Conoil Plc H1 2020

20 August 2020

MPR: 12.50%
July '20 Inflation Rate: 12.82%
Q1 '20 GDP: 1.87%

TICKER:	CONOIL	Upside Potential:	8.20%
Sector:	Oil & Gas; Downstream	Performance Rating:	A (Long-term Rating is BB)
Price as at 20 August 2020:	NGN15.25	Recommendation:	HOLD
Target Price:	NGN16.50	Suggested Entry Price:	NGN13.00

Financial Summary (N'Bn)	H1 2020	H1 2019	Y-o-Y%Δ
Turnover	57.46	72.22	-20.44%
Gross Profit	4.78	6.69	-28.63%
Operating Expense	3.81	4.06	-6.21%
EBIT (Operating Profit)	1.13	2.69	-57.85%
PAT	0.34	1.03	-67.20%
Total Assets	53.63	61.62	-12.96%
Total Liabilities	33.83	43.67	-22.55%
Shareholders' Funds	19.81	17.95	10.37%

Source: Company Financials, Cowry Research

Financial Ratios	H1 2020	H1 2019	Industry Average
Gross Profit Margin	8.31%	9.27%	7.69%
Operating Profit Margin	1.97%	3.72%	1.36%
Return on Equity	1.79%	5.68%	1.63%
Return on Total Assets	1.97%	4.47%	1.53%
Interest Coverage Ratio	1.78	2.30	5.61
CCC (in days)	117.25	32.61	111.36
Quick Ratio	1.26	1.10	1.01
Debt to Capital	13.79%	35.14%	29.69%
Equity Multiplier	2.71	3.43	2.85
Debt to Cash	1.86x	3.04x	3.00x
Debt to EBITDA	1.61x	0.61x	2.50x

Source: Company Financials, Cowry Research

Investment Ratios	FY 2019	Industry Average
EPS TTM	1.84	3.76
F' EPS	0.98	1.84
NAV	28.54	50.81
EV/EBITDA	7.59x	13.29x
PER TTM	9.17x	11.52x
Weighted PER	0.87x	8.93x
P/B	0.59x	0.75x
Dividend yield at suggested entry price	11.54%	

Source: NSE, Company Financials, Cowry Research

Conoil Plc Still Holds Value Despite Plunged Profit…

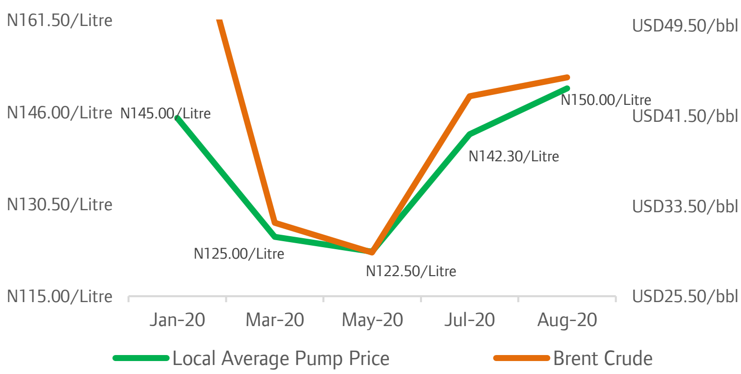
Conoil Plc churned out weaker operating performance in H1 2020 as its revenue was hard hit amid strict restrictions on movements, particularly at the inception of Q2 2020, due to COVID-19 pandemic fears. Hence, its profit after tax (PAT) plummeted year-on-year by 67.20% to N0.34 billion – as both white products and lubricants were impacted. We observed that performance across players in the sub-sector was also weak due to the pandemic. Meanwhile, activity in the industry was relatively volatile in H1 2020, as FG began partial implemention of market-based pricing regime amid declinig crude oil prices. Also, oil marketers are now allowed to import Premium Motor Spirit. Going forward, we expect revenue in H2 2020 to be better than that of H1 2020 given the two-time increase in pump price to around N148.70 in August, from N123.00 in April. Amid the challenges in the sector, Conoil's performance amongst other players was above industry average based on financial ratio anaysis, hence our 'A' rating.

… Liquidity Challenge, Weak Performance Should be Short-lived.

In addition to the weak profitability, Conoil Plc appeared to be grapling with liquidity issues given the dwindling cash & cash equivalent assets and the rapid rise in non-trade creditors. However, we observed that Conoil Plc is efficiently managing its liquidity challenge as it strategically exposed itself to non-interest bearing liabilities to reduce its relatively high interest-bearing borrowings (cost of debt stood at 15.75% in H1 2020). Borrowings and finance costs fell y-o-y by 65.36% and 62.80% to N3 billion and N0.25 billion respectively. Despite Conoil's liquidity issues, declining revenue and possible lower profit which may lead to a cut in dividend payout in FY 2020, we recommend a 'HOLD' position in expectation that the challenges should be short-lived.

Key: EPS – Earnings Per Share; NAV – Net Asset Value; PER – Price to Earnings; P/B – Price to Book; F' – Full Year Forecast; TTM – Trailing Twelve Months; CCC – Cash Conversion Cycle

Evolution of Nigeria's Pump Price vs Brent Crude Price



Source: BBC News, U.S. Energy Information Administration, Cowry Research

We expect Conoil's profit and liquidity to improve as the pump price rises in tandem with the rising crude oil prices and as fuel consumption grows.

Conoil Plc's Long-term Average Financial Ratios

	Nine-Year Averages	
Financial Ratios	Conoil Plc	Industry
CCC	5.90 days	14.74 days
Quick Ratio	1.18	0.92
Gross Profit Margin	11.5%	9.4%
Operating Profit Margin	4.5%	4.4%
Debt to Capital	40.4%	34.8%
Return on Equity	11.6%	18.7%

Source: Company Financial Reports, Cowry Research

Given the current partial deregulation of the Nigerian downstream sector and removal of subsidies, we note the possibility that significantly higher fuel prices could reduce the purchasing power/effective demand of the consumer. Hence, we expect competition among oil marketers for the consumer's wallet to also thin their profit margins in the medium to long run during which we expect players to increase their current capacity.

Our HOLD recommendation is hinged on two main factors – expected rise in pump price and sustained operating efficiency.

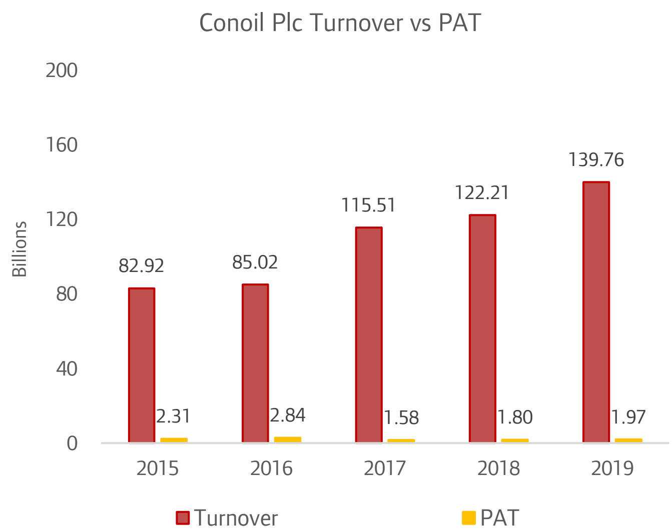
… As the Global Economy Continues to Improve.

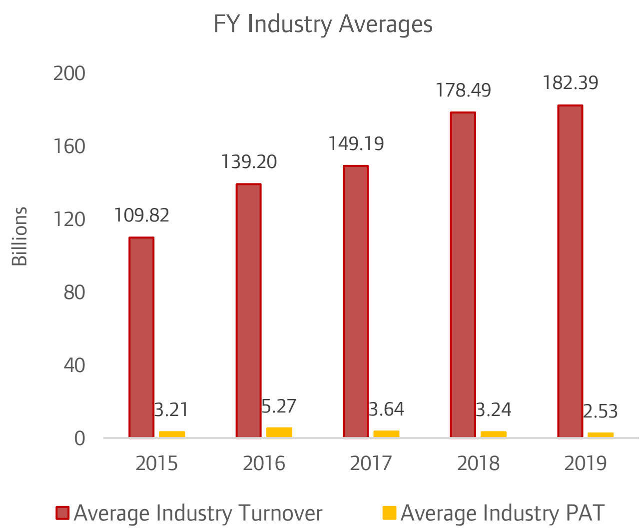
Against the backdrop of an improved global demand for oil amid the continued resumption of economic activities especially in China, the world's second largest consumer of crude oil (after the United States) which returned to growth in Q2 2020, brent crude spiked by 134.71% to USD45.37 a barrel as at August 19, 2020 from a year low of USD19.33 a barrel as at April 21, 2020 around when the pandemic triggered an oil demand shock. As countries continue to ease lockdown and as we expect demand for transportation fuels (for commuting, international flights and shipping) to rise. In the August edition of its Monthly Oil Market Report, Opec forecast OECD demand for crude at 45.77mbpd in Q4 2020, higher than 44.13mbpd forecast for Q3 2020.

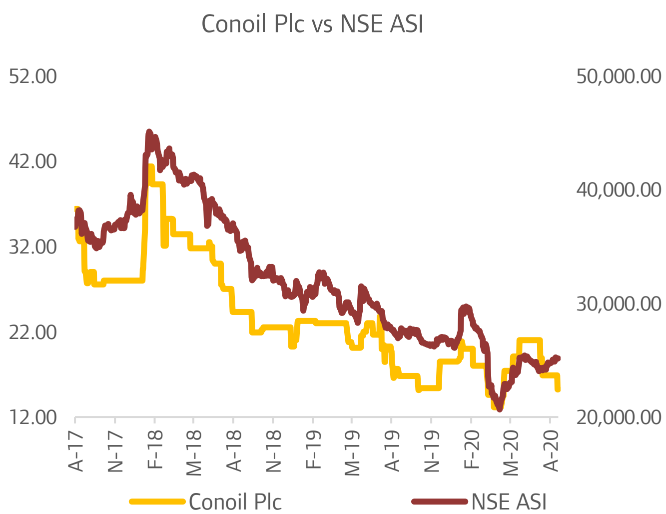
…And Operating Efficieny is Sustained

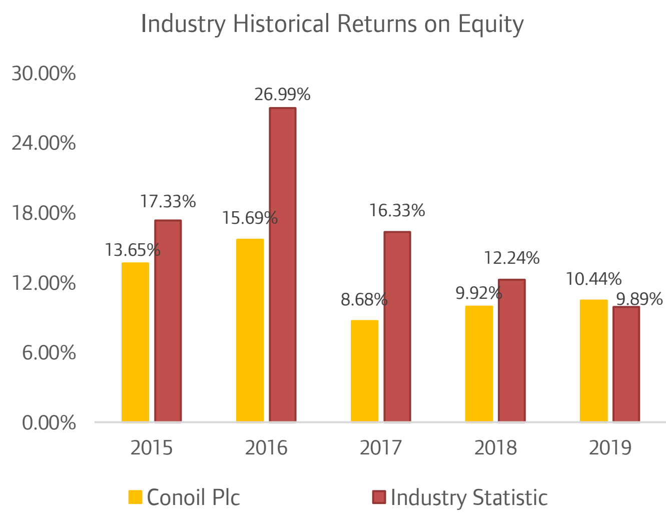
As already pointed out, Conoil has consistently been an efficient player in the rather low-margin Nigerian retail space and so naturally, we believe the company should record increased profitability with increase in pump price. Over the span of nine years (from 2011 - 2019), the downstream player, on average, outclassed its competitors (listed on the Nigerian Stock Exchange) in terms of gross profit margin (11.5% vs industry average of 9.4%) and operating profit margin (4.5% vs industry average of 4.4%). However, return on equity was lower at 11.6% compared to an industry average of 18.7%. This was essentially due to higher interest expenses as a significant borrower – its average debt to capital was 40.4%, higher than industry average of 34.8%. However, given recent efforts to lower its cost of debt (borrowings plunged year-on-year by 67% to N3.2 billion in H1 2020), and the opportunity to refinance its borrowings at lower interest rate, we expect ensuing savings to boost its bottom line.

Conoil Plc H1 2020 20 August 2020









Source: Company Financial Reports, Cowry Research

IMPORTANT DISCLOSURES:

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Performance Rating (PR)	Meaning
A	Security's Performance (Operating and Investment) rated '**Excellent**'; scores ≥ 75% in its industry
BB	Security's Performance rated '**Investment Grade**'; scores between 65% and 75% in its industry
Bb	Security's Performance rated '**Acceptable**'; scores between 50% and 65% in its industry
D-E	Security's Performance rated '**Not Acceptable**'; scores below industry average

Analyst Recommendation (AR)	Meaning
BUY	PR is a 'BB' or 'A' and/or Security's Upside Potential is X: X > 500bps above 364-day T-Bill rate
MODERATE BUY	PR is a 'Bb' or 'BB' and Security's Upside Potential is X: 364-day T-Bill Rate < X < 500bps above 364-day T-Bill Rate
HOLD	PR is a 'Bb' and Security's Upside Potential is X: X is positive and ≤ 364-day T-Bill Rate
MODERATE SELL/ REDUCE	PR is a 'Bb' and Security is Overvalued
SELL	PR is a 'D' or 'E' and Security is Overvalued