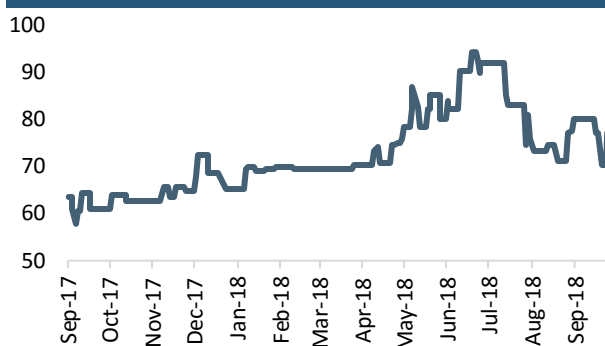




Rating	STRONG BUY
Price	₦79.80
52-week range	₦70.1 – ₦94.7
Market Cap. (₦bn)	66,869
1-month Avg. Vol	155,377
Current PE	8.29x

OKOMUOIL: NL - Share Price Trend



Analyst(s)

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The Okomu Oil Palm Plc (OKOMUOIL.NL)

Initial View

Lower cost of sales propels earnings

- Last Friday, The Okomu Oil Palm Plc (Okomu) released its Q3 2018 result wherein earnings rose to ₦1.3billion vs ₦159 million in Q2 17, translating to an EPS of ₦1.36. This represents a rebound in earnings following a weak Q2 18. Cumulatively, PAT was up 13.3% YoY to ₦7.2 billion, translating to a 9M 18 EPS of ₦7.59.
- Further breakdown reveals that the company recorded revenue contraction of 8.9% to ₦3.75 billion largely driven by the free fall of global CPO prices (-21% YoY to \$512/MT) and rubber prices (-9% YoY) in the period. For context, given that Okomu's CPO prices largely mirrors global prices, local CPO prices contracted 6% YoY over the period. However, we think volumes rose during the period (+5% YoY) which accounts for the tamer flattish growth in CPO sales (+1 YoY to ₦3.15 billion) over Q3 18. Elsewhere, given that Okomu exports all its rubber, export sales (-36% YoY to ₦598 million) were marred by plunging rubber prices in the period.
- Over Q3 18, cost of sales (-55.9% YoY to ₦504 million) eased with Okomu recording its lowest cost to sales ratio (Q3 18: 13.5% vs 29% in Q4 18) in eight years. This came as a surprise as Okomu usually records higher cost over H2 18 which is usually its planting season. More so, the firm has been grappling with bottlenecks in achieving its planned energy mix due to the failure of Benin Electricity Distribution Company (BEDC) to supply adequate power due to disruptions. We seek to get further clarity from management regarding the driver of the tamer cost of sales over the period. Accordingly, on the back of lower than expected cost of sales, gross margin expanded to 86.5% from 71% in Q3 17.

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- Further down, in lock step with declining cost of sales, operating expenses dipped 9.9% to ₦1.46 billion with OPEX to sales plunging 50bps YoY to 39%. As a result, EBIT margin jumped to 47.5% from 31.5% in the prior year. Overall, despite lower finance income (-44.4% YoY to ₦75.2 million),—which is reflective of lower foreign exchange gain emanating from the stability in the naira as well as lower yield environment— and higher interest expense (+11.6% YoY to ₦78.4 million), earnings spiked from ₦159 million in the prior year to ₦1.3 billion over Q3 18.
 - Okomu trades at a current P/E of 8.29x which is at a discount to MENA peer average of 13.5x and Presco of 9.2x. We have a **FVE** of **₦92.45** which translates to a **STRONG BUY** rating on the stock.
 - **More analysis to follow.**
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Summary of Results and Forecast

Income statement – (₹ million)	Q3 18	YoY growth	QoQ growth	Deviation from forecast	9M 18	9M 17
Revenue	3,746	-8.9%	-33.1%	-19.9%	16,685	16,586
Cost of sales	504	-57.7%	-55.9%	198%	2,302	2,478
Gross profit	3,242	-11%	-27.2%	-54%	14,383	14,108
OPEX	1,462	-9.9%	-2.9%	-47%	5,637	4,881
Operating profit	1,780	37.2%	-39.6%	-21%	8,746	9,227
Finance expense	78.5	11.6%	-37.5%	-62%	332	437
PBT	1,776	30.4%	-40.1%	-19%	8,720	9,173
PAT	1,300	718.2%	-47.3%	12%	7,243	6,394

Key Ratios	Q3 18	Q3 17	Change(pps)	9M 18	H1 17	Change(pps)
Gross margin	86.5%	71.0%	15.5%	86.2%	85.1%	1.08%
EBIT margin	47.5%	31.5%	16.0%	56.4%	55.6%	-6.51%
PBT margin	47.4%	33.1%	14.3%	52.3%	55.3%	-5.78%
PAT margin	34.7%	3.9%	30.8%	43.4%	38.6%	-2.01%
Effective tax rate	26.8%	88.3%	-61.5%	16.9%	30.3%	3.2%

Source: ARM Research *unless otherwise stated

ARM ratings and recommendations

ARM now employs a two-tier rating system which is based on systemic importance of the security under review and the deviation of our target price for the stock from current market price. We characterize systemic importance as a function of a stock's ranking among the group of top 20 stocks by NSE market capitalization over a trailing 6-month period (minimum) to the review date. We adopt a 5-point rating system for this category of stocks and a 3-point rating system for stocks outside this group. The choice of top 20 stocks arises from the consideration that this group of stocks constitutes >75% of overall market capitalization and stocks outside this group are generally less liquid and individually account for <<1% of market capitalization. For stocks in both categories, the basis for ratings subject to target price deviation is outlined below:

TOP 20		NON-TOP 20	
Rating	Deviation	Rating	Deviation
STRONG BUY	>20%	BUY	>20%
OVERWEIGHT	10% — 20 %	NEUTRAL	5% — 20 %
NEUTRAL	0% — 10 %	SELL	<5%
UNDERWEIGHT	-5% — 0%		
SELL	<-5%		

RECOMMENDATION KEY	
Rating	Recommendation
BUY	Accumulate security to a substantial extent constrained only by portfolio diversification considerations
OVERWEIGHT	Accumulate security to an extent moderated by cognizance of its benchmark weight
NEUTRAL	Maintain status quo for security with respect to current holding—i.e. keep if already holding and don't buy otherwise—subject to reasonable portfolio constraints
UNDERWEIGHT	Minimize exposure to security taking cognizance of its index weighting
SELL	Sell-off security completely from portfolio
RESTRICTED	In certain circumstances, Asset & Resource Management ("ARM") Group policy and/or applicable law and regulations preclude certain types of communications, including an investment recommendation, during the course of ARM Securities' and/or ARM Group's engagement in an investment banking transaction and in certain other circumstances.

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