

24 October 2018

Okomu Oil Palm Company Plc.

Cost gains and lower finance charge to propel sturdy earnings

Update: Over 9M-18, OKOMU reported a 13.3% y/y growth in earnings, buoyed by sharp decline in COGS amidst relatively flat revenue and lower effective tax rate. We have revised our revenue estimate for 2018E slight lower to NGN20.86 billion (from NGN21.1 billion) to reflect weaker performance in Q3. To add, we cut our FY-18 projection for input cost to NGN3.19 billion (from NGN3.58 billion) which should neuter weaker topline amidst continued gains from lower finance charges. **Bringing it all together, we now expect earnings to climb 4.5% to NGN9.6 billion**

Weaker commodity prices underpin lower topline: For the rest of the year, we expect revenue to be slightly weakened by sustained moderation in commodity prices. Pertinently, lower global rubber prices led to lower rubber sale in Q3-18, and given OKOMU exports all its rubber production, pressured global rubber prices (-30.1% YTD to USD1.28/kg) will continue to drive benign rubber sale. Instructively, reflecting weakening global demand and expiration of cartel-like agreement among Thailand, Indonesia and Malaysia, rubber prices have sustained downtrend on the back of supply glut as producers continue to boost shipments. **Thus, whilst we maintain our FY-18 projection for CPO sales at NGN17.95 billion, we revise revenue projection for rubber to NGN2.91 billion (previously: NGN3.14 billion), reflecting the (1) weak volume and price performance in Q3-18 and (2) persisting supply glut, amidst weaker demand from China and brewing global trade concerns.**

Cost gains and lower finance charge to propel sturdy earnings: Elsewhere, we expect management's tight lid on input cost will continue to buoy gross margin which should largely offset rising operating expenses. Therefore, to reflect lower-than-expected COGS, together with faster rise in operating cost in Q3-18, we revise our input cost lower by 11% to NGN3.19 billion (prior forecast: NGN3.58 billion) and operating cost higher by 6.7% NGN6.57 billion (prior forecast: NGN6.16 billion). We highlight that higher operating cost continues to reflect the start-up operations at Extension II. The combined impact of the foregoing will lead to 2% y/y increase in EBIT to NGN11.3 billion.

No changes to finance expenses: Furthermore, we expect the soft interest charges to persist through the rest of the year as OKOMU had already paid down the FCY portion of its gross loan. Whilst we acknowledge that the company's debt position increased by 125.2% to NGN2.8 billion, we do not see any material impact on finance charges, at least through the rest of the year, as negotiation over potential moratorium is still ongoing before the commencement of payment. The increased debt was a drawdown from the concessionary loan (10% per annum) from the Bank of Industry (BOI) under the federal government's agricultural credit scheme

Valuation: Largely reflecting strong earnings growth in Q1, Okomu stock has rallied 17.9% YTD, outperforming the broader market's 13.8% loss. The stock trades at current P/E of 7.6x relative to 49.7x for Bloomberg peer average which is at a stack discount. On current market price of NGN79.80, our revised TP implies an upside of 14.75%, and expected total return of 19% after incorporating our 2018E dividend yield of 4.4%. We maintain our HOLD recommendation on the stock.

HOLD

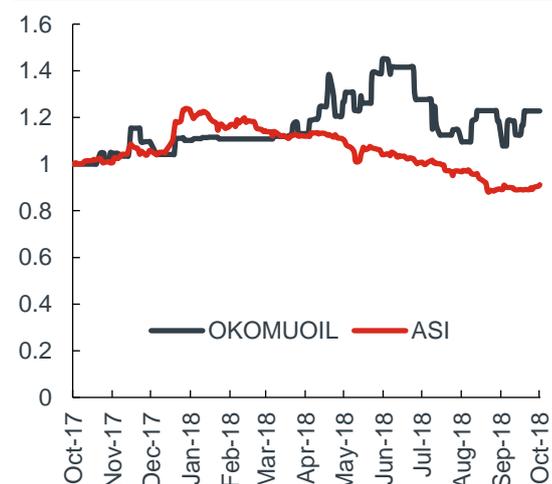
Target Price (NGN)	91.57
Current Price (NGN)	79.80
Implied Return (%)	14.6
2018E Dividend Yield (%)	4.4
Expected Total Returns (%)	19.0

Company Data

NSE Code	OKOMUOIL
Bloomberg Code	OKOMUOIL NL
Reuters Code	OKOMUOIL.LG
Sector	AGRICULTURE
Market Cap. (NGN' bn)	79.17
Free Float (%)	37.31

Ratios	Q3-2018	Q3-2017	2017FY
Gross margin	12.97%	12.11%	79.1%
Opex margin	5.49%	4.73%	25.0%
EBIT margin	5.95%	5.66%	54.9%
PAT margin	0.73%	1.77%	35.6%
EPS (NGN)	4.70%	4.80%	9.6

Price movement (OKOMUOIL vs. NSEASI)



Source: NSE, Bloomberg, Cordros Research

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Summary of quarterly results.

Income Statement (NGN'mn)	30-Sep-18	30-Sep-17	y/y % Δ	q/q% Δ	Q3-18	Q2-18
Revenue	16,685	16,586	0.6%	-8.9%	3,746	4,111
Cost of Sales	2,302	2,478	-7.1%	-57.7%	504	1,191
Gross profit	14,383	14,108	2.0%	11.0%	3,242	2,920
Operating Expense	5,637	4,891	15.3%	-9.9%	1,462	1,623
Other Income	-	-			-	-
EBIT	8,746	9,216	-5.1%	37.2%	1,780	1,297
Finance income	308	375	-18.0%	-44.4%	75	135
Finance charges	332	382	-13.0%	11.6%	78	70
Profit/Loss Before Tax	8,721	9,444	-7.7%	30.4%	1,776	1,362
Taxation	1,478	2,778	-46.8%	-60.4%	476	1,203
Profit/Loss After Tax	7,243	6,394	13.3%	718.2%	1,300	159

Ratios	30-Sep-18	30-Sep-17	Q3-18	Q2-18
Gross profit margin	86.2%	85.1%	86.5%	71.0%
Cost of sales ratio	13.8%	14.9%	13.5%	29.0%
Gross opex margin	33.8%	29.5%	39.0%	39.5%
Operating profit margin	52.4%	55.6%	47.5%	31.5%
PBT margin	52.3%	56.9%	47.4%	33.1%
Net profit margin	43.4%	38.6%	34.7%	3.9%
Effective tax rate	16.9%	29.4%	26.8%	88.3%

Source: Company Accounts, Cordros Research estimates

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Financial statements (NGN billion).

Income Statement (NGN'bn)	2015a	2016a	2017a	2018e	2019e	2020e	2021e	2022e	Profitability Ratios	2015a	2016a	2017a	2018e	2019e	2020e
Turnover	9.74	14.36	20.26	22.18	28.73	31.51	32.71	34.44	Gross margin	64.8%	75.0%	79.1%	80.0%	80.0%	80.0%
Cost of sales	-3.43	-3.59	4.23	-4.44	-5.75	-6.30	-6.54	-6.89	Operating Margin	33.7%	48.4%	54.9%	50.2%	57.5%	57.5%
Gross Profit	6.31	10.78	16.04	17.75	22.98	25.21	26.17	27.55	EBITDA Margin	44.5%	56.7%	61.2%	59.2%	66.0%	66.0%
other income	0.29	0.12	0.15	0.22	0.29	0.32	0.33	0.34	PBT Margin	29.8%	41.1%	55.0%	50.7%	58.0%	58.5%
Admin Expenses	2.27	-2.02	3.11	-3.34	-4.31	-4.73	-4.58	-4.82	Net Margin	27.0%	34.2%	45.1%	45.0%	46.4%	46.8%
Depreciation	-1.05	-1.20	-1.28	-1.98	-2.44	-2.68	-2.65	-2.86	ROAE	24.3%	33.8%	44.1%	37.3%	38.2%	33.1%
Total OPEX	-3.32	-3.94	-5.06	-6.83	-6.75	-7.40	-7.23	-7.68	ROAA	13.9%	22.0%	32.7%	29.0%	30.7%	29.6%
EBIT	3.28	6.96	11.13	11.14	16.52	18.12	19.27	20.22							
EBITDA	4.33	8.15	12.40	13.12	18.96	20.79	21.92	23.08	Liquidity Ratios	2015a	2016a	2017a	2018e	2019e	2020e
Interest income	0.04	0.29	0.49	0.44	0.57	0.63	0.33	0.28	Working capital (NGN'bn)	460.6	(1,067.7)	3,971.2	(958.7)	330.5	483.6
Interest Expense	-0.43	-1.34	0.48	-0.34	-0.43	-0.32	-0.39	-0.34	Current ratio (x)	1.1	2.0	1.9	2.8	4.9	8.5
Net Interest Earnings	-0.39	-1.05	0.01	0.10	0.14	0.32	-0.07	-0.07	Quick Ratio (x)	0.5	1.4	1.2	2.1	3.7	6.5
Profit-before-tax	2.90	5.91	11.14	11.25	16.66	18.43	19.20	20.15	Cash Ratio (x)	0.4	1.1	0.8	1.9	3.1	5.5
Taxation	0.27	1.00	1.99	1.26	3.33	3.69	3.84	4.03							
Profit-after-tax	2.63	4.91	9.15	9.99	13.33	14.75	15.36	16.12	Solvency Ratios	2015a	2016a	2017a	2018e	2019e	2020e
									Debt to Equity	30.9%	16.4%	5.1%	14.7%	7.5%	0.0
									Debt to Capital	23.6%	14.1%	4.9%	12.8%	7.0%	0.0
									Financial Leverage (x)	1.5	1.5	1.3	1.0	1.0	1.1
									Interest Coverage (x)	7.7	5.2	23.0	114.2	38.3	57.5
Financial Position (NGN'bn)	2015a	2016a	2017a	2018e	2019e	2020e	2021e	2022e	Activity Ratios (x)	2015a	2016a	2017a	2018e	2019e	2020e
Fixed Assets	9.85	9.22	11.22	14.12	16.22	18.69	22.02	27.40	Inventory Turnover	0.6	0.6	0.5	0.3	0.4	0.4
Biological Asset	7.40	9.40	12.90	13.31	15.29	17.62	20.76	25.83	Payables Turnover	1.0	1.2	1.9	1.0	1.5	2.8
Total Fixed Assets	17.24	18.62	24.12	27.43	31.51	36.31	42.77	53.23	Asset Turnover	0.5	0.6	-1.4	0.6	0.6	0.6
Inventories	1.49	1.72	2.69	3.07	3.52	4.06	4.78	5.95	Fixed Asset Turnover	1.0	1.6	1.8	1.6	1.8	1.7
Trade receivables	0.06	0.12	0.47	0.35	0.40	0.45	0.52	0.63							
Due from related companies	-	0.47	0.50	-	-	-	-	1.49							
Other receivables	0.30	0.38	0.51	1.01	1.39	1.60	1.89	2.35							
Cash at bank and in hand	0.96	3.20	3.09	8.48	9.52	10.98	12.95	14.64							
Total Current Asset	2.81	5.89	7.26	12.91	14.83	17.09	20.13	25.05							
Total Assets	20.05	24.51	31.37	40.33	46.34	53.40	62.90	78.27	Investment Ratios	2015a	2016a	2017a	2018e	2019e	2020e
Trade Creditors	0.89	0.64	0.49	1.14	0.74	0.50	0.53	0.45	DPS (NGN)	0.1	1.5	3.0	3.7	4.8	6.2
Other Creditors	0.58	0.11	0.03	0.41	0.27	0.20	0.21	0.18	EPS (NGN)	2.8	5.1	9.6	10.9	14.0	15.4
Due to related companies	0.01	0.00	0.00	0.05	0.03	0.02	0.03	0.02	Payout Ratio	3.6%	29.1%	31.0%	34.0%	34.0%	40.0%
Borrowings	0.34	0.37	0.49	0.50	0.35	0.26	0.27	0.24							
Retirement Benefit Obligations	0.02	0.43	0.44	0.07	0.02	0.01	0.06	0.05							
Bank Overdraft	0.00	0.00	0.00	1.03	0.68	-	-	-							
Dividend Payable	0.06	0.06	0.06	0.11	0.08	0.07	0.08	0.07							
Taxation	0.61	1.39	2.26	1.30	0.86	0.63	0.67	0.57							
Total Current Liabilities	2.52	3.01	3.77	4.60	3.03	2.24	2.36	2.03							
Long Term Loans	3.39	2.42	0.77	2.93	1.93	1.42	1.50	1.29							
Deferred taxation	1.73	1.76	1.66	2.30	1.52	1.12	1.18	1.01							
Staff Retirement benefit	0.35	0.32	0.67	0.44	0.29	0.75	0.74	0.63							
Total Non-Current Liabilities	5.47	4.49	3.10	23.21	26.55	30.60	36.04	44.85							
Total Liabilities	7.99	7.50	6.87	10.27	6.77	4.99	5.27	4.53							
Net Asset/Equity	12.06	17.01	24.51	30.23	39.56	48.41	57.63	73.75							
Share Capital	0.48	0.48	0.48	0.48	0.48	0.48	0.48	0.48							
Share Premium	1.87	1.87	1.87	1.87	1.87	1.87	1.87	1.87							
General Reserves	9.72	14.67	22.16	27.89	37.22	46.07	55.28	71.40							
Shareholders' Funds	12.06	17.01	24.51	30.23	39.56	48.41	57.63	73.75							

Source: Company Accounts, Cordros Research estimates

Disclosures.

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