

Presco Plc. | Earnings Report

12 months ended 31st December, 2015

Lower biological asset gains weigh on earnings
(NEUTRAL: ₦38.49)

- Presco Plc. (**Presco**) released FY 2015 audited results wherein revenue rose 14.3% YoY to ₦10.4 billion while PBT and PAT declined 46.7% and 55.3% YoY to ₦4.2 billion and ₦2.3 billion respectively.
- In addition, Presco proposed a FY 15 **dividend per share of ₦1.00** (FY 14: ₦1.00) **which translates to a dividend yield of 2.9%** using last trading price.

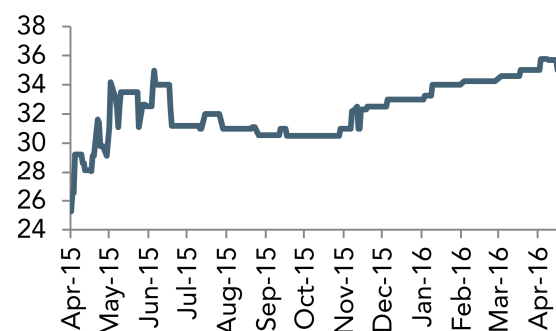
Volatile biological asset revaluation undermines earnings...

- Earnings were largely undermined by a ₦1.1 billion loss on biological assets in Q4 15 (Q4 14: ₦4.1 billion gain) which dragged FY 15 biological asset lower (-81.6% YoY to ₦1.1 billion). It is noteworthy that the plunge in biological asset gains largely stemmed from restatement of 2014 figures (four-fold higher from prior reading). Had 2014 biological asset gains not been restated, Presco would have reported improved earnings. Specifically, Q4 15 post-tax loss would have declined 17.1% YoY to ₦1.2 billion while FY 15 PAT would have tripled YoY to ₦2.3 billion).

Income Statement Data (₦'million)			
	2015 – 12M	2014 – 12M	%chg
Revenue	10,448	9,138	14.3%
PBT	4,215	7,901	-46.7%
Tax	1,894	2,707	-30.0%
PAT	2,321	5,194	-55.3%

Balance Sheet Data ₦'million)			
	2015-Dec	2014-Dec	%chg
Fixed Assets	12,962	10,946	18.4%
Receivables	2,986	1,769	68.8%
Cash	669	63	961.9%
Payables	3,357	3,397	-1.2%
Net Assets	30,395	29,060	4.6%

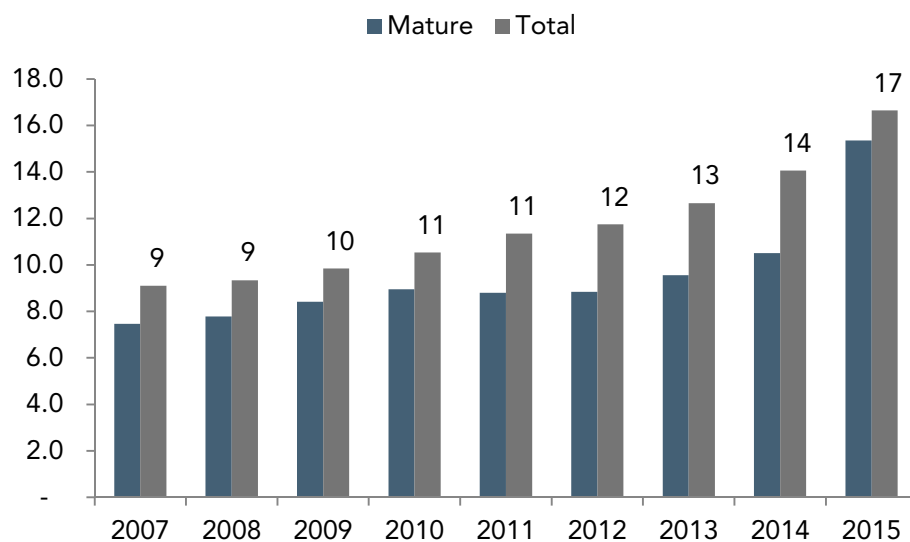
Stock Data	
Price	₦35.02
52 week range	₦25.26 – ₦35.76
Market Cap. (₦'m)	28,478.21
1-month Avg. Vol	1,213,518
Curr. PE	15.1x
Bloomberg Ticker	PRESCO:NL
Reuters Ticker	PRESCO:LG

Presco Oil Palm Plc- Share Price Trend

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...even as costs of higher cultivation weigh on gross margin

Largely reflecting increased cultivation activities, FY 15 COGS climbed 19.2% higher YoY to ₦3.8 billion. Particularly, upkeep costs of mature plantings, harvesting & laboratory surged (+29.4% YoY to ₦1.2 billion) in tandem with a 46.2% YoY expansion in Presco's mature plantation to 15.4 kilo hectares. Thus, while the higher plantation acreage was positive for volume, as Presco's FY 15 revenue (+14.3 % YoY) rose faster than domestic CPO prices (+9.9% YoY), gross margin contracted 148bps YoY to 63.5%. (Gross profit: +11.7% YoY). Focusing on Q4 15, revenue climbed for the eight consecutive quarter at 8.5% YoY to ₦2.4 billion. Nonetheless, gross profit declined 36.1% YoY to ₦1.9 billion, reflecting higher COGS of ₦478 million over the period (Q4 14 COGS was negative on account of over accruals in prior quarter).

Figure 1: Trend in Presco's cultivated plantation (Kilo hectares)

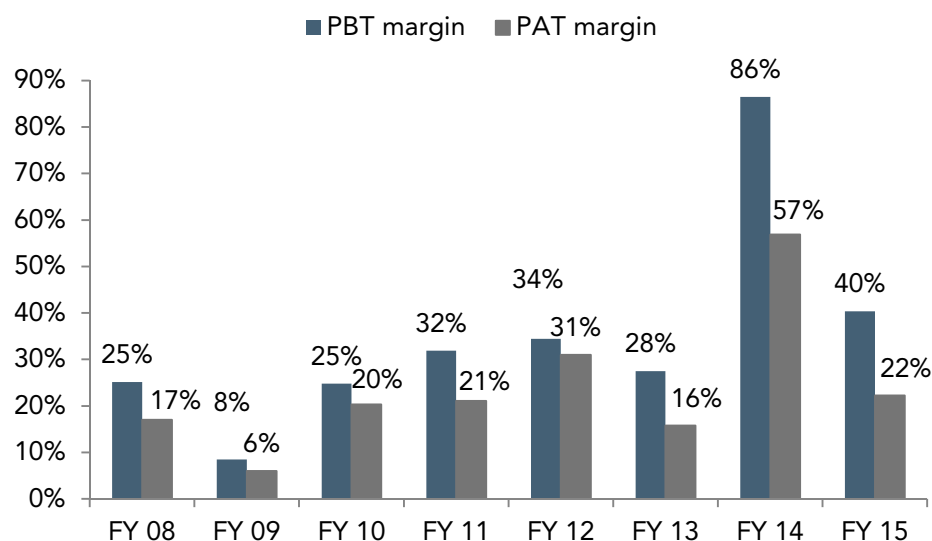


Source: Company's presentations, ARM Research

- The contraction in gross margin was exacerbated by surging finance costs (Q4 15: five-fold YoY to ₦126 million, FY 15: +95.2% YoY to ₦708 million) which tracked similar movement in borrowings (doubled YoY to ₦6.1 billion). Importantly, amid concerns over the naira outlook, Presco (similar to Okomu) refinanced all of its foreign borrowings (58% of 2014 total debt) with domestic

borrowings. Consequently, Presco reported a 46.7% and 55.3% YoY contraction in PBT and PAT to ₦4.2 billion and ₦2.3 billion respectively, while earnings over Q4 15 were negative (pre-tax loss: ₦609 million, post-tax loss: ₦1.2 billion).

Figure 2: Trend in earnings margin



Source: Company's financials, ARM Research

Higher prices and increased production to sustain top-line growth

- Going forward, we expect Presco's expanded mature plantation to support volume growth. Furthermore, amidst higher domestic CPO prices (Q1 16: 34.4% YoY) which reflect recovery in global prices and fallout of CBN's FX proscription to CPO imports, **we forecast 40.8% YoY jump in Presco's top-line to ₦14.7 billion for FY 2016.** (Okomu's CPO sales surged 50.9% YoY in Q1 16). Over our forecast horizon, 2016-2020, whilst government policy remains inward looking to plug the domestic CPO supply shortfall, entrance of PZ-Wilmar into Nigeria with a plan to cultivate 50,000 hectares as back-end to their Lagos refinery poses competitive pressures to Presco. Consequently, **we now project revenue CAGR of 13.5% vs. 14.4% over the last five years.**
- The top-line gains should more than offset higher COGS (2016E: +38.9% YoY, 2016-2020 CAGR: +12.5%), as management guides to cultivating 1000-1500 hectares each year through to 2020, leaving gross profit over the forecast horizon higher (2016E: +41.9% YoY to ₦9.4 billion 2016-2020 CAGR: +14.0%).

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- Whilst operating costs (2016E: +27.8% YoY 2016-2020 CAGR: +9.4%) and finance expense (2016E: +6.3% YoY, 2016-2020 CAGR: +5.5%) should mirror increased production activities and borrowings, top-line gains should still filter through to earnings (PBT: 2016E: +37.2% YoY, 2016-2020 CAGR: +14.2%). Furthermore, amidst expectation of lower effective taxes (mean: 2016-2020: 37%, 2011-2015: 33%), we project PAT to grow an average 19.2% per annum over our forecast horizon (2016E: +49.5% YoY to ~~₦~~3.4 billion). Net effect of these assumptions resulted in blended FVE (weighted average of DCF and relative valuation) of ~~₦~~**38.17** (vs. ~~₦~~32.64 previously) for Presco.
 - Currently, Presco trades at a P/E of 15.1x (27.8x — if gains from biological assets are excluded) vs. 8.7x for domestic peer Okomu. On a forward basis, Presco's P/E of 10.1x is similarly at a premium to Okomu's 9.1x. The stock has climbed 6.1% YTD, with last trading price at a 10% discount to our FVE (~~₦~~**38.49**) which translates to a **NEUTRAL** rating.
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Presco Plc - Summary of Results and Forecasts - Naira (N=million)*

QUARTERLY					
Income Statement (N=mln)*	Q1 2016F	Q2 2016F	Q3 2016F	Q4 2016F	
Sales	3,078	3,418	4,018	4,200	
Cogs	1,108	1,230	1,446	1,512	
Gross profit	1,970	2,187	2,571	2,688	
Operating cost	856	950	1,117	1,168	
Operating profit	1,145	1,271	1,495	1,562	
Net finance costs	1,222	1,349	1,572	1,640	
Profit before taxation	489	540	629	656	
Tax	733	809	943	984	
Profit after taxation	3,078	3,418	4,018	4,200	
ANNUAL					
Income Statement (N=mln)	FY 2015A	FY 2016F	FY 2017F	FY 2018F	FY 2019F
Sales	10,448	14,713	15,780	17,295	18,463
COGS	3,813	5,297	5,681	6,226	6,462
Gross profit	6,635	9,417	10,099	11,069	12,001
Operating cost	3,140	4,090	4,703	5,154	5,133
Operating profit	3,860	5,473	5,555	6,088	7,053
Interest expense	708	752	839	846	883
PBT	4,215	5,783	5,777	6,304	7,232
Tax	1,894	2,313	2,253	2,459	2,531
PAT	2,321	3,470	3,524	3,846	4,701
Balance Sheet (N=mln)					
	FY 2015A	FY 2016F	FY 2017F	FY 2018F	FY 2019F
Assets					
Fixed Assets	12,962	15,042	17,245	19,679	21,952
Biological Assets	36,319	40,138	42,814	45,651	48,608
Stocks	1,106	1,536	1,647	1,805	1,873
Trade debtors	2,986	4,205	4,509	4,942	5,276
Cash& Bank balance	669	1,066	1,305	1,192	2,257
Total Assets	55,478	63,422	68,957	74,705	81,404
Liabilities					
Trade Creditors	3,357	4,662	5,000	5,480	5,688
Long term liabilities	18,656	19,337	19,872	20,198	20,932
Total liabilities	25,083	27,349	28,360	29,262	30,260
Shareholders' fund	30,395	36,073	40,597	45,443	51,144
Key Ratios					
	FY 2015A	FY 2016F	FY 2017F	FY 2018F	FY 2019F
Valuation multiples					
EPS	2.32	3.47	3.52	3.85	4.70
P/E	15.09	10.09	9.94	9.11	7.45
EV/EBITDA	8.17	5.63	5.38	4.88	4.17
ROA	8%	10%	9%	8%	9%
ROE	4%	6%	5%	5%	6%

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 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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