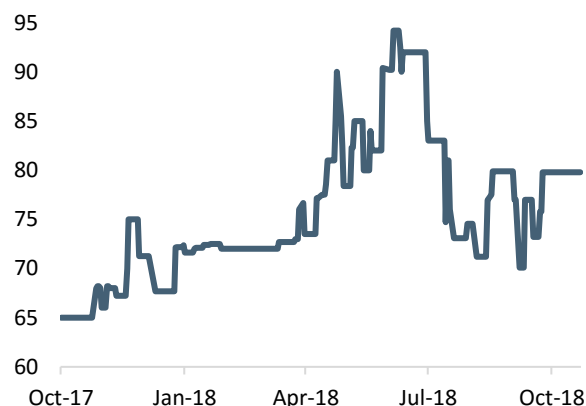


Rating	<b>STRONG BUY</b>
Price	₦75.75
FVE	<b>₦97.75</b>
52-week range	₦65- <del>₦94.7</del>
Market Cap. (₦'bn)	76.12
1-month Avg. Vol	275,063
Curr. PE	8.51x

Quarterly EPS	Q1	Q2	Q3	Q4
<b>2016 A</b>	1.67	2.11	0.61	0.77
<b>2017 A</b>	3.22	2.72	0.17	2.89
<b>2018 A(E*)</b>	3.64	2.59	1.36	1.18*

#### OKOMU:NL - Share Price Trend



#### Analyst(s)

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**Click link below for recent report on Okomu**

**9M 2018 Initial View: Lower cost of sales propels earnings**

## The Okomu Oil Palm Plc. (OKOMU.NL)

### Stock report

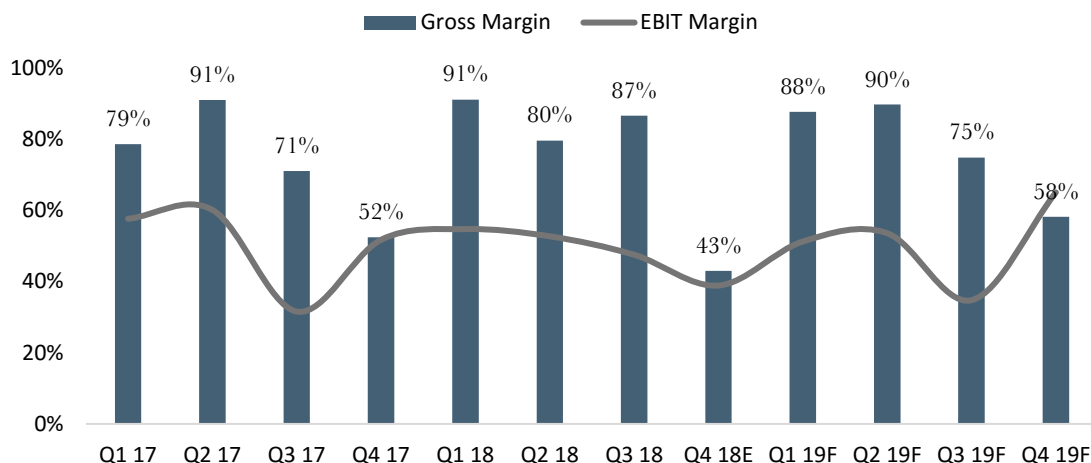
#### A Rejuvenating prospect

- We have engaged with management of Okomu following the release of its nine-months 2018 result and thus revise our estimate for FY 18E and FY 19F.
- While we hold our views on Q4 volumes and input cost, nine-months run-rate informs some adjustment to estimate. On volumes, the impressive run in volumes over 9M 2018 (+10.5% YoY to 32,032 MT) informs a revision to FY 18 revenue of ~~₦20.3~~ billion (+7% YoY). Furthermore, given the abysmally low input cost in Q3 18 relative to trend levels<sup>1</sup>, we have revised our FY 18 cost of sales estimates lower by 15.7% to ~~₦4.1~~ billion (previous: ~~₦4.9~~ billion) and made slight adjustment to FY 18E our interest expense estimate (+38% YoY to ~~₦380~~ million) in line with 9M 18 run rate of ~~₦332~~ million.
- Over in 2019, we anticipate a modest growth in CPO volumes which brings our CPO sales expectation for 2019 to ~~₦16.3~~ billion. Father out, from 2020 we anticipate boost to Okomu's production emanating from the harvest of fresh fruit bunches from its extension 2 plantation. As a result, we have increased our FY 20-22F sales forecast by 12% on average. Overall, the upward revision to our sales forecast over the medium term informs our decision to raise FVE by 6% to **₦97.75** (previous: ~~₦92.45~~) thus, we maintain our **STRONG BUY** rating on the stock. On our 2019 numbers, Okomu trades at a forward P/E of 8.55x relative to 9.2x for Presco and Bloomberg Middle-East and Africa (MENA) peers of 13.5x.

<sup>1</sup> 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.

**Cost pressures to drag Q4 18 to the mud.** Following the impressive run in volumes over 9M 2018 (+10.5% YoY to 32,032 MT) we made upward revision to our volumes estimate (+8%) and revise our FY 18E revenue higher by 7% YoY to ₦20.3 billion. Furthermore, incorporating Q3 18 results, we have revised our FY 18 cost of sales estimates lower by 15.7% to ₦4.1 billion (previous: ₦4.9 billion). Based on the new adjustment, we now expect cost of sales of ₦2.1 billion over Q4 18 which would translate to a 3% YoY growth cost of sales over Q4 18. Our expectation for input cost pressure over the last quarter is hinged on the pass through of seasonal related cost emanating from higher wage cost linked to the planting season and repair and maintenance cost incurred usually in the last quarter of the year. Against this backdrop, we estimate FY 18E gross margin to contract 60bps YoY to 78.5%. Furthermore, we raise our interest expense estimate by 38% YoY to ₦380 million in line with 9M 18 run rate of ₦332 million. Net impact of this including higher operating expenses (+5% YoY to ₦5.3 billion) translates to a 13.3% YoY expansion in earnings to ₦7.2 billion in FY 18E.

**Figure 1: Gross and EBIT margin (Historical and Forecast)**

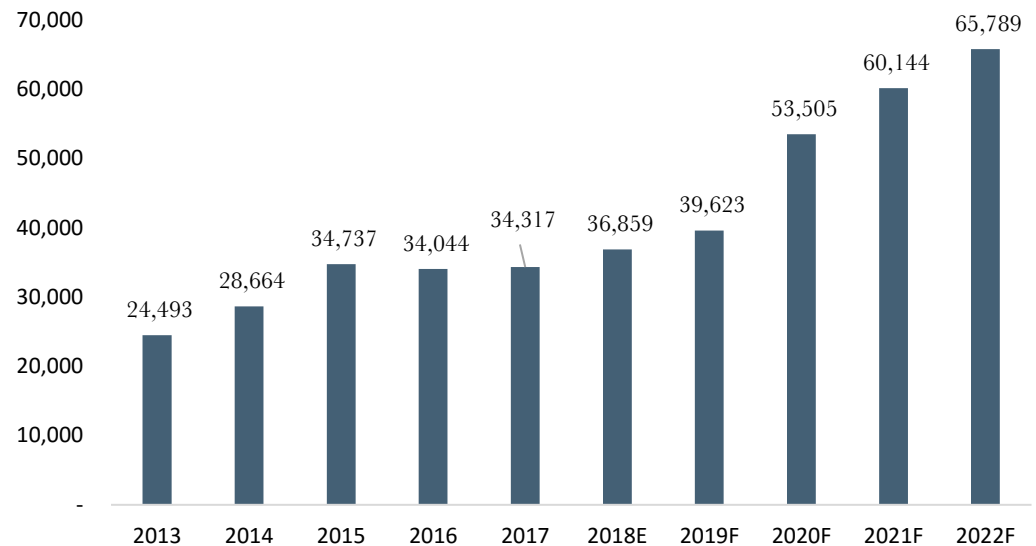


Source: Company financials, ARM Research

- Volumes growth buoy earnings outlook beyond 2018.** Farther out into 2019, while the widening global CPO surplus (+28% YoY to 4.1 MMT in September 2018) provides scope for subsisting pressure on CPO prices, we see volumes supporting revenue in the period. We forecast modest CPO volume growth of 7% YoY which brings our CPO sales expectation for FY 19F to ₦17.4 billion. The first set of acreage area planted in extension 2 in 2016 is staged to mature in 2019, but management guided to nurturing the palm trees in anticipation of reaping better yields in 2020 rather than harvesting them which implies stronger sales in the medium term. Hence, we have raised our FY 20-22F sales forecast by 12% on average.

Notably, the inherent demand-supply gap in the market which currently stands at ~430,000 MT indicates that a ready market exists to cater for the higher volumes over the medium term.

**Figure 2: Volumes trend (tons)**



Source: Company sources, ARM Research

- In addition, given that Okomu exports all its rubber and enters into a forward contract with off-takers of its rubber, we hold the view that Okomu's rubber sales over 2019 will be vulnerable to the persisting glut in the global rubber market which has depressed prices (-34% YTD). Thus, we model rubber sales of ₦3.8 billion over 2019 (FY 18E: ₦3.9 billion). Against this backdrop, we forecast a 5% YoY growth in combined FY 19E revenue to ₦21 billion.
- **Strong topline to support margins expansion.** We have revised our FY 19E input cost higher (+2% YoY to ₦4.4 billion) to capture modestly higher volumes over the period. However, with sales growth rising faster than input cost, gross margin is estimated at 79% (+50bps YoY), relative to 78.5% in FY 18E with related profit at ₦16.7 billion (+6% YoY). Also, with our FY 19E operating costs expectation of ₦5 billion (-6% YoY), we expect EBIT to print higher at ₦10.95 billion (+13% YoY).
- In a recent discussion, management ruled out further expansion plan and hinted at little or no borrowings over 2019. Thus, our model only takes into cognizance the new loan (₦1.95 billion) obtained from the Bank of Industry under the Agriculture credit loan scheme of the Federal Government in April 2018 at a 10% interest rate with interest payment expected to commence in 2019. Furthermore, with the recent stability in the Naira, we do not envisage

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material foreign exchange losses in FY 19. Thus, we project interest expense at ~~₦~~422 million (vs ~~₦~~332 million reported as at 9M 18). Net impact of our revisions translates to PBT and PAT of ~~₦~~10.8 billion (+12% YoY) and ~~₦~~8.8 billion (+12% YoY) respectively.

- On our 2019 numbers, Okomu trades at a forward P/E of 8.08x relative to 9.2x for Presco and Bloomberg Middle-East and Africa (MENA) peers of 13.5x. We retain our **STRONG BUY** rating on the stock with our revised FVE estimate of **₦97.75** (previous: ~~₦~~92.45).

## Summary of Results and Forecasts - Naira (₦)

ANNUAL					
Income Statement (N'm) *	2016A	2017A	2018E	2019F	2020F
Revenue	14,365	20,262	20,307	21,165	27,303
COGS	3,589	4,226	4,366	4,445	6,007
Gross Profit	10,775	16,035	15,941	16,720	21,296
Operating Cost	3,938	5,061	5,788	5,926	7,645
Operating Profit	6,952	11,128	10,275	10,921	13,815
Interest expense	1,341	484	380	422	364
Interest income	291	491	456	412	570
PBT	5,906	11,140	10,352	10,911	14,021
Tax	996	1,992	1,863	1,964	2,804
PAT	4,910	9,148	8,488	8,947	11,217
Balance Sheet (N '000) *					
Fixed Assets	9,400	12,899	15,153	17,013	19,534
Stocks	1,719	2,687	2,008	2,044	2,763
Trade debtors	506	978	812	847	1,092
Cash & other bank balances	3,198	3,094	4,400	7,007	8,910
Total Assets	24,508	31,372	37,909	46,127	54,994
Liabilities					
Trade Creditors	641	488	786	800	1,081
Non-current Liabilities	4,488	3,097	3,212	5,148	5,289
Total liabilities	7,496	6,865	7,375	9,151	9,606
Shareholders' fund	24,508	31,372	37,909	46,127	54,994
Key Ratios	2016A	2017A	2018E	2019E	2020E
Gross Margin	75.01%	79.14%	78.50%	79.00%	78.00%
EBIT Margin	48.39%	54.92%	50.60%	51.60%	50.60%
PBT Margin	41.12%	54.98%	50.97%	51.55%	51.35%
Net Margin	34.18%	45.15%	41.80%	42.27%	41.08%
EPS	5.15	9.59	8.90	9.38	11.76
P/E	10.20	5.48	8.97	8.51	6.79
EV/EBITDA	6.10	3.89	6.14	5.39	4.20
ROA	20.04%	29.16%	22.39%	19.40%	20.40%
ROE	28.86%	37.33%	27.80%	24.20%	24.71%

Source: ARM Research \*unless otherwise stated

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