

Rating	BUY
Price	₦85.00
FVE	₦102.33
52-week range	₦50.9 – ₦90.0
Market Cap. (N'bn)	81.08
1-month Avg. Vol	378,845
Current PE	8.5x

OKOMUOIL.NL - Share Price Trend



Analyst(s)

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Okomu Oil Palm Plc. (Okomuoil.NL)

Stock Report

Green Shoots or a False Spring?

- In this report, we transfer coverage of Okomu Oil Palm Plc. (Okomu) to Damilola Olupona.*
- Upside Abounds.** Shares of Okomu has returned +26% YTD, reflecting a remarkable 1st quarter 2018 performance wherein the company reported EPS of ₦3.64 (+13% YoY) on the back of margin expansion and lower debt profile. Going forward, the repeated concern in the mind of investors is if there is still room for upside on the stock. Following revision to our estimates, we arrive at a FVE of ₦102.33 which implies a 20.4% upside from current pricing. Our optimism is hinged on expectation of strong volumes growth, better operating efficiency, and lower finance cost over FY 18. Hence, we reiterate our **BUY** rating on the stock. Okomu trades at a forward P/E of 8.0x relative to 13.72x for Bloomberg MENA peers.
- Strong volumes growth to mask lower CPO prices.** Domestic CPO prices have faced a downtrend in line with global CPO prices, with prospect of widening CPO surplus (USDA forecasting a +51% jump in global surplus to 4.9 million MT) dragging global CPO prices with pass through effect on domestic CPO prices (-27% YoY to ₦391,969.44/MT). However, having recorded strong volumes growth in Q1 18 (+73% YoY to 16,091MT)—owing to better than expected harvest, we see scope for higher volumes over 2018 which would provide succor to FY 18 revenue. The current market dynamics where local demand for CPO currently outweighs supply further buttresses our outlook

for volume growth in 2018 as such, we model a +16% growth in volumes over FY 18. Net impact of the decline in domestic CPO price and increase in volumes translate to FY 18 revenues of ₦21 billion (+3% YoY).

- **Improved energy mix will support margin expansion.** In a bid to preserve margins, management guided to measures to keep costs lower over 2018. Specifically, the company mentioned that its plant is now connected to the national grid with Benin Electricity Disco Company (BEDC) accounting for 60% of its total power usage (previously 40%) while also guiding to plans to increase the usage to 70% over 2018 to keep energy costs lower. We believe the company's improved energy efficiency reflected in Q1 18 as Cost of Goods Sold (COGS) dipped 48.2% YoY to ₦655 million. However, in line with past trends where the company records higher COGS at the tail end of the year due to the outset of the planting season, we see scope for cost pressures at subsequent quarters. Irrespective, due to the high base of the prior year, we forecast a 11% YoY decline in COGS to ₦3.8 billion over FY 18 which translates to a 340bps YoY expansion in gross margin to 82.5%.
- **Lower operating cost on the cards:** In the first quarter of 2018, operating expenses increased by a whopping +116.1% YoY to ₦2.7 billion (Q1 18: OPEX to sales ratio: +15.49ppts YoY to 36.4%) which management linked to carryover expenses from prior quarter. In subsequent quarters, we expect a normalization in OPEX hence, we model an 11% YoY expansion in FY 18 OPEX which translates to a flat growth in OPEX to sales ratio of 25%. Thus, we forecast a 12% YoY jump in operating profits to ₦12.5 billion, which translates a 30bps jump in EBIT margin to 58%.
- **Lower finance costs bolster earnings:** In Q1 18, Okomu scaled down its borrowing (Q1 18: ₦1.1 billion vs ₦1.3 billion in FY 17) following payment of its FCY loan (€10 million) owed to its parent company—*SOCFINAF S.A.* As a result, net finance charges dipped to ₦36.7 million vs ₦105.9 million in Q1 18. In our view, this provides leeway for lower finance expense over FY 18. Irrespective, given ongoing expansion plans, we expect a slight increase in gross debt to N1.5 billion (+20% YoY). However, management noted its preference for local borrowings, largely from the FG/CBN intervention. Thus, reflecting the paydown of foreign borrowings, finance cost is expected to print at N275 million (2017: N484 million).
- On balance, we now look for FY 18E PAT of ₦10.1 billion (+11% YoY) with most of the gains expected to come from stronger volumes, greater cost efficiency and lower finance expense as opposed to the price-led gains of 2017. We have a FVE of ₦102.33 (Previous:

₦67.3) which implies a 20.4% upside from current pricing. Hence, we reiterate our **BUY** rating on the stock. Okomu trades at a forward P/E of 8.0x relative to 13.7x for Bloomberg MENA peers.

Summary of Results and Forecast

ANNUAL					
Income Statement (₦' m) *	2016A	2017A	2018F	2019F	2020F
Revenue	14,365	20,262	21,502	22,178	23,964
COGS	3,589	4,226	3,763	3,881	4,313
Gross Profit	10,775	16,035	17,740	18,297	19,650
Operating Cost	3,938	5,061	5,376	5,544	5,991
Operating Profit	6,952	11,128	12,493	12,885	13,803
Finance Income	1,341	484	275	194	196
Finance expense	291	491	315	109	163
PBT	5,906	11,140	12,661	12,933	13,914
Tax	996	1,992	2,532	2,587	2,783
PAT	4,910	9,148	10,129	10,346	11,131
Balance Sheet (₦ 'm) *					
Fixed Assets	9,217	11,217	15,337	19,249	22,022
Biological Assets	9,400	12,899	15,308	17,292	19,365
Stocks	1,719	2,687	1,731	1,785	1,984
Trade debtors	506	978	860	887	959
Cash and other bank balances	3,198	3,094	5,270	7,303	10,719
Total Asset	24,508	31,372	39,004	47,015	55,547
Liabilities					
Trade Creditors	641	488	677	699	776
Long Term Liabilities	4,488	3,097	3,250	3,434	3,489
Total liabilities	7,496	6,865	7,305	7,557	7,740
Shareholders' fund	17,012	24,507	31,698	39,458	47,807
Key Ratios					
P/E	16.51	8.86	8.00	7.84	7.28
ROA	20.0%	29.2%	26.0%	22.0%	20.0%
ROE	28.9%	37.3%	32.0%	26.2%	23.3%
Gross Margins	75.0%	79.1%	82.5%	82.5%	82.0%
EBIT Margins	48.4%	54.9%	58.1%	58.1%	57.6%
PBT Margins	41.1%	55.0%	58.9%	58.3%	58.1%
Net Margins	34.2%	45.1%	47.1%	46.7%	46.5%
EPS	5.15	9.59	10.62	10.85	11.67
P/B	2.94	2.04	1.58	1.27	1.05

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

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