

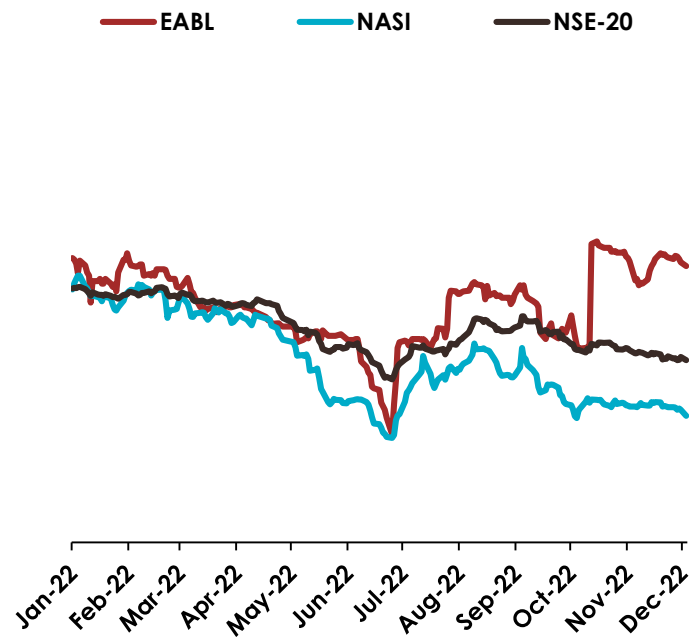
East Africa Breweries Limited (EABL) Update

Rating: ACCUMULATE	Current Price: KES 176.25	Target Price: KES 195.18
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Share Data

Bloomberg Ticker	EABL KN
Reuters ticker	EABL.NR
Current Price (KES)	176.25
Target Price (KES)	195.18
Upside	11%
Rating	ACCUMULATE
52WK High (KES)	180.00
52WK Low (KES)	110.00
Market Cap (Bn)	343.68
Shares outstanding (Mn)	1.95
Dividend yield (%)	2.2%
EPS (FY 2022)	15.0
P/E	11.7

Share price performance



Source: Bloomberg, NSE, NCBA IB Research

In this update, we revise our recommendation to **ACCUMULATE** with a revised target price of **KES 195.18**, implying an 11% upside relative to the volume weighted average price of KES 176.25 recorded on 31st January 2023 exclusive of dividend yield. We opine that investors who accumulate at current levels are set to unlock capital gains and dividend yield.

Target price		Rating	
Previous	Current	Previous	Current
KES 179.63	KES 195.18	BUY	ACCUMULATE

Source: NCBA IB Research Estimates

Eabl's financial position

HY2023 results saw performance improve slightly in a period deeply impacted by persistent high inflation as well as multiple excise tax increases in Kenya. Gross sales increased by 8% y/y to close at KES 107.66Bn. Further, 1HY23 performance was undermined by weaker revenue growth as a result of pallid GDP growth in the region.

Profit after tax (PAT), however remained relatively unchanged at KES 8.7Bn. PAT closed flat because revenue gains were offset by increases in cost of sales largely due to significant inflationary pressures on the cost of inputs over the period.

Regional subsidiaries support growth

Tanzania has stood out as the company's fastest growing market delivering continuous double-digit growth. In Tanzania net sales grew by 19% largely supported by Serengeti brands beer consumption, while in Uganda net sales grew by 11% supported by mainstream spirits and value beers.

Kenya on the other hand, saw a 1% decline as volumes dropped following multiple excise increases. EABL's current revenue contribution has Kenya, Uganda and Tanzania contributing 64%, 20%, and 16%, respectively.

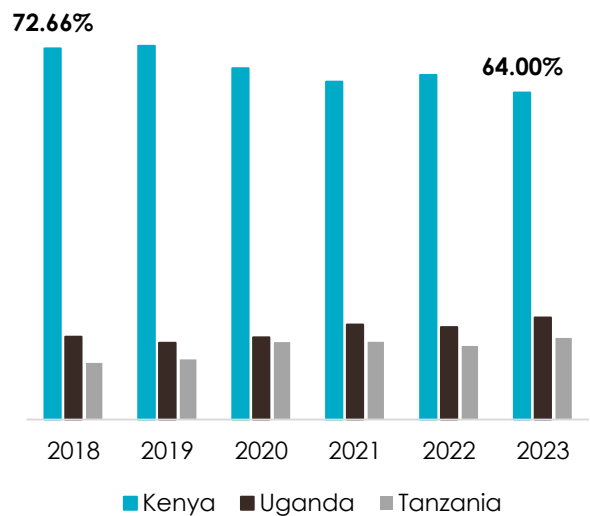
We estimate Tanzania share to grow to 25% in FY2023, a 500bps increase on the back of robust sales growth supported by sufficient brewing capacity.

Mainstream spirits support growth

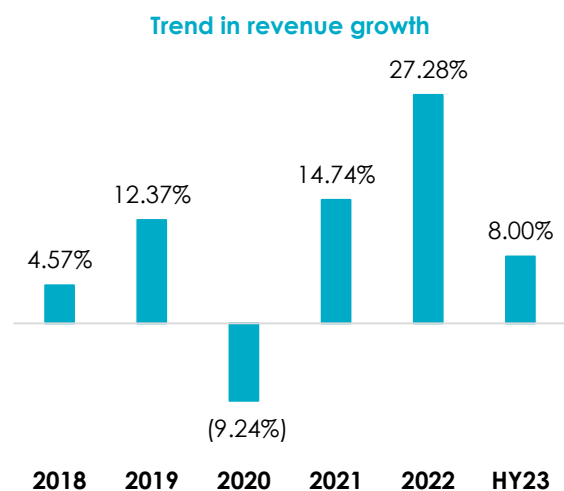
Continued consumption of spirits has become entrenched as the favorite for the vibrant young population.

Mainstream spirits growth has consistently outperformed the beer category. Net sales from spirits rose by 4% y/y (previously rose by 12% y/y) while the beer category grew by 2% y/y.

We expect growth in net sales in Kenya to be driven by continued growth in the spirits fueled by premiumization in spirits with brands like Tanqueray and Gordons. This has further been boosted by themed advertising and marketing events whose major sales are in the spirits category.



Source: Company financials, NCBAIB Research



Source: Company financials, NCBA IB Research

Steep increase in Kenya excise tax

Excise tax on beers increased by 17% to KES 142 per litre while that of spirits rose by 28% to KES 356 per litre.

EABL's margins have steadily declined following heavy taxation and excessive regulation on the business. As much as the tax implications are passed on to the final consumer, EABL recorded a decline of 1% in sales volumes from the Kenyan market.

EABL launched a lobbying frenzy against the excise tax hike with the view that the steep excise taxes negatively affect businesses and drive consumers to illicit harmful alcohol.

Consumers trade down to cheaper beers and their illicit counterparts to escape the tax which poses a threat to volume growth for the brewer.

Shift in consumer behavior

Weaker economic trends and pressure on real growth in consumer income has pushed the middle and lower income consumer globally, shifting consumption to more affordable products to either value beers or illicit brews.

We expect a diminished per capita alcohol consumption due to slower growth in consumer disposable income on the back of inflationary pressures and heavy indirect taxes.

Consumption in the upper income bracket continues to outpace GDP growth and is driving demand for local and international premium brands.

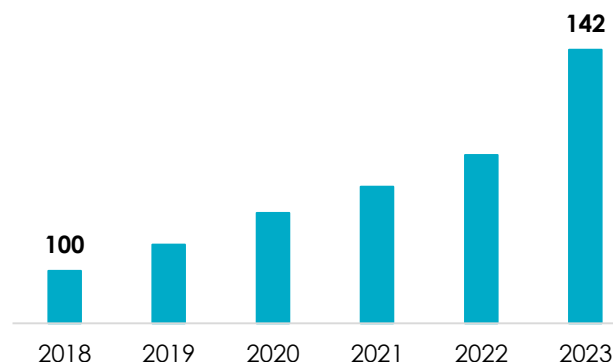
As reported by EABL, premium beers and spirits recorded sales growth of +13% y/y.

Dividend yield

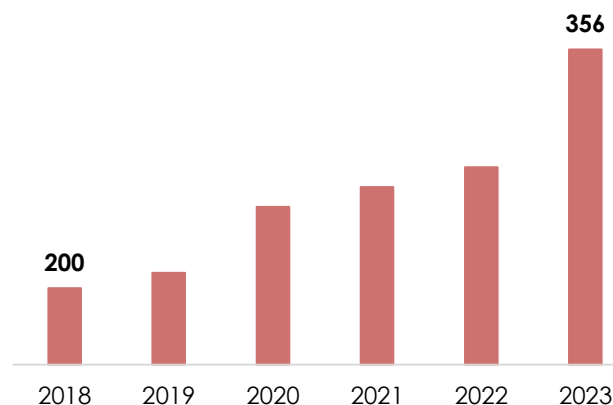
EABL declared an interim dividend of KES 3.75 for HY2023 which is a marginal increase from KES 3.50 in HY2022.

We expect that the company will declare a full year (FY2023) dividend for the period following steady revenue growth.

Beer excise tax KES per litre

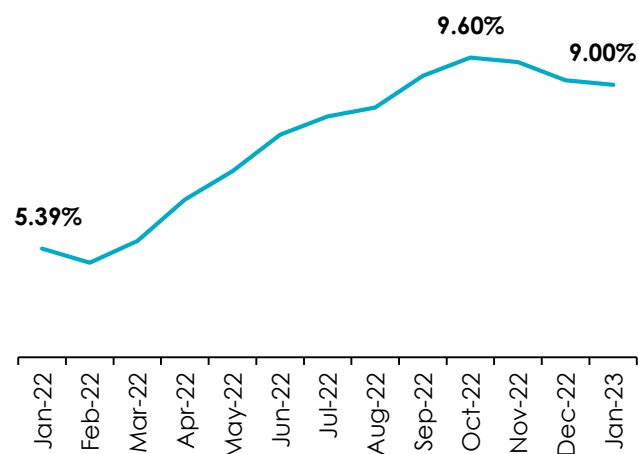


Spirits excise tax KES per litre



Source: Company financials, NCBA IB Research

Headline Inflation



Source: KNBS, NCBA IB Research

The Tender Offer:

Diageo Kenya announced that it received the requisite regulatory approvals for its proposed acquisition of up to 118,394,897 ordinary shares which represents a maximum of 14.97% of the issued share capital of EABL. We opine the share buyback is to bump up the stock price. We see this as a small price to pay for better long term positioning.

Companies execute share buy backs for various reasons among them;

- i) To improve the firm's financial ratios- Reducing the number of outstanding shares boosts return on assets (ROA) and Earnings per share (EPS) which consequently boosts investor confidence in the company.
- ii) To shore up its share price when the company believes its stock price is undervalued.
- iii) Paying off existing shareholders of the firm, so that they relinquish their claim over the firm, which reduces the number of investors that control the company.
- iv) The company is investing in itself which reflects management's confidence that the company has substantial room for growth.

EABL's share purchase will be executed by means of a partial tender offer at an offer Price of KES 192.00 per ordinary share. In a tender offer, the company solicits existing shareholders, (shareholders registered at the close of business on 16th January 2023) with a specified stock price.

The offer price implies a 9% premium from the current market price of KES 176.25 but is at a discount of 1.6% to what we believe to be the fair value of the company from our estimates.

Since the announcement the share price has rallied as shown below;

Price before announcement (13-Oct-22)	Current price (31-Jan-22)	Offer price	NCBA IB Research target price
KES 138.00	KES 176.25	KES 192.00	KES 195.18

Source; Company reports, NSE, NCBA IB Research estimates

NCBA IB Research Outlook

Despite the less than impressive 1HY23 performance, we believe EABL will continue to deliver relatively stable growth. We maintain a strong positive outlook for FY23 mainly driven by sales growth in regional subsidiaries.

However, we are cognizant of the fact that higher prices driven by excise taxes will negatively impact sales volumes given the high cost of living and thus increased consumer price sensitivity to substitutes.

Investment Case

Expected economic recovery to see an improvement in sales volumes.

The economy has gradually improved, the cost of inputs is declining, and supply chain disruptions have dwindled. The IMF projects the Kenyan economy to grow at 5.1% in 2023.

With inflation averaging 9.0% in January 2023 from a peak of 9.6% in October 2022, consequently the cost of inputs will decline.

We forecast an improvement in the manufacturing sector driven by continued infrastructural investment. The sector remains highly sensitive to the general economy and continued recovery in the business environment is anticipated to drive sales growth going forward.

Robust growth in regional subsidiaries underpins our outlook.

Volume growth in Tanzania to be supported by increased production from Serengeti Breweries. We opine that the Senator brand is a strong growth area capable of delivering double digit growth in Tanzania.

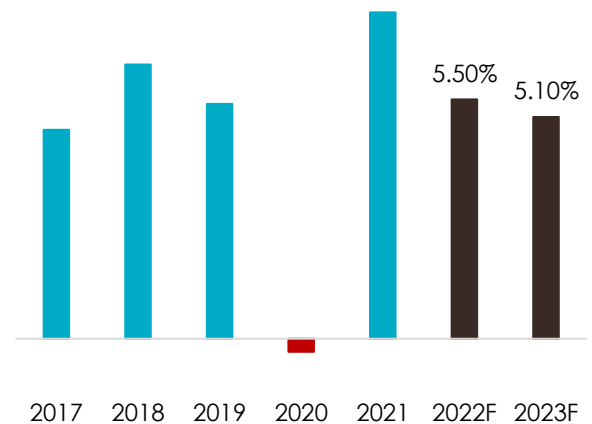
In Uganda, a gradual improvement in Uganda's economy (projected to grow at 5.9% by the IMF) underpins our optimistic FY23 EABL outlook.

In our financial forecasts, we estimate the company will grow at a rate of 5%, in line with the average GDP growth rate.

EABL has historically outperformed the GDP growth rate with an average growth rate of 10% because the company was in the growth phase of the business life cycle.

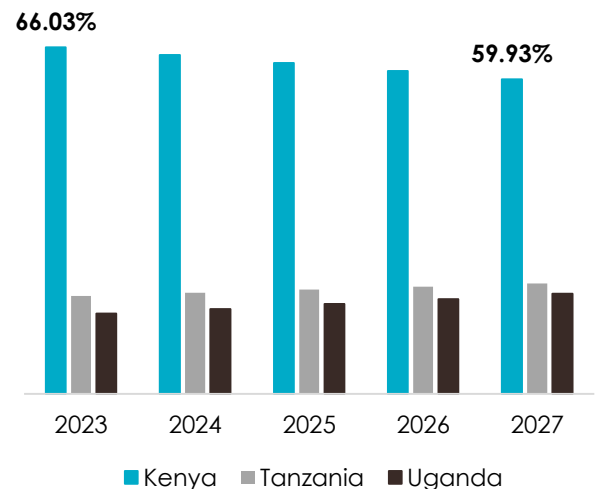
We opine that going forward, the company is in the mature phase and therefore, we see growth tracking the GDP growth rate.

Kenya Economic growth



Source: KNBS, NCBA IB Research

Revenue contribution by country NCBA IB Research forecasts



Source: NCBA IB Research estimates

Threats to our outlook

Downside risks include taxation in Kenya which is EABL's main market, accounting for 64% of revenue.

Adverse taxation has a negative impact on sales volumes.

In the fiscal year 22/23 tax revenue mobilization being a key policy for the government, excise tax on beverages, tobacco, alcohol products among others increased.

The prohibitive excise taxes in Kenya affected sales volumes in 1HY23 by a 1% decline. Though this is quite muted, it could have been worse, especially for the first half which outperforms the second half of EABL's financial year.

We see the negative impact increasing in 2HY23 especially for sales in the spirits which had the highest excise tax increment of 27.60% i.e., from KES 279 per litre to KES 356 per litre.

Any weakness in macroeconomic indicators in the region would pose a threat to our outlook.

2022 was a brutal year for all asset classes, globally, with emerging and frontier countries suffering their worst year in a decade.

Global growth is estimated to have slowed down from 6.0% in 2021 to 3.2% in 2022 attributable to a myriad of factors, among them; geo-political risks and lingering effects of the covid-19 pandemic, persistent inflationary pressures and a strong US dollar.

The KES depreciated against the USD by 9% in 2022 and there is a potential threat to it depreciating further.

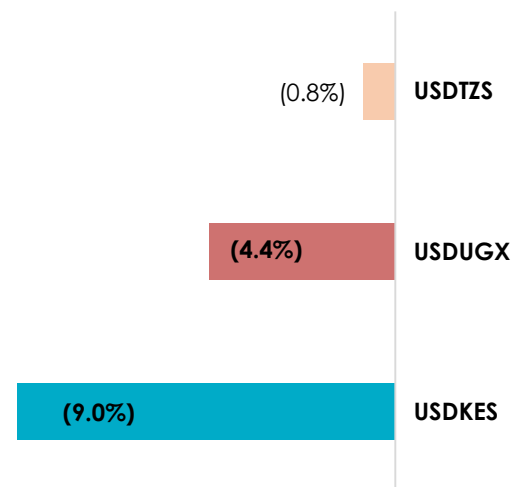
The region's exposure to these global risks is expected to transfer to corporate earnings and our financial forecasts.

Est. 5%-8%
Inflationary adjustment

In the 22/23 finance act, effective 1st october 2022 excise duty will be subject to an annual inflationary adjustment based on the average inflation for the previous fiscal year.

Source: Finance act 2022, NCBA IB Research

Depreciation of regional currencies against the US dollar in 2022



Source: Central banks, NCBA IB Research

VALUATION

Following the HY2023 earnings release, and given the key business announcement by the company, we have reviewed our forecasts and subsequently our valuation of the stock.

From our estimates and assumptions, we see a significant upside potential and recommend **ACCUMULATE** with a target price of **KES 195.18**. The target price implies an upside of 11% to the current trading price of KES 176.25 as of 31st January 2023.

Valuation Methodology	Implied Price	Weighting	Weighted Value
DCF Approach	192.79	70%	134.95
EV/EBITDA	174.08	10%	17.41
P/E Approach	210.90	10%	21.09
P/B Approach	217.31	10%	21.73
Fair Value		100%	195.18
Current Price (at 31.01.2023)			176.25
Upside/(Downside)			10.7%

Source: NCBA IB Research estimates

Relative Valuation: Regional Peers

Company	Location	Ticker	Mkt Cap (KES Bn)	EV/EBITDA	P/E	P/B	Dividend Yield
Champion Breweries Plc	Africa	CHAMPION NL	10.14	9.22	23.43	3.59	-
East African Breweries Plc	Africa	EABL KN	137.99	5.32	11.64	8.51	6.30%
Namibia Breweries Ltd	Africa	NBS NW	68.25	11.19	19.66	3.88	-
Nigerian Breweries Plc	Africa	NB NL	113.11	5.86	21.84	2.30	3.05%
Phoenix Beverages Ltd	Africa	PBL MP	23.58	8.73	20.11	2.06	2.68%
Sechaba Breweries Holdings	Africa	SCHB BG	21.34	9.61	10.87	2.59	6.25%
Tanzania Breweries Ltd	Africa	TBL TZ	171.60	10.60	22.00	4.60	2.66%
Zambian Breweries	Africa	ZABR ZL	25.07	14.81	-	3.15	-

Source: Bloomberg, NCBA IB Research estimates

Historical Financial performance (KES Mn)

Statement Of Comprehensive Income	2018	2019	2020	2021	2022
Kenya: Net sales Actuals	53,371,231	60,369,485	51,518,731	56,849,012	73,818,318
Uganda: Net sales Actuals	11,912,213	12,436,690	12,047,155	16,021,240	19,798,985
Tanzania: Net sales Actuals	8,173,388	9,737,066	11,350,373	13,091,563	15,791,724
Total Net Sales Actuals	73,456,832	82,543,241	74,916,259	85,961,815	109,409,027
Gross sales Actuals	135,037,775	149,660,062	133,351,955	152,572,477	193,849,847
Indirect Taxes Actuals	(61,580,943)	(67,116,821)	(58,435,696)	(66,610,662)	(84,440,820)
Total Revenue Actuals	73,456,832	82,543,241	74,916,259	85,961,815	109,409,027
Raw materials and consumables Actuals	(21,639,676)	(22,514,463)	(20,195,033)	(24,930,181)	(28,840,034)
Distribution and warehousing Actuals	(5,251,900)	(6,230,883)	(6,375,413)	(7,894,835)	(8,853,756)
Maintenance and other costs Actuals	(7,288,566)	(7,984,548)	(7,872,189)	(7,845,567)	(9,519,304)
Staff costs Actuals	(3,711,495)	(4,353,728)	(3,590,529)	(3,617,615)	(4,540,798)
Depreciation and amortisation Actuals	(3,160,772)	(3,342,482)	(3,863,065)	(4,259,924)	(4,799,137)
Cost Of sales Actuals	(41,052,409)	(44,426,104)	(41,896,229)	(48,548,122)	(56,553,029)
Gross Profit Actuals	32,404,423	38,117,137	33,020,030	37,413,693	52,855,998
Selling and distribution costs Actuals	(6,423,767)	(7,209,400)	(6,590,629)	(7,362,119)	(9,733,709)
Administrative expenses Actuals	(8,534,844)	(9,398,222)	(8,565,240)	(9,320,113)	(10,841,540)
Other (expenses)/income, net Actuals	(2,344,884)	(322,889)	(3,382,811)	(5,924,689)	(4,028,499)
Total Operating Expenses Actuals	(17,303,495)	(16,930,511)	(18,538,680)	(22,606,921)	(24,603,748)
Operating Profit Actuals	15,100,928	21,186,626	14,481,350	14,806,772	28,252,250
Finance income Actuals	81,949	120,601	164,873	91,242	184,528
Finance costs Actuals	(3,441,067)	(3,492,577)	(3,990,964)	(4,039,981)	(4,420,520)
Net Finance costs Actuals	(3,359,118)	(3,371,976)	(3,826,091)	(3,948,739)	(4,235,992)
Profit before income tax Actuals	11,741,810	17,814,650	10,655,259	10,858,033	24,016,258
Income tax (expense)/ credit Actuals	(4,486,255)	(6,299,520)	(3,634,344)	(3,896,093)	(8,441,859)
Total Net Profit After Tax Actuals	7,255,555	11,515,130	7,020,915	6,961,940	15,574,399

Source: NCBA IB Research Estimates, Company Financials

Financial forecasts (KES Mn)

Statement Of Comprehensive Income	2023	2024	2025	2026	2027
Kenya: Net sales Actuals	80,461,967	87,703,544	95,596,863	104,200,580	113,578,632
Uganda: Net sales Actuals	22,768,833	26,184,158	30,111,781	34,628,549	39,822,831
Tanzania: Net sales Actuals	18,634,234	21,988,396	25,946,308	30,616,643	36,127,639
Total Net Sales Actuals	121,865,034	135,876,098	151,654,952	169,445,772	189,529,102
Gross sales Actuals	213,234,832	234,558,315	258,014,146	283,815,561	312,197,117
Indirect Taxes Actuals	(91,369,798)	(98,682,217)	(106,359,195)	(114,369,789)	(122,668,015)
Total Revenue Actuals	121,865,034	135,876,098	151,654,952	169,445,772	189,529,102
Raw materials and consumables Actuals	(32,903,559)	(36,686,546)	(40,946,837)	(45,750,358)	(51,172,858)
Distribution and warehousing Actuals	(9,749,203)	(10,870,088)	(12,132,396)	(13,555,662)	(15,162,328)
Maintenance and other costs Actuals	(9,749,203)	(10,870,088)	(12,132,396)	(13,555,662)	(15,162,328)
Staff costs Actuals	(4,874,601)	(5,435,044)	(6,066,198)	(6,777,831)	(7,581,164)
Depreciation and amortisation Actuals	(6,858,546)	(8,320,927)	(9,951,440)	(11,771,299)	(13,804,649)
Cost Of sales Actuals	(64,135,112)	(72,182,693)	(81,229,267)	(91,410,812)	(102,883,327)
Gross Profit Actuals	57,729,922	63,693,405	70,425,685	78,034,960	86,645,776
Selling and distribution costs Actuals	(9,749,203)	(10,870,088)	(12,132,396)	(13,555,662)	(15,162,328)
Administrative expenses Actuals	(12,186,503)	(13,587,610)	(15,165,495)	(16,944,577)	(18,952,910)
Other (expenses)/income, net Actuals	(4,509,006)	(5,027,416)	(5,611,233)	(6,269,494)	(7,012,577)
Total Operating Expenses Actuals	(26,444,712)	(29,485,113)	(32,909,125)	(36,769,733)	(41,127,815)
Operating Profit Actuals	31,285,209	34,208,292	37,516,560	41,265,227	45,517,960
Finance income Actuals	184,528	184,528	184,528	184,528	184,528
Finance costs Actuals	(5,015,468)	(4,397,433)	(3,705,234)	(2,929,972)	(2,061,678)
Net Finance costs Actuals	(4,830,940)	(4,212,905)	(3,520,706)	(2,745,444)	(1,877,150)
Profit before income tax Actuals	26,454,270	29,995,387	33,995,854	38,519,784	43,640,811
Income tax (expense)/ credit Actuals	(9,258,994)	(10,498,385)	(11,898,549)	(13,481,924)	(15,274,284)
Total Net Profit After Tax Actuals	17,195,275	19,497,001	22,097,305	25,037,859	28,366,527

Source: Company financials, NCBA IB Research Estimates

About NCBA Investment Bank

NCBA Investment Bank is a subsidiary of NCBA Group. The services offered by the brokerage department include equities trading for listed securities, fixed income trading for both corporate and government bonds, Over the Counter (OTC) equity transactions as well as execution of equities transactions across the East African countries. Additionally, NCBA Investment Bank backs these activities with solid advice from the research team to enable investors meet their return objectives. NCBA Investment Bank deploys simple and convenient client driven technologies, robust risk management, highly competent and experienced staff and has the backing of robust research capabilities to differentiate itself from other players in the market.

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Certification

The following analyst(s) who prepared this research report: Victoria Mututu hereby certifies(y) that: (i) all of the views and opinions expressed in this research report accurately reflect the research analyst's(s') personal views about the subject investment(s) and companies (y) and (ii) no part of the analyst's(s') compensation was, is or will be directly or indirectly related to the specific recommendations or views expressed by the analyst(s) in this research report.

Rating Definitions

BUY – Total expected 12-month return (incl. dividends) greater than 20%
ACCUMULATE - Total expected 12-month return (incl. dividends) between 10% - 20%
HOLD – Total expected 12-month return (incl. dividends) between 0% -10%
SELL – Total expected 12-month return (incl. dividends) less than 0%

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