

KINGDOM SECURITIES

BAT Kenya Plc

Earning Updates – Full Year - 2020

BAT (K) FY-2020 Returns Saved by Covid-19 Initiative while Performance Suppressed by Regulations.

BAT Kenya posted a 42.0% increase in profits after tax (PAT) from KES 3.89Bn in FY19 to KES 5.52Bn. we recommend a HOLD on the stock with dividend payment the key driver as the current dividend yield stands at 10.2%. Profit before tax (PBT) grew by 34.0% y-y from KES 5.53Bn to KES 7.42Bn. Performance was boosted by lower VAT at 14% compared to 16%, a 3.1% decline in operational costs and a 5% reduction of corporate tax from 30% to 20% on government directive to cushion businesses. BAT (K) continues to control >75% of Kenya's market share while exports to more than 17 other markets in the region ensuring strong revenue stage. Directors recommended a KES 41.50 dividend per share for a payout of 81.6%, a 34.3% increase compared to KES 33.50 per share paid in 2019 for a payout of 86.2%. The stock continues to trade above 12 months average.

- The cigarette manufacturer performance managed to weather tough economic challenge due to Covid-19 pandemic to post a 2.5% decline in gross sales. Net sales improved by 5.4% on reduction of VAT from 14% to 16%. Sales performance was affected by contracting domestic sales necessitated by dipping consumer income and downgrading to lower priced offers.
- The company H2-2020 results helped cushion FY-2020 performance as second half net revenues grew by 58.4% compared to 53.0% in H2-19 while PBT increased by 102.3% against 53.7% in H2-19.
- Streamlining of operations and lower administration cost due to work from home moderation aided operating costs to declining by 3.1% y-y to push earnings before interest and tax (EBIT) up by 32.5%. This led to operating margins to increase 29.9% from 23.8% in 2019.
- The decline in local revenues was mitigated by higher export performance with Kenya's hub servicing more than 17 markets in the region.
- The PBT and PAT margins increased to 29.3% and 21.8% from 23.0% and 16.2% in 2019 respectively. Higher PAT helped enhance ROaE and ROaA to 51.1% and 25.4% from 40.8% and 19.4% respectively. ROCE increased to 60.7% on higher EBIT from 47.5% in 2019.
- Balance sheet saw shareholders' funds increase by 22.3% boosted by a 31.2% increase in retained earnings. A lower current liability pushed current ratio to 1.3 from 1.1 with equity ratio increasing to 54.8% from 44.5% same period in 2019.

Upside

- The reopening will grow sales both local and export sales. introduction of new markets will continue to grow sales for both cigarettes and cut rags.
- Product development will increasingly transition the business from cigarettes to alternative and innovative nicotine products that provide consumers with greater choice and less risk.
- Transformation of product portfolio has created international brand recognition which will help drive market share.

Bloomberg Ticker:	BATK
Company Statistics	
Recommendation	HOLD
Current Price	439.75
6 Month Av	361.17
52 Week Ave	360.88
12 Month High/Low	499.50 - 309.5
No of Shares ('000)	100,000
Market Cap (Bn)	43.98
Free Float	40.0%
EPS (LTM)	55.18
Dividend	45.00
PE (LTM)	8.0x
P/B (LTM)	3.7x
Dividend Yield	10.2%

P&L (KES Mn)	2018	2019	2020
Gross Revenues	36,496	39,827	38,845
Excise Duty and VAT	(15,746)	(15,788)	(13,506)
Net Revenues	20,750	24,039	25,339
OPEX	(14,531)	(18,313)	(17,750)
EBIT	6,219	5,726	7,589
PBT	5,881	5,533	7,416
Tax	(1,796)	(1,648)	(1,898)
PAT	4,085	3,885	5,518
EPS	40.85	38.85	55.18
DPS	35.00	33.50	45.00

Balance Sheet (KES Mn)	2018	2019	2020
Share Capital	1,000	1,000	1,000
Revaluation Surplus	1,820	1,756	1,756
Retained Earnings	6,490	6,959	9,129
Shareholders Fund	9,310	9,715	11,885
Non-Current Liabilities	3,237	1,871	1,576
	12,547	11,586	13,461
Assets	9,123	10,685	10,914
Working Capital			
Current Assets	9,216	11,122	10,792
Current Liabilities	(5,792)	(10,221)	(8,274)
Net Working Capital	3,424	901	2,518
	12,547	11,586	13,432

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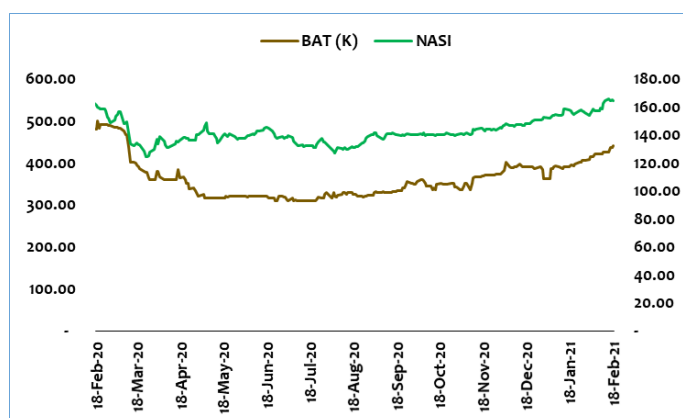
Downside

- In 2019, the company invested KES 2.5Bn in factory for the local manufacture of Lyft, an oral nicotine product without tobacco. The product has faced headwinds with anti-tobacco groups requesting for stringent regulations and even a possible ban.
- Solatium levy and inflation adjustment on excise duty continues to put pressure on sales with the new excise duty pushing the prices up by 4.9%.
- Illicit products continue to eat into the industry's revenues with the illicit cigarette market share hitting 23%.
- Proposed regulation, Tobacco Control Act Amendment Bill 2021, intends to review the minimum age of smoking and access to tobacco products from 18 to 21 years cutting off the younger appeal to tobacco products.

Key Ratios	2018	2019	2020
EBIT Margin	30.0%	23.8%	29.9%
PBT Margin	28.3%	23.0%	29.3%
PAT Margin	19.7%	16.2%	21.8%
ROaE	47.6%	40.8%	51.1%
ROaA	22.6%	19.4%	25.4%
ROCE	52.3%	47.5%	60.7%
Effective Tax	30.5%	29.8%	25.6%
Pay Out	85.7%	86.2%	81.6%
Current Ratio	1.6	1.1	1.3
Equity Ratio	50.8%	44.5%	54.8%

P&L (KES Mn)	2016	2017	2018	2019	2020	2017 %Δ	2018 %Δ	2019 %Δ	2020 %Δ
Gross Revenues	36,676	34,468	36,496	39,827	38,845	-6.0%	5.9%	9.1%	-2.5%
Excise Duty and VAT	(16,826)	(15,794)	(15,746)	(15,788)	(13,506)	-6.1%	-0.3%	0.3%	-14.5%
Net Revenues	19,850	18,674	20,750	24,039	25,339	-5.9%	11.1%	15.9%	5.4%
OPEX	(13,306)	(12,921)	(14,531)	(18,313)	(17,750)	-67.0%	-69.2%	26.0%	-3.1%
EBIT	6,544	5,753	6,219	5,726	7,589	-12.1%	8.1%	-7.9%	32.5%
PBT	5,911	4,867	5,881	5,533	7,416	-17.7%	20.8%	-5.9%	34.0%
Tax	(1,677)	(1,531)	(1,796)	(1,648)	(1,898)	-8.7%	17.3%	-8.2%	15.2%
PAT	4,234	3,336	4,085	3,885	5,518	-21.2%	22.5%	-4.9%	42.0%
EPS	42.34	33.36	40.85	38.85	55.18	-21.2%	22.5%	-4.9%	42.0%
DPS	43.00	26.00	35.00	33.50	45.00	-39.5%	34.6%	-4.3%	34.3%

Balance Sheet (KES Mn)	2016	2017	2018	2019	2020	2017 %Δ	2018 %Δ	2019 %Δ	2020 %Δ
Capital and Reserves									
Share Capital	1,000	1,000	1,000	1,000	1,000	0.0%	0.0%	0.0%	0.0%
Revaluation Surplus	1,902	1,861	1,820	1,756	1,756	-2.2%	-2.2%	-3.5%	0.0%
Retained Earnings	5,895	4,979	6,490	6,959	9,129	-15.5%	30.3%	7.2%	31.2%
Shareholders Fund	8,797	7,840	9,310	9,715	11,885	-10.9%	18.8%	4.4%	22.3%
Non-Current Liabilities	3,357	3,391	3,237	1,871	1,576	1.0%	-4.5%	-42.2%	-15.8%
	12,154	11,231	12,547	11,586	13,461	-7.6%	11.7%	-7.7%	16.2%
Assets									
Working Capital									
Current Assets	8,968	8,665	9,216	11,122	10,792	-3.4%	6.4%	20.7%	-3.0%
Current Liabilities	(6,346)	(6,574)	(5,792)	(10,221)	(8,274)	3.6%	-11.9%	76.5%	-19.0%
Net Working Capital	2,622	2,091	3,424	901	2,518	-20.3%	63.7%	-73.7%	179.5%
	12,154	11,231	12,547	11,586	13,432	-7.6%	11.7%	-7.7%	15.9%



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Recommendation Guide:

Analysts' stock ratings are defined as follows:

- **Buy** – A buy rating reflects 1) An analyst has a bullish conviction on a stock 2) A 10% or greater expected return.
- **Accumulate** – An accumulate rating reflects 1) An analyst has a lesser bullish conviction on a stock 2) Expected return falls between 5% and 10%.
- **Hold** – A hold rating reflects 1) An analyst has a neutral conviction (lack of bullish or bearish conviction) on a stock 2) Expected return falls within the range of -5% to +5%.
- **Speculative Buy** – A speculative buy rating reflects 1) An analyst has a bullish conviction accompanied by a substantially higher than normal risk 2) Expected return falls above 10%.
- **Sell** – A sell rating reflects 1) An analyst has a bearish conviction on a stock 2) Expected return falls below 5%.

*Expected Return (ER) represents the sum total of both capital appreciation and the dividend yield.

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