recorded ₦9.1 billion in 2023, compared to an operating loss of ₦2.4 billion in 2022. The improvement in profitability is attributable to three factors. The first is the topline growth across our operating segments. The second is the gross profit margin expansion, particularly at our Animal Feeds and other Edibles segment and our Packaged Food and Beverages segment. The gross profit margin expansion was achieved due to deliberate cost-saving initiatives implemented to reduce conversion costs and energy costs across those businesses. There was also a focus on operational efficiency initiatives, and this was aimed at limiting the impact of the higher distribution and haulage costs experienced during the year. The third factor supporting our improved operating profit was the gain we recorded from the sale of non-core property assets.

Across the Group, our operating expenses were 17% higher year on year and this increase reflects the impact of inflation on our expenses as well as the effect of the Naira depreciation on expenses that are pegged to the foreign currency.

Our profit before tax was ₦12.3 billion compared to the loss before tax of ₦4 billion recorded in 2022, and this was supported by the improvement in our finance income and profitability of our associate companies. More specifically, the Group recorded net finance income of ₦2.4 billion in 2023, compared to a net finance cost of ₦2.1 billion in 2022. Our finance income was positively impacted by higher cash balances as well as gains in the Treasury portfolio.

The share of profit recorded from our associate companies was eight times higher at ₦860 million compared to the ₦103 million reported in 2022. This was driven by the expansion of MDS Logistics' transport business as well as the profit recorded at UPDC PLC, our real estate business.

We recorded ₦3.8 billion in free cash flow and our return on invested capital for the year was 20%. Please turn to Slide 17, which provides additional context on the key drivers of operating profit in 2023.

Additional context on operating profit

Our underlying operating profit, when adjusted for the non-recurring gain from non-core property assets, was ₦2.1 billion and this is an improvement when compared to the operating loss of ₦2.4 billion in 2022. The improvement was a result of the higher revenues recorded in our operating segments, the cost initiatives, which more than offset the impact of inflation across the Group.

Please turn to slide 18, which shows a snapshot of the Group's financial position as at the year ended 31 December 2023.

Group financial position

The group has net assets of ₦53 billion, which is ₦8 billion higher year on year. The increase can be largely attributable to the higher cash balance which was generated from the disposal of non-core assets throughout the year. Our net debt at the end of the year was ₦2.2 billion. Total debt across the group is ₦27 billion and this amount is largely short term in nature and used to support working capital across our businesses, particularly the Animal Feeds and other Edibles segment. We are conscious of the impact of finance costs on profitability, especially given the recent increases in the monetary policy rate and so we continuously seek to optimize funding costs across our businesses.

Across the Group, our capital expenditure for 2023 was ₦4.7 billion, and this was largely concentrated in the Packaged Food and Beverages segment. The investment represents the final phase of a bottling line that was installed to increase capacity of our spring water business in the first quarter of 2023.

Looking at our cash cycle, this increased slightly versus what we recorded in 2022 and that is reflective of the increase in advance payments at our various businesses to lock in favorable prices and to mitigate against the impact of increasing prices.

I will now hand the call back to Fola so he can take us through the next section of the presentation.

Fola Aiyesimoju *(UAC Group Managing Director)*

Thank you, Funke. Please turn to page 20.

Corporate action

We proposed a dividend of 22 Kobo per share, the same as was paid last year and we plan to hold our Annual General Meeting on the 20th of June.

In conclusion, on page 21, we expect economic conditions to continue to remain difficult over the course of 2024, and we have focused on maintaining margins via supply chain efficiencies and proactive pricing. We will seek to alleviate the impact of inflation on our employees by improving salaries and work conditions and ramp up our efforts to attract and develop leaders for our businesses. Thank you for listening to the presentation. We will now take questions.

2. Questions and Answers

Moderator

It is time for the Q&A session. To ask a question, please raise your hand or type in the chat box. Kindly introduce yourself and the organization that you represent before asking your question.

Your first question is from Chidinma.

Chidinma Opesanya *(Access Pensions)*

My name is Chidinma, a fund manager at Access Pensions, and I have two questions.

The first question is with respect to the conversion costs at the Animal Feeds and Edibles segment, could you please speak more to the actual cost management strategy that was implemented in the Animals Feeds and Edibles segment?

And the second question is what is the percentage of raw materials which are sourced locally and the percentage of raw materials which are sourced internationally across the business segments just to get a picture of foreign exchange exposure with respect to raw materials. Thank you.

Fola Aiyesimoju *(UAC Group Managing Director)*

Thank you, Chidinma. Your first question was around efforts to reduce cost of the Animal Feeds business, and you specifically talked about conversion costs. But in addition to conversion costs, there was a change in the route to market that meaningfully reduced distribution expenses. From a conversion cost perspective, the two biggest things were: one, a change of energy source – introducing in bio, as opposed to fire boilers, which is clean and cheaper than using diesel or heavy fuel oil.

And the second was just very many small production efficiencies, shift management, ensuring longer runs for bigger SKUs and the like. These several incremental gains resulted in the overall improvement in conversion costs.

Your second question was around the percent of raw materials sourced locally. I would say that, by far, the bulk of our raw materials across the Group are sourced locally. I think it is important for you to note that some of these raw materials are imported, and we buy them from domestic companies, but we do very, very little import. The only business that does meaningful importation of raw materials is our Paints business, and there I will put the number at around 40% or lower.

Onome Ohwovoriole *(Money Africa)*

Good afternoon, I am Onome an analyst with Money Africa. I have a couple of questions.

One, for your QSR business, I would say in line with the increased costs everywhere, do you have a timeline for when you would break even? That is one. And do you have an update on, I know in the last call, you had a number of restaurants you were looking at opening. Any update as to how many were opened last year and how many you expect to open this year? That is for the QSR.

Two is for the Paints business. I also remember at the last call, there was to be an expansion, I believe, into some paint line that could generate FX. So, is there any progress for that and what are the plans for the current financial year?

And three, for the Foods business, what has been the response of the market to the new products? That is one. How are you managing the cost pressures generally? Are you facing pressures from the commodity side of the Foods business and for the Feeds business as well? Thank you.

Fola Aiyesimoju *(UAC Group Managing Director)*

Thank you, Onome. I have three questions. On QSR, what is the timeline to break even? What is the outlook for opening restaurants? For Paints, what are our efforts to generate FX income? And for the Food business, market response to new products and how we are dealing with commodity or with raw material cost increases. Did these capture your questions, Onome?

Onome Ohwovoriole *(Money Africa)*

Yes.

Fola Aiyesimoju *(UAC Group Managing Director)*

Okay. For the Quick Service Restaurant business, we have about 30 restaurants open currently and there are two formats – there are what we call the big Corporate stores and then there are the Express stores. Our plan last year was to double that footprint, but we meaningfully slowed down our pace of expansion. And this was tied to, I guess, the first point you raised, which was meaningful escalation in costs, in particular, energy costs. We felt it was important to get a firm handle on the stand-alone economics of each store before continuing to accelerate the pace of store openings, which we are doing. Do I have a timeline to break even? We have a target to break even and we are hoping to get this business close at or close to breakeven within the next 12 months. And to achieve this, we would need to do two things. One is implement a number of the initiatives that we have put in place to manage energy costs at the restaurants; and two, we think we still need to at least double the footprint of profitable stores to get this to break even.

On the Paints business, there are two avenues for us to generate foreign exchange income. The first and easier is to scale our Marine and Protective category. We have a business that has so far sort of played second fiddle to the decorative category. Last year, we got full accreditation from the Nigerian Content Development Board, and that should meaningfully improve our ability to expand our offering in the oil and gas sector. This is an FX linked business. And we have recruited an individual to begin efforts to try to export products in the region and the person we recruited is currently based in Cameroon. So that is the secondary thing that we are doing to try to grow some FX income from the Paints business.

On the Foods business, the new product we launched was Kingsway Pastry Roll and I need to credit Yemi and his team. I think it is trading far ahead of my expectations. As we know, Gala is clear number one, and Kingsway, which was launched, I mean, just about six (6) months ago, in some months already begins to occupy the #3 position in the market. So, it is trading very, very well and I think it is a testament to the effort of Yemi and the team at UAC Foods.

We see price escalation everywhere across our businesses. You spoke about Foods and Feed in particular. But what we are is we are very disciplined around pricing and protecting our naked margin, which is selling price minus material costs. I think those efforts have so far translated into the improved profitability we recorded last year. We continue to keep our eye on the ball to maintain this pricing discipline going forward. You recall when I went through the presentation, that I think the foundation for this improved performance was on the strength of our brands and distribution. There is no way you can effectively dictate pricing if you do not have the kind of market-leading brands and nationwide distribution reach that we do.

Uthman Yuguda *(Stanbic IBTC)*

I wanted to ask about the profit on property sales. I noticed you made a considerable amount to the bottom line. Could you please shed some light onto that?

Fola Aiyesimoju *(UAC Group Managing Director)*

Very clear. Funke, do you want to take that question?

Funke Adesua Ijaiya-Oladipo *(UAC Group Finance Director)*

Okay. Thanks. I got the question. I think you asked about more information on the property sales. And I think you would have also seen in our results last year that one of our strategic initiatives is to essentially exit what we consider "non-core assets" and non-core assets are certain properties that UAC of Nigeria holds across the country. So, in line with that strategic initiative to unlock liquidity from low-yielding assets, we embarked to sell some of these assets, and that is the one-off profit you see in 2023.

Moderator: Your next question is from Edward Nwaokoro *(Stanbic IBTC)*. He asked – how does the business plan mitigate the challenges posed by FX this year? And please can you give more details on the expansion plan for the Paints business? Margins declined in 2023 when compared to 2022.

Fola Aiyesimoju *(UAC Group Managing Director)*

In terms of dealing with FX challenges, there are two things that are within our control. One is continuing to try to find sort of alternatives, raw and packaging materials at lower costs, and we had some success with that over the last 12 months. And the second is to be disciplined around pricing. The important thing for us is that, given our position in our various markets where we are mostly the market leader where we play, anything that affects us affects the rest of the market. And so, we found that once we have been disciplined with pricing to maintain margin, we have been fine in terms of generating profitability in spite of rising FX. So, we wish it was more stable, but we try to manage it by looking for alternatives and having pricing discipline.

The Paints business – Yes, the margins were lower last year, but if you follow that business, you would see that it is growing extremely fast. It was a business that was sort of flat in revenues for about five (5) years and has really tripled in size over the last three (3) years. And this requires meaningful investment in distribution, colour centers, and the salesforce to manage that increased retail footprint. And then there is a lag between investing in this improved reach and the profitability coming through, and so we continue to expand that business very aggressively over the next few years because we believe there is still opportunity for us to take.

Moderator: Your next question is from Sunmisola Ikoli-Oluwo *(CSL Stockbrokers)*. Sunmisola wants to know if the company is in a position to earn more from its exchange gain in 2024. She also wants to know if volume of production has been affected by the increase in commodity prices.

Fola Aiyesimoju *(UAC Group Managing Director)*

The short answer on whether we would earn more in exchange gain this year. I do not know. We are not a financial institution, so we do not think about foreign exchange as a profit or loss center. We try to make sure we have enough to meet our procurement needs for technical materials, new plant and equipment and so on and so forth. I keep stressing how we make sure we price – we are in the business of selling consumer goods profitably – we make sure we price those profitably regardless of the FX regime. So, we think about this more from keeping our business going and risk management, than trying to make money on a lot of FX. It is not our core job.

Around volumes, we have been surprised that over the last 12 months, where we have increased prices meaningfully in response to rising commodity prices. We have seen volumes hold or increase across our Paints business, across our Foods business. The one area where we saw dip in volumes was in the Animal Feeds segment of Grand Cereals. In the Edibles segment we saw massive growth in volumes. And that I guess is a combination of much higher prices as well as the challenges you would have read about in the Nigerian poultry farming industry.

Temiloluwa Oyenuga *(Meristem Securities Limited)*

Hi, thank you. Good afternoon. I want to ask regarding your Animal Feeds segment. I know that that segment has been pretty challenging for a couple of years now, and even looking at the revenue performance, there has been like decline for like the past 3 years. I think this year was just 1.5% growth in topline in that segment and that constitutes a larger part of total revenue. What is the company's plan on that particular segment? What are you trying to do to boost performance and increase profitability? The second question is regarding the FX, I know you just mentioned, someone just asked about it and I want to get more clarity about that particular aspect. I mean it was a major contributor to bottom line in 2023 and for 2024 are we expecting that much FX gains?

Fola Aiyesimoju *(UAC Group Managing Director)*

Okay, thank you. I think on Feeds, you point out that revenue growth was slow, but you would see that the swing in profitability of the Feeds business was quite meaningful. This is because of an increased focus in that segment on driving the higher-margin parts of the business. So, we are not trying to just grow scale in the Feeds business for the sake of scale, we are trying to drive profitability. The Feeds and Edibles business, we have historically, largely focused on the Feeds side. Now looking at the Edibles which is Pure Soya Oil and our Cereals in that business and also, even within the Feeds segment, there are higher margins so if you focus on the higher-quality feed niches, you would have lower volumes but higher margin. So, I think our focus there is not on volumes or revenues, our focus is on profitability. And so far, we have seen those results come through and that is going to be our continued focus in the near future.

On FX, I think what we successfully did in 2023 was avoid losses. So, we tried to almost under no circumstance, keep foreign exchange liabilities. And we try to get foreign exchange to buy the things we need to buy. So, I do not have a better answer, we do not budget or plan, or strategize to make FX gains. We just try to avoid losses, which is risk management, and try and make sure we have enough of what we need and price to make money regardless of whether or not the FX rate is a 1,000 or 2,000 to a dollar. So, I am sorry, I do not know a clearer answer, but we are not a hedge fund, we do not run our businesses to make money on FX. We try to avoid losses not try to make money from FX.

Dean Tlotleng *(Steyn Capital Management)*

Thank you for hosting this call today. I have three questions on my side. There has been some recent strength in the currency from about 1,700 to about 1,300 and there is some news as well that the queue has been cleared. My question is, have you been able to source FX and are you able to access those FX markets? The second question is, which of your businesses are you most positive about for 2024 and beyond and why? And third question is, you touched on some of the things you have done to simplify the group structure. Can you sort of give us an idea of what further plans you have for 2024 to further simplify the structure? And just the last question is, what are you currently seeing on the ground in terms of the Nigerian consumer?

Fola Aiyesimoju *(UAC Group Managing Director)*

Okay. Thank you, Dean. I think your first question was around what we are seeing around FX and ability to source. I would say because the market has been somewhat liberalized, yes, if we bid for FX at the right rate, we get. So, we have seen a meaningful improvement in FX liquidity experienced on the ground here.

The next was which of our businesses are we most positive about. And that is a quite impossible question to answer. What we do is we sit with the management teams of our respective businesses, and we work with those management teams to develop strategies that we are excited about. And the outcomes depend very much on what happens in the environment and the quality of execution. So, we are excited about the strategies that are in place for each of our businesses. The challenge is to work with the management teams or support the management teams, I mean, I think they do most of this stuff on their own, to execute those strategies and hope we get some tailwinds and not too many headwinds from the operating environment.

In terms of simplifying the group structure, it is not an event. It is something that is going to be constantly at the fore of our minds, which is how can we organize ourselves to be simpler. We do not have anything specific to announce now. We are a listed company so if we are going to make the announcement, there is a procedure we need to go through. But simplifying the group structure is core to the way we run the business. So, it is not a one-and-done.

The Nigerian consumer is stressed but I would say that, for me, the biggest takeaway from the current environment is surprise at the resilience of the consumer. So, we see a meaningful disconnect between the expectation of what the consumer should be doing and the experienced reality on ground, which I think is testament to the resilience of that consumer.

Moderator: Your next question is from Chidinma Opesanya who asked, do we expect to see more of these sizeable strategic sale of non-core assets this year and beyond?

Fola Aiyesimoju *(UAC Group Managing Director)*

So, I think I will link the response to what I just responded to Dean. A core part of our strategy, and one of the things we spend time on at the holding company, is capital allocation, which is thinking, where is our capital currently concentrated and is there a rationale to move that capital from a particular use to what we feel is a reuse that gives us a better risk-return outcome. Last year was real estate. It was not an operating company. So, it was non-core real estate. We do not anticipate any similar moves from a non-core real estate perspective. But we continue to work on the rest of the group and ask the question continually – where is that capital tied up and is there a scope to reallocate this capital?

Moderator: There are no more questions. I will now hand the call back to Fola Aiyesimoju for his closing remarks.

Fola Aiyesimoju *(UAC Group Managing Director)*

Thank you, Temitope. I thank everyone for participating in the call and for the questions, and I wish you a wonderful rest of the day.

Moderator: That concludes the UAC of Nigeria PLC Full Year 2023 Results Conference Call. Thank you for your participation. You may now hang up.