



Equity Research | Oando Plc

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Lingering COP deal dampens Oando Plc earnings outlook: cues from OER

Recommendation: SELL

- Oando Energy Resources (OER) a subsidiary of Oando Plc's (Oando), recently released its FY 2013 results on the TSX wherein revenues declined 5.9% YoY to \$127.2 million on account of lower crude oil production. OER also reported a loss-before-tax (LBT) and loss-after-tax (LAT) of \$27.2 million (~~₦~~4.3 billion) and \$38.2 million (~~₦~~6.1 billion), respectively, compared to 2012 PBT and PAT of \$52.1 million (~~₦~~8.3 billion) and \$16.0 million (~~₦~~2.6 billion).
- Management attributed losses to interest charges incurred on loans related to the funding of the COP deal, delays which directly contributed to finance charges tripling YoY to \$55.4 million (~~₦~~8.9 billion). Furthermore, earnings were also adversely impacted by general and administrative expenses, which more than doubled YoY to \$42.6 million (~~₦~~6.8 billion) in 2013. In particular, the latter rise was driven by a 6-fold spike in 'consulting and professional fees' to \$21.5 million (~~₦~~3.4 billion) in 2013 which is again likely related to the COP deal which was meant to be completed in September 2013.

Income Statement Data

	2013- 9M'm	2012 -9M'm	%chg
Revenue	386,251	487,770	-21%
PBT	9,761	1 9,859	-51%
Tax	(3,669)	(8,135)	-55%
PAT	6,092	11,646	-47%

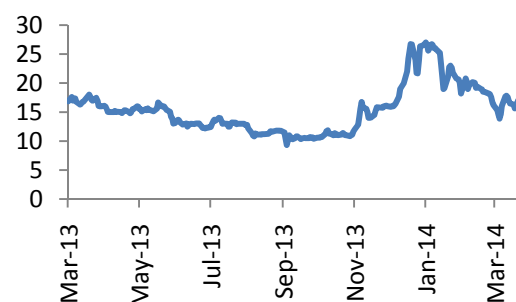
Balance Sheet Data

	2013-9M'm	FY 12 'm	%chg
Fixed Asset	149,290	130,324	15%
Stocks	30,077	18,110	66%
Trade Debtors	129,376	114,385	13%
Cash	12,778	13,408	5%
Trade Creditors	118,771	86,399	37%
Net Assets	157,791	105,354	49%

Stock Data

Price	₦16.80
52 week range	₦9.32 - ₦29.46
Market Cap. (N'm)	149,443
1-month Avg. Vol	4,617
Curr. PE	21x
Bloomberg Ticker	Oando NL
Reuters Ticker	Oando.LG

Oando Plc - Share Price Trend



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- The delays meant that whilst benefits from the COP deal could not yet accrue, charges already incurred by OER crystallised, with a sizeable chunk being recognised in the final quarter. Specifically, 65% of the \$27 million (~~₦~~4.3 billion) general and administrative expenses and 33% of the finance charges came in Q4 13, which amongst others, led OER to record steeper LBT and LAT of \$37.1 million (~~₦~~5.9 billion) and \$41 million (~~₦~~6.6 billion) in Q4 13, compared to LBT of \$5.6 million (~~₦~~896 million) and LAT of \$9.6 million (~~₦~~1.5 billion) in Q4 12. The fact that the twin drivers of Q4 loss (which underpinned FY weakness) were both related to COP deal underscores concerns we entertained about the detrimental impact the COP deal could have on other business divisions. Specifically, we believe this—in addition to subsidy issues—informed management’s decision to significantly scale down volumes at its downstream division, with impact on 9M 13 revenues (-21% YoY) and earnings (-48% YoY), even as the company surprisingly sold the East Horizon Gas Company—an asset which management had touted as key to its midstream business in the eastern region of Nigeria—to aid the funding of the COP deal.

OER loss portends significantly weaker Q4 13 for Oando

- Factoring OER’s Q4 13 numbers, we have revised our Q4 13 expectations for Oando by increasing our administrative and interest expenses 34% and 66% higher to ~~₦~~12.8 billion and ~~₦~~5.9 billion. This primarily drives LBT and LAT of ~~₦~~1.9 billion and ~~₦~~1.3 billion, respectively from our previous PBT (~~₦~~4.0 billion) and PAT (~~₦~~2 billion) and compares with respective LBT and LAT of ~~₦~~2.3 billion and ~~₦~~938 million in Q4 12. Accordingly, our FY 13 PBT and PAT nearly halves to ~~₦~~7.8 billion and ~~₦~~4.7 billion, implying 55.4% and 43.5% YoY declines.
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Resolving delays critical to harvesting value

- Despite significant near-term profit revisions, our FV estimate is only moderately changed—now ₦13.25 from ₦13.51—as forward estimates were largely unchanged, in line with our view that administrative expenses should normalise in 2014 and having already factored in relatively higher interest expense. Pertinently, however, it affirms our SELL rating given that Oando’ current price of ₦16.80 is at a 27% premium to our FVE. In addition, Oando trades at a current P/E of 21.1x and EV/EBITDA of 9.2x, a premium to peer averages of 14x and 6.5x. Current delays would appear to justify our decision to discount the impact of the COP deal from our valuation, which continues to be delayed by regulatory approval--a precondition to closure. Whilst we believe the deal holds ample value, ongoing approval delays could continue to erode shareholder value, as the company continues to incur elevated COP financing interest expenses. Further risk remains in the form of potential loss of deposit (now \$500 million-~~₦~~80 billion) if the deal is not approved. The deal is now scheduled to close end of April 2014, and we will continue to watch closely to see whether value addition from acquisition will be back on track.
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Summary of Results and Forecasts

QUARTERLY					
	Q2 2013A	Q3 2013A	Q4 2013F	Q1 2014F	
Income Statement ('mln)					
Turnover	159,266	105,924	133,015	141,024	
COGS	(142,081)	(89,435)	(115,483)	(123,232)	
Gross Profit	17,186	16,489	17,532	17,792	
Operating Costs	(13,613)	(9,853)	(13,830)	(11,141)	
Operating Profit	3,847	8,685	4,080	7,215	
Profit Before Taxation	1,866	3,606	(1,934)	3,201	
Taxation	(43)	(1,785)	590	(1,376)	
Profit After Taxation	1,823	1,820	(1,344)	1,824	
ANNUAL					
	2012A	2013F	2014F	2015F	2016F
Income Statement (mln)					
Turnover	673,182	519,267	587,601	611,364	628,031
COGS	(591,560)	(446,134)	(503,766)	(519,624)	(531,804)
Gross Profit	81,622	73,132	83,834	91,740	96,227
Operating Costs	(49,594)	(45,695)	(43,482)	(45,241)	(46,474)
Operating Profit	35,619	22,454	33,002	38,388	40,830
Profit Before Taxation	17,554	7,895	20,329	25,094	27,463
Taxation	(6,768)	(3,079)	(8,742)	(10,790)	(11,809)
Profit After Taxation	10,786	4,816	11,588	14,303	15,654
Balance Sheet ('mln)					
Fixed Assets	130,325	134,429	139,419	144,147	148,413
Stocks	18,110	21,498	24,275	25,039	25,626
Trade Debtors	115,755	87,885	109,881	120,439	130,002
Creditors	87,886	65,851	74,358	76,699	78,496
Net Assets	105,354	153,656	163,195	172,864	182,796
Key Ratios					
Operating Margin	5%	4%	6%	6%	7%
Net Margin	2%	1%	2%	2%	2%
P/E	3.5	17.0	15.5	7.4	6.8
P/BV	0.3	0.5	0.6	0.6	0.6
P/Sales	0.0	0.1	0.2	0.2	0.2

Source: Company financials, ARM Estimates

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
STRONG 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	Minimise exposure to security taking cognizance of its index weighting
SELL	Sell-off security completely from portfolio

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