Ardova Petroleum Plc

Non-recurring income from prior year overwhelms bottomline…Adjusted EBIT up 46% y/y .

United Capital
The Intelligent Choice

Equity Research | Earnings Update

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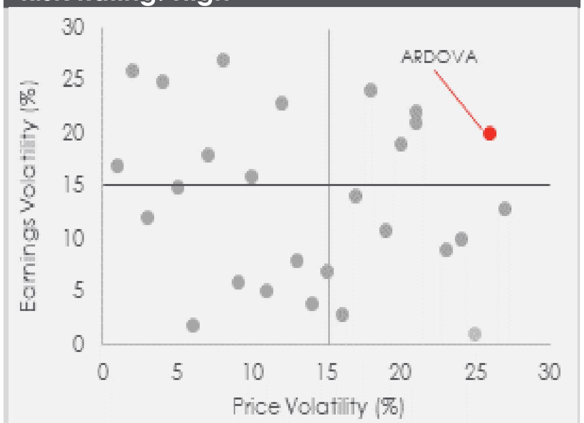
Stock Rating	Target Price	Expected Return*
BUY	**Old N18.9** **New N17.63**	**19.6%**

Note: Including dividend yield

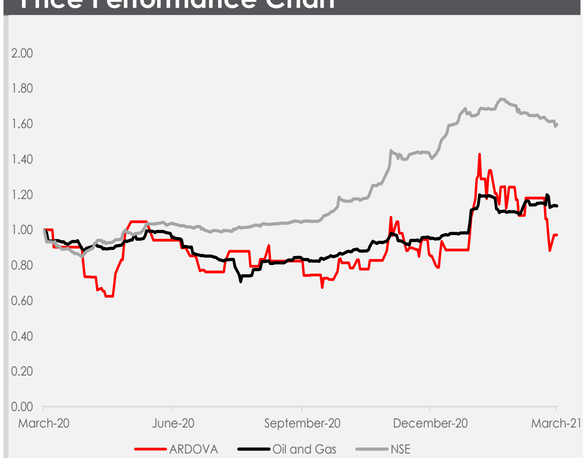
Risk Rating: High



Key Data

Last Price (₦)	14.85
52 week High/Low (₦)	22/ 9.84
1M Price Change (%)	-1.4
3M Price Change (%)	+10.3
6M Price Change (%)	+30.8
YTD Change (%)	9.6
Beta	0.7
Market Capitalization (₦'m)	19341,85
Market Capitalization ($'m)	47,08.
Shares Outstanding. (Units'm)	145.04
Float (%)	11.1
Dividend Yield (%)	1.3

Price Performance Chart



In its recently released FY-2020 audited financials, ARDOVA Plc ("ARDOVA" or "the Company") reported a 3.1% y/y growth in revenue, printing at N181.9bn, from N176.5bn in FY-2019. Revenue growth was driven by increased sales of petroleum products, which grew by 3.4% y/y in FY-2020. Cost of sales grew at a slower pace, up 2.6% y/y to N169.7bn in FY-2020. As a result, gross profit recorded a decent 12.1% y/y growth to print at N12.1bn in FY-2020. However, Operating income dropped by 16.0% y/y to N4.1bn, largely driven by the 2019 high base due to gain on disposed assets recorded. As such, Profit before tax and Profit after tax declined by 37.6% and 52.6%, to N2.9bn and N1.8bn, respectively, in the period under review. Earnings per Share (EPS) fell 52% to N1.4 per share in FY-2020. The firm proposed a dividend of N0.19 per share. We review our forecasts for the company and present our outlook below.

Reasonable growth despite tough operating environment

In 2020, the economic lockdown brought about by the Covid-19 pandemic hampered fuel demand in Nigeria. However, due to the price hikes and increased market share, Ardova Plc reported a relatively strong year. Total revenue grew by 3.1% in 2020, primarily driven by growth in sales of fuel products, which grew by 3.4% y/y to N164.4bn in FY-2020 from N159.2bn in FY-2019. Lubricant sales fell by 1.6% y/y from N17.2bn in FY-2020 to N16.9bn in FY-2019. Solar system business performed poorly as it recorded a 74.4% y/y decline in revenue to printed at N10.0m in FY-2020 from N39.0m in FY-2019. At the company's FY-2020 analyst presentation, it stated that its rising sales numbers were due to its increased market share to become the market leader , citing data from Nigeria's Major Oil marketing association (MOMAN).

Cost of sales printed higher at N169.7bn in FY-2020 from N165.2bn in FY -2019, representing a 2.6% y/y growth. The growth in cost of sales was mainly driven by an increase in petroleum product costs, which grew

Key Risks

3.0% y/y to N157.0bn in FY-2020 from N152.3bn in FY-2019. In addition, the company booked N25.0m in direct costs due to the unveiling of its haulage business as part of its efforts to bolster operating efficiency. Consequently, gross margins rose 3bps to 6.7% y/y. We note that the marginal improvement in gross margin was driven by the higher margins in its Lubricant (26.2%) segment compared to Petrol or PMS(4.2%). Profit margins in the PMS segment remained low, as the firm does not hold any wholesaler privileges, which would have allowed for improved margins. However, ARDOVA's drive to increase its market share in the lubricant market by signing an agreement with Shell lubricant is laudable as it looks to support its more profitable segment. Overall, operating expenses fell 11.7% y/y in FY-2020 due to a 16.6% y/y decline in administrative expenses to N7.3bn.

We note that the marginal improvement in gross margin was driven by the higher margins in its Lubricant (26.2%) segment compared to Petrol or PMS(4.2%)

Improved performance on an adjusted basis

Despite marginal uptick in revenue and improved cost efficiency, operating profit fell 16.0% y/y to N4.1bn in FY-2020. However, adjusting for the non-recurring profit of N2.6bn booked on disposal of the company's stake in Amperion Power Distribution Company Limited (Amperion), Forte Upstream Services Limited (FUS) and AP Oil and Gas Ghana, Operating profit was up 46.6%, in the period under review, better projecting Ardova's performance in FY-2020. A moderation in the yield environment in 2020 saw finance cost moderate by 68.9% y/y to N1.5bn in FY-2020. Finance income also declined by 94.1% y/y, mainly due to interest on subsidy booked of N3.9bn in 2019 . Overall, net finance cost increased by 356.1%. Consequently, profit before tax and profit after tax declined 37.6% y/y and 52.6% y/y, to N2.9bn and N1.8bn in the period under review. EPS fell to N1.4 per share in FY-2020. The firm proposed a dividend of N0.19N per share, representing a 1.3% dividend yield at the current price, subject to shareholders approval at its AGM.

Our outlook for ARDOVA remains moderate, considering the firm's cost improvement and efficiency management drive observed in recent quarters; Operating margin and profit before tax margin were up 100bps and 47bps y/y, respectively, due to a 166bps

Balance sheet- Expansions in PPE drive balance sheet growth

Ardova's total assets in the period under review grew 10.4% to N68.4bn , mainly due to increases in building under construction, as the company continues to expand on its base (retail stations). Hence, PPE rose 49.0% to N15.2bn in the period. The company extended its debt/borrowing lines in the period under review, as total debt grew 121.1% y/y to N11.8bn. However, finance costs fell by -68.9% though average cost of borrowing settled at 10.5% mainly because the bulk of the borrowing was accessed via overdraft facilities. At 10.5%, ARVODA's cost of borrowing is well above discount rates on commercial papers which tumbled to a record low in 2020, with several large corporates issuing capital at sub -3%. As such, we opine that ARDOVA would benefit from a capital market program to optimize its funding cost, considering that the yield environment remains relatively friendly for private sector capital raise. Interest coverage was stronger at 3.9x in FY-2020 vs. 1.5x in FY-2019, respectively. Net cash flows from operations printed at N4.8bn in FY-2020, from N4.7bn in FY-2019.

OUTLOOK

Outlook for Ardova is moderate following uncertainty in the downstream oil and gas sector

Our outlook for ARDOVA remains moderate, considering the firm's cost improvement and efficiency management drive observed in recent quarters; Operating margin and profit before tax margin were up 100bps and 47bps y/y, respectively, due to a 166bps moderation in operating costs y/y (adjusting for gain on assets in 2019). However, due to the continued uncertainty around the adjustment of Petrol (PMS) prices, we have also tempered our optimism around full price recovery . Although the FGN made efforts to partially deregulate and moved away from its regulated pricing regime in 2020, recent dynamics in the market points to another episode of policy backflip. According to the PPPRA pricing framework, the landing cost of PMS should be in the range of N209-N212 per litre, considering the rising spot FOB Rotterdam prices The FX challenges and the continuation of the NNPC direct sale, direct purchase program (DSDP) means the NNPC through the PPMC remains the sole importer of PMS. As such, ARDOVA and other downstream players will continue to earn a retailer's margin for PMS sales.

In view of the foregoing, our expectation for the performance of ARDOVA in 2021 remains moderate as such, we retain our model assumption while awaiting details about the proposed acquisition.

Recently, the company disclosed its intentions to acquire Enyo. Clearly, the Enyo acquisition fits nicely into ARDOVA's expansion drive and would complement its retail base. ARDOVA currently has a network of about 450 or more stations, Enyo will add to this strong base with about 90 or more retail outlets in 15 Nigerian states. While we are unable to factor in the potential impact of the acquisition into our model estimates for now due to non-availability of the official data, we expect this to further bolster volumes and improve overall performance due to a potential benefit from economies of scale.

In view of the foregoing, our expectations for the performance of ARDOVA in 2021 remain moderate. As such, we retain our model assumption while awaiting details about the proposed acquisition. Nevertheless, adjusting our valuation estimates for a higher risk-free rate, we adjust our Target Price for ARDOVA to **N17.63** compared to the current market price of N14.85. This portends an upside of 19.6% thus we retain our **BUY** rating on the ticker.

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ARDOVA Plc: Summary Financials

Earnings Flash | ARDOVA Plc FY-2020 Audited Result

Financial Highlights (N'Mn)			
Headlines	**FY - 2020**	**FY- 2019**	**Change**
Revenue	**181,938**	**176,550**	3.1%
Cost of Sales	-169,808	-165,269	2.7%
Gross Income	**12,130**	**11,281**	**7.5%**
Other Income	1,472	4,317	-65.9%
Operating Expense	-9,465	-10,673	-11.3%
Operating Profit	**4,137**	**4,925**	**-16.0%**
Finance Income	270	4,555	-94.1%
Finance Costs	-1,502	-4,825	-68.9%
Profit Before Tax	**2,905**	**4,655**	-37.6%
Taxation	-1,047	-739	41.7%
Profit After Tax	**1,858**	**3,916**	-52.6%
	FY - 2020	**FY - 2019**	
Cash and Cash Equivalents	3,006	1,984	51.49%
Trade & Other Receivables	**28,490**	**16,678**	70.82%
Trade & Other Payables	35,481	22,823	**55.46%**
Total Debt	11,804	5,329	121.51%
Total Assets	**64,846**	**47,019**	**37.91%**
Net Assets	18,021	16,163	**11.49%**
Gross Margin	**6.7%**	**6.4%**	**0.3%**
Cost to Sales	**93.3%**	**93.6%**	**-0.3%**
Net Margin	**1.0%**	**2.2%**	**-1.2%**
Leverage (Debt/Equity)	**65.5%**	**33.0%**	**32.5%**
Leverage (Net Debt/ Equity)	**48.8%**	**20.7%**	**28.1%**
Price(N)	**14.85**		
EPS(N)	**1.43**		
BVPS(N)	**13.84**		
P/E (x)	**10.27**		
P/BV (x)	**1.06**		
Trailing 12M ROAE	**10.87%**		
Final Dividend (N)	0.19		
Dividend Yield	1.3%		

Disclosure Appendix

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United Capital Research adopts a 3-tier recommendation system for assets under our coverage: Buy, Hold and Sell. These generic ratings are defined below;

Buy: Based on our valuation and subjective view (if any), the total return upside on the stock's current price is greater than our estimated cost of equity.

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Sell: Based on our valuation and subjective view (if any), the total return upside on the stock's current price is less than the Standing Deposit Facility rate of the Central Bank of Nigeria (which is currently MPR – 200bps; i.e. 10%). We consider this as the minimum return that may deserve our holding of a risk asset, like equity, especially as we consider the average 4.5% total transaction cost for an average retail investor.

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Dangote Flour Plc	h
Dangote Sugar Plc	h
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