KenolKobil - FY16 Earnings Update
'Firing On All Cylinders'

KenolKobil posted a solid 19.8% y/y growth in net profit to KES 2.4B, driven by a 30% y/y growth in volume across the group's business segments. Total sales surged 19.6% y/y on the back of higher volume to KES 103.5B. The group increased dividend pay-out by KES 0.10 (+28.6% y/y) to KES 0.45.

Solid volume growth boosts top line: The group recorded growth in all product segments, leading to a 30% y/y increase in volume, which translated to a 19.6% y/y increase in net sales to KES 103.5B. The first half of 2016 was characterized by low crude prices, boosting the group's top line. The group added a total of 30 retail outlets to its network in FY16, bringing the number of retail outlets operated by KenolKobil across the region to 380.

Gross margin improves on lower costs of sales growth: Cost of sales grew 19.1% y/y to KES 96.1B; 50bps slower than the 19.6% y/y growth in revenue. Consequently, gross margin improved 40bps y/y to 7.1% in 2017. The growth in margins is attributable to increased focus on high margin products as well as the implementation of strategies to protect margins in an increasingly competitive environment.
Consequently, the group registered an impressive 26.5% y/y growth in gross profit to KES 7.4B.

Other income down on account of asset sale in FY15: Income generated from non-fuel revenue streams declined 44.1% y/y to KES 464.4M in FY16. The growth of non-fuel income has been a key tenet of the group's turnaround strategy and we expect non-fuel income to increase over the medium term on the back of retail outlet expansion and increased management focus on growth in the segment. Non-fuel income accounted for 5.9% of total income in FY16, down from 12.5% in FY15.

Finance costs decline as net borrowings reduce: Finance costs plunged 59.8% y/y to KES 354.7M, even as higher oil prices necessitated an increase in working capital. A larger cash position (+410.0% y/y), mitigated the effects of an increase in short-term borrowings (+57.2% y/y). As part of its turnaround strategy, the group aims to rationalize borrowing to boost the bottom line and protect margins.

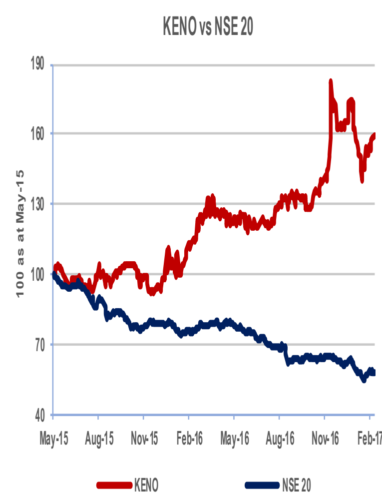
Exchange rate gains boost bottom line: The group realized a net forex gain of KES 2.5M, in FY16; a considerable improvement from the FX loss of KES 232.1M realized in FY15. The exchange rate gain was attributable to relative stability of the Kenyan Shilling throughout the year. Nonetheless, the group faced some currency headwinds due to a volatile Zambian Kwacha.

Cash generated from operations declines: Cash generated from the group's operations plunged 47.2% y/y to KES 3.1B.

Bloomberg Ticker:	**KNOC.KN**
Reuters Ticker:	**KENO.NR**

Share Statistics	
Current Price (KES)	14.05
P/E (x)	8.6
P/B (x)	2.1
Dividend Yield (%)	3.2%
Issued Shares (M)	1,471.8
Market Cap (USD M)	198.8
Year End	31-Dec

Price Trend



Source: Bloomberg, ApexAfrica Research

Research Analyst

Abizer Sharafali, ACCA

agulamabbass@apexafrica.com

+254 20 760 2534

www.apexafrica.com

While the group currently sits at a healthy cash position (KES 3.9B as at FY16), we note that a decline in cash generated from operations may necessitate the uptake of debt to fund the group's working capital requirements. This may be exacerbated by rising oil prices and increased currency volatility ahead of the 2017 General Elections in Kenya. Additionally, the group used KES 1.3B in investing activities for the year while generating KES 2.1B from financing activities. Total borrowings jumped 58.0% y/y to KES 7.4B, with the bulk of the increase coming from a jump in short-term borrowings to fund working capital requirements.

Bottom line jumps and pay-out ratio maintained: Strong volume growth allowed the group to shrug off the effects of rising oil prices in 2H16, to post a 13.2% y/y increase in EBITDA to KES 4.8B, translating to a 19.8% y/y increase in net profit to KES 2.4B. Shareholder funds climbed 15.3% y/y to KES 9.9B as the group brought a year of record performance to a close.

KenolKobil announced a final dividend of KES 0.30, translating to a total divided of KES 0.45 (+28.6% y/y). The dividend translates to a pay-out ratio of 27.4%, largely unchanged y/y. We expect the group to maintain a pay-out ratio of c.25% — 30%, over the medium term.

Key ratios pointing in the right direction: The group's gross margin rose 40bps y/y to 7.1% due to increased focus on higher margin business segments, while the current ratio increased marginally to 1.3 from 1.2 in FY15. The group's total borrowings as a percentage of shareholder equity rose to 74.7% in FY16, from 54.5% in FY15, largely as a result increased working capital requirements due to higher volume and crude prices.

Return on equity (ROE) rose 90bps y/y to 24.5% while the group's interest coverage ratio remained at a healthy 10.7 times FY16 finance cost; alluding towards a higher pay-out for shareholders in the medium term.

Looking ahead: The group's results marginally surpassed our expectations to the upside. Kenol's growth trajectory remains intact and we expect the group to grow significantly on the back of stable oil prices, increased margins due to operational efficiency and higher volumes across the region. The group's position as a premier oil marketer across the regions remains unchallenged even as competition from smaller players increases. A growing retail network across the region is expected to power volume growth over the medium term while also enhancing non-fuel income which is in turn expected to diversify Kenol's income streams and reduce reliance on fuel income. Additionally, growth in consumption in the group's core Kenyan market on the back of increased infrastructure development will boost the group's top-line and increase headroom for regional growth.

Furthermore, stable oil prices and prudent working capital management policies are expected to improve margins and reduce the need for short-term borrowing, ensuring investors a steadily growing dividend pay-out.

However, exchange rate volatility and the price of oil remain key risks. In our view, a pay-out ratio of c.25% - 30% will support the stock price as the group continues to expand its bottom line. KenolKobil currently trades at 8.6 times FY16 earnings and 2.1 times FY16 book value, with a trailing dividend yield of 3.2%.

Share Price Update: KenolKobil was the best performing counters on the NSE in 2016, closing trade up 55.2% in 2016, against a 21.1% decline in the blue-chip NSE 20. The stock is down 5.7% YTD but trades close to its 52-week high of KES 15.70. In our view, the market has priced in the group's FY16 numbers and consequently, we do not expect a significant surge in stock price in the wake of the results. Our estimates suggest that current valuation metrics are justified given the group's growth prospects over the medium term and we expect accumulation by growth investors around the current share price of KES 14.05.

Financials

	FY15 KES '000	1H16 KES '000	2H16 KES '000	FY16 KES '000	% chg y/y
Income Statement					
Net sales	86,557,936	36,937,907	66,556,018	103,493,925	19.6%
Cost of sales	(80,720,486)	(33,481,421)	(62,628,949)	(96,110,370)	19.1%
Gross profit	5,837,450	3,456,486	3,927,069	7,383,555	26.5%
Other income	830,391	216,493	247,860	464,353	-44.1%
Administrative and operating cost	(2,077,117)	(969,911)	(1,511,366)	(2,481,277)	19.5%
Impairment provision of KPRL Yield Shift Receivable	(146,694)	(400,000)	(200,000)	(600,000)	
Share of profit/ (loss) in associate	1,214	-	1,215	1,215	0.1%
Exchange gain/ (losses)	(232,064)	39,344	(36,819)	2,525	
EBITDA	4,213,180	2,342,412	2,427,959	4,770,371	13.2%
Finance cost	(651,344)	(97,997)	(256,693)	(354,690)	-45.5%
Finance income	83,909	-	92,461	92,461	10.2%
Depreciation and amortization	(863,324)	(518,941)	(450,945)	(969,886)	12.3%
Profit before income tax	2,782,421	1,725,474	1,812,782	3,538,256	27.2%
Income tax expense	(884,491)	(535,537)	(589,512)	(1,125,049)	27.2%
Profit for the year	1,897,930	1,189,937	1,223,270	2,413,207	27.1%
Loss from discont. Operations	117,044	-	-	-	
Profit for the year	2,014,974	1,189,937	1,223,270	2,413,207	19.8%
EPS (KES)	1.37	0.81	0.83	1.64	19.7%
DPS (KES)	0.35			0.45	28.6%
Balance Sheet					
Retained earnings	3,567,610	4,757,547	5,318,524	5,318,524	49.1%
Total shareholder funds	8,555,639	9,252,683	9,865,151	9,865,151	15.3%
Borrowings	-	109,245	36,325	36,325	
Total non-current liabilities	210,797	321,513	312,253	312,253	48.1%
Payables and accrued expenses	3,695,586	4,067,981	6,393,653	6,393,653	73.0%
Borrowings	4,662,431	4,616,391	7,330,234	7,330,234	57.2%
Total current liabilities	8,610,667	9,130,639	14,024,301	14,024,301	62.9%
Total equity and liabilities	17,377,103	18,704,835	24,201,705	24,201,705	39.3%
Property, plant and equipment	3,544,414	3,628,640	3,887,525	3,887,525	9.7%
Total non-current assets	6,722,294	6,599,187	6,564,485	6,564,485	-2.3%
Inventories	3,095,900	4,936,753	5,828,398	5,828,398	88.3%
Receivables and prepayments	6,524,544	5,904,725	7,773,875	7,773,875	19.1%
Total current assets	10,654,809	12,105,648	17,637,220	17,637,220	65.5%
Total assets	17,377,103	18,704,835	24,201,705	24,201,705	39.3%
Cash Flow					
Net cash generated from operating activities	5,224,416	1,223,581	1,288,560	2,512,141	-51.9%
Net cash (used in)/ generated from investing activities	668,962	(720,000)	(564,222)	(1,284,222)	
Net cash generated from/ (used in) financing activities	(6,313,815)	(110,086)	2,234,657	2,124,571	
Net increase/ (decrease) in cash and cash equivalents	(420,437)	393,495	2,958,995	3,352,490	
Ratios					
Gross margin	6.7%	9.4%	5.9%	7.1%	
Net margin	2.2%	3.2%	1.8%	2.3%	
EBITDA Margin	4.9%	6.3%	3.6%	4.6%	
Current ratio	1.2	1.3	1.3	1.3	
Acid test ratio	0.88	0.79	0.84	0.84	
Total borrowings/ shareholder equity	54.5%	51.1%	74.7%	74.7%	
Total borrowings/ total assets	26.8%	25.3%	30.4%	30.4%	
Interest coverage ratio	5.14	18.61	7.70	10.71	
Return on equity (ROE)	23.6%	25.7%	24.8%	24.5%	
Return on assets (ROA)	11.6%	12.7%	10.1%	10.0%	
Payout ratio	25.5%			27.4%	
Earnings yield				**11.7%**	
Dividend yield				**3.2%**	
P/E (x)				**8.6**	
P/B (x)				**2.1**	

Source: Company Filings, ApexAfrica Research

Appendix

Investment ratings

- **Buy:** A total return is anticipated in excess of the market's long-term historic annual rate (approximately 10%). Total return expectations should be higher for stocks that possess greater risk.

- **Hold:** Hold the shares with neither a materially positive total return nor a materially negative total return anticipated.

- **Sell:** Stock should be sold as materially negative total return is anticipated.

Disclaimer

ApexAfrica and its parent company Axys Group seek to do business with companies covered in their research reports. Consequently, a conflict of interest may arise that could affect the objectivity of this report. This document should only be considered a single factor used by investors in making their investment decisions. The reader should independently evaluate the investment risks and is solely responsible for their investment decisions. The opinions and information portrayed in this report may change without prior notice to investors.

This publication may not be distributed to the public media or quoted or used by the public media without prior and express written consent of ApexAfrica or Axys Group.

This document does not constitute an offer, or the solicitation of an offer, for the sale or purchase of any security. Whilst every care has been taken in preparing this document, no representation, warranty or undertaking (express or implied) is given and no responsibility or liability is accepted by Apex Africa or any of its employees as to the accuracy of the information contained and opinions expressed in this report.

ApexAfrica Capital Ltd
A The Riverfront, 1st Floor, Prof. David Wasawo Drive, Off Riverside Drive | P.O. Box 43676-00100 | Nairobi | Kenya |
T: +254-20-2226440 | Fax: +254-20-2319092 | Cell: +254-723-420204|
W : www.apexafrica.com
Part of Axys Group
W : www.axys-group.com