EABL EARNINGS UPDATE:

Growth Galore in FY 19 performance

July 26, 2019

EABL

Rating:	**BUY**
Target Price	**256.60**
Current Price	**203.25**
Upside	**25%**
Dividend Yield(ntm)	**4%**
Forecast Total Return	**29%**
52- Week trading range	**268 to 160**

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- **EABL market price continues to be driven by Global Macros rather than company specific factors:** The market valuation of **EABL** remains low driven by reduced investor appetite for frontier market equities in the face of rising global uncertainty. We maintain our **BUY** rating despite rising geopolitical tensions and increased downside risks to global economic growth because we believe that global financing conditions are becoming increasingly accommodative. Fed rate cuts and a possible resolution of the US-China later this year could increase the global appetite for global equities and provide a tailwind for asset prices.
- **We maintain a our BUY rating but update our valuations to reflect our new outlook on the Group:** We have adjusted the Group's valuation to incorporate new assumptions. We have now updated the cost of debt upwards towards 12.5% to cater for the possibility of a rate cap repeal in the medium term. We have also tapered down our profitability margin to align our model with a faster than we had anticipated utilization of the Kisumu plant. Our Target Price has now been revised downwards to **KES 253.60**, **24.8%** above the current market price of **KES 203.25**. We have also revised our target Capital structure to 50% debt and 50% as managements indication that they were looking to mature the debt over the medium term necessitated an overhaul in our previous assumption.
- **The 11% growth of Group's volumes drove the 12% broad based growth of the Group's Net Sales:** EABL's Net-Sales grew an impressive **12%** beating our expectation of a **4.1%** NSV growth in **FY19**. The growth suggests that the group were able to build on their previously impressive **13% HY19** growth of both volumes and Net Sales. The **FY19** performance represents only the third time since **FY11** (**16.1%** in **FY11** & **23.7%** in **FY12**) that the group has attained double digit growth in NSV growth. The normalization of operating environment in Kenya after the 2017 elections along with the recovery of consumer confidence inspired by low food inflation were most likely the key drivers of the group's impressive FY19 performance.
- **Cost of Sales lets of pressure on Gross Profit:** Positive procurement savings, logistic savings in **FY19** and a positive product mix help let off Cost of Sales (**COS**) impact on the bottom line. The Cost of Sales as a percentage of Revenue declined to **53.8%** in **FY19**, **210 basis points** (**bp**) lower than the **55.9%** and **55.7%** COS to sales ratios witnessed in **FY18** and **FY17** respectively. Management also pointed out that the increased contribution from Senator Keg, which is has relatively lower COS than the overall mix but marketing intensive may have played a part in the lower COG.
- **Gross Margin Performance improved but was lower than we had anticipated:** We had expected operating profits to stand at KES 21.6Bn, higher than the actual KES 21.5Bn witnessed in FY19. Higher than expected administrative cost and selling costs were responsible for the differences. That meant that the actual operating margin stood at 25.7% lower than the 28.3% we had envisioned.
- **PBT performance was better than our expectation but PAT was in-line with expectation.** PBT Actual FY 19 performance of KES 17.8Bn was 13.6% above our KES 15.7Bn projection for FY19. Our FY19 PAT projections were, however, only 5% below the actual FY19 PAT performance of KES 11.52Bn. The fact that the actual tax burden for EABL was at 35.4% above our assumed tax burden of 30%, helped line the actual earnings performance to our projections.

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