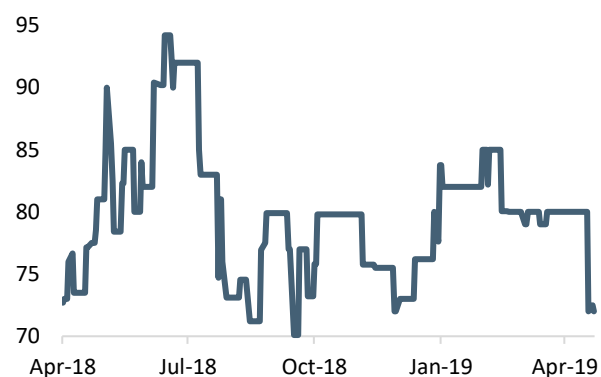




Rating	NEUTRAL
Price	₦72.00
FVE	₦75.6
52-week range	₦70.1--₦94.7
Market Cap. (₦'bn)	68.682
1-month Avg. Vol	2,570,015
Curr. PE	10.6x

Quarterly EPS	Q1	Q2	Q3	Q4
2017 A	3.22	2.72	0.17	2.89
2018 A	3.64	2.59	1.36	1.32
2019 E	1.06	2.76	1.86	1.21

OKOMU:NL - Share Price Trend



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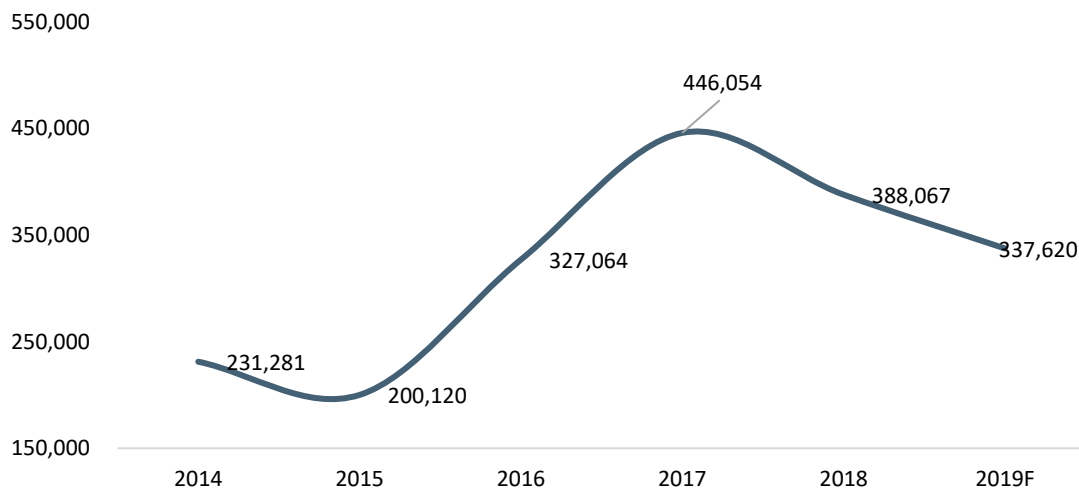
The Okomu Oil Palm Plc. (OKOMU.NL)

Stock report

Bumpy year ahead

- The Okomu Oil Palm Plc Q1 19 numbers released earlier this week, came with few surprises to us, with the major one being the more than expected decline in revenue over the period. Beyond doubt, the numbers can only be tagged a ***“Worrisome start to the year”*** as the company reported its weakest first quarter performance since 2014. Going by our communication with management, the poor performance stemmed largely from material erosion in global crude palm prices when compared to same period in the prior year and the increasing influx of lower priced CPO into the country. Beyond the obvious, we believe the high base in the prior year (due to bumper harvest and a much more favorable pricing) further magnified the material revenue crunch.
- With the Q1 numbers signaling a bumpy year ahead, we have updated our models accordingly. Particularly, with year to date appreciation in global CPO prices still far from the level in the prior year and growing intensity of smuggled CPO, we expect local CPO prices to remain depressed over 2019. Worthy of note, while large corporates typically have controlled quality on the use of CPO and palm olein products, our market check suggests that much smaller corporates and individual households (which in our view accounts for the largest share of consumption) are not as concerned about the quality of CPO and its end products. With this in mind and our understanding of the need of management to empty its excess tank over Q2, guides our expectation of 13% YoY decline in domestic CPO price to ₦337,620.

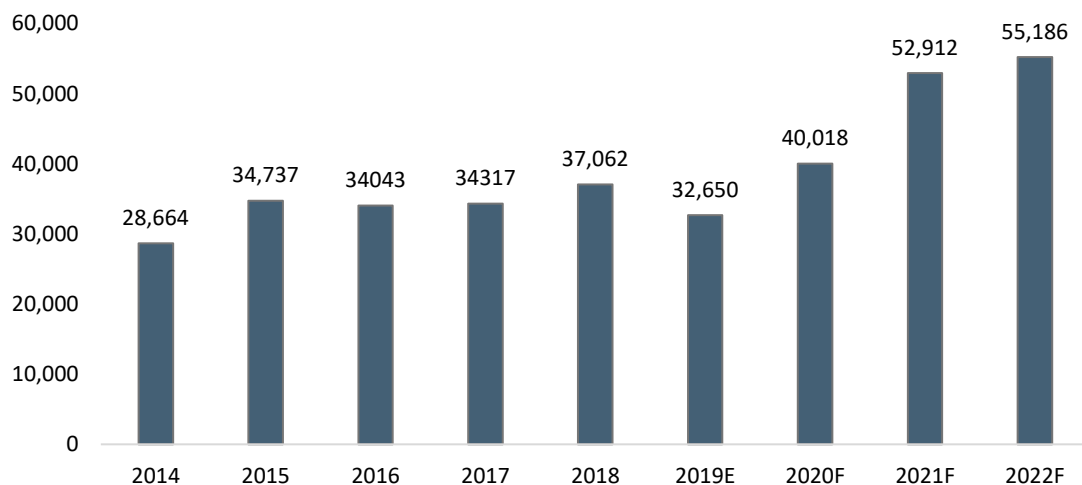
Figure 1: Trend in Local CPO prices (Naira)



Source: Company, ARM Research

- On volumes, with our discussion with management suggesting that only ~54% of volumes produced over Q1 19 were sold, we see further pressure on volumes over the rest of the year. Specifically, while we expect some pick up over Q2 19, we believe volume will remain depressed for most part of the year and thus estimate a 12% YoY decline. Beyond 2019, we believe better volumes and relatively flat price will be central to revenue growth. We remain broadly optimistic on volumes growth over the medium-term stemming from management's decision to nurture the first set of acreage area staged to mature in 2019 in anticipation of reaping better yields in 2020. This takes into cognizance commissioning of a new 30 ton/hour oil mill in extension 2 in 2021 and 2023 which should bring its total oil mill capacity to 135 ton/hour in 2023. Hence, we have raised our FY 20-23F sales forecast by 16% (Previous: 12%) on average.

Figure 2: Volumes trend (tons)



Source: Company, ARM Research

-
- ***Medium term gross margin expansion on the cards.*** In line with our expectation for lower CPO volumes over FY 19E, we forecast 2019 production cost to decline 19% YoY to ~~₦~~4.1 billion (Cost to sales ratio: 25%) which translates to a gross margin compression of 20bps YoY to 75%. However, given our expectation for cost savings from the acquisition of a 5MW turbine and room for a better economy of scale emanating from the production of higher volumes over our forecast horizon, we lower FY 20-23E Cost to sales forecast to 22% on average. Consequently, we model 400bps expansion in EBIT margin over our forecast horizon.
 - According to management, Okomu is averse to expensive credit facility and hinted at limiting its source of financing to CBN, BOI or other concessionary sources. This in addition to the lower interest rate environment informs our expectation of slower increase in interest expense by 5% YoY to ~~₦~~308 million in 2019. Cumulative impact of our adjustments translates to double-digit decline in EPS to ~~₦~~6.75 (-24% YoY) over FY 19E.
 - Factoring the gloomy expectation for 2019 into our model, we cut our FVE by 22% to ~~₦~~75.60 and downgrade to a **NEUTRAL** rating. Okomu trades at a forward P/E of 10.6x relative to 9.2x for Presco and Bloomberg Middle-East and Africa (MENA) peers of 12.94x.
-

Summary of Results and Forecasts - Naira (₦)

ANNUAL					
Income Statement (N'm) *	2017A	2018A	2019E	2020F	2021F
Revenue	20,262	20,258	16,168	19,776	25,970
COGS	4,226	5,019	4,042	4,548	5,843
Gross Profit	16,035	15,238	12,126	15,227	20,127
Operating Cost	5,061	5,162	4,042	4,746	6,233
Operating Profit	11,128	10,260	8,181	10,600	14,050
Interest expense	484	293	308	225	244
Interest income	491	354	144	526	588
PBT	11,140	10,337	7,853	11,201	14,738
Tax	1,992	1,835	1,414	1,568	1,474
PAT	9,148	8,502	6,440	9,633	13,264
Balance Sheet (N '000) *					
Fixed Assets	11,217	13,392	11,784	13,284	13,056
Stocks	2,687	3,149	1,859	2,092	2,688
Trade debtors	978	744	647	791	1,039
Cash & other bank balances	3,094	4,129	6,383	10,410	17,903
Total Assets	31,372	38,418	37,528	45,008	55,368
Liabilities					
Trade Creditors	488	1,548	728	819	1,052
Non-current Liabilities	3,097	4,981	4,146	4,279	4,424
Total liabilities	6,865	9,904	8,247	8,502	8,914
Shareholders' fund	31,372	38,418	43,185	50,665	61,025
Key Ratios					
Gross Margin	79.14%	75.22%	75.00%	77.00%	77.50%
EBIT Margin	54.92%	50.65%	50.60%	53.60%	54.10%
PBT Margin	54.98%	51.03%	48.57%	56.64%	56.75%
Net Margin	45.15%	41.97%	39.83%	48.71%	51.07%
EPS	9.59	8.91	6.75	10.10	13.91
P/E	5.48	8.95	11.82	7.90	5.74
EV/EBITDA	3.89	6.53	6.28	4.83	3.41
ROA	29.16%	22.13%	17.16%	21.40%	23.96%
ROE	37.33%	29.82%	18.43%	22.85%	25.45%

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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