

MITA No. 010/06/2008

2 April 2009

# Olam International Ltd

Downgrade to

## HOLD

Previous Rating: BUY

### S\$1.44

### Fair Value: S\$1.51

Stock Code:

Reuters: OLAM.SI

ISIN Code O32

Bloomberg: OLAM SP

Event: Update

#### General Data

Issued Capital (m)	1,713
Mkt Cap (S\$m/US\$m)	2,467/1,624
Major Shareholder	
Kewalram Singapore Ltd	(24.28%)
Free Float (%)	69.5%
NAV per share (S cents)	48.1
Daily Vol 3-mth ('000)	11,317
52Wk High (S\$)	3.190
52Wk Low (S\$)	0.835

## Downgrading to HOLD on valuations

**Laudable growth amid a recessionary environment.** Olam International Ltd (Olam) stands out in the current recessionary environment for its resilient earnings growth profile. Despite the global economic recession and slump in commodities prices, management remains confident of delivering 25% to 30% earnings CAGR over the next three years. Growth will be driven by increase in volumes, achieved via market share gains or by inorganic growth.

**Merits already in the price.** The stock has surged by over 21% since we initiated coverage with a BUY rating on 12 Mar 09. At current levels, it is trading at 13.3x current PER and 3.9x NAV, substantially higher than its peer Noble Group Ltd (Noble) which is commanding just 7.2x PER and 1.5x NAV, and also richer than the STI's 11.4x PER and 1.0x NAV. We continue to see merit in Olam's defensive earnings trait and ability to grow profits amid a recessionary environment, but are of the view that price valuation could have run ahead of its strong fundamentals. In addition, we note that Olam's balance sheet strength pales in comparison to its peers.

**Potential lag during economic recovery.** According to the International Monetary Fund's (IMF) estimates, commodity markets are expected to recover from their recent troughs. The energy and metals markets are expected to outperform the food market during the economic recovery (exhibit 1). Given that Olam participates only in agricultural commodities (mainly food, for which demand is relatively inelastic), whereas Noble's portfolio encompasses a broader spectrum of commodities spanning agriculture, energy, metals, minerals and ores, Olam may underperform as demand-supply fundamentals and macroeconomic sentiment improve. It may also stand to gain less from governments' pump-priming initiatives given the lack of exposure to hard commodities.

**Downgrade to HOLD on valuations.** Nevertheless, in the near term, Olam will continue to gain favour for its resilient earnings growth profile amid an environment of earnings contraction. We are keeping our estimates intact but raising our fair value estimate to S\$1.51 (from S\$1.37) based on 11x FY10 PER (previously 10x) as we realign it with the STI's valuations. Given the limited upside to our target, we downgrade Olam to **HOLD**. We will turn buyers again at lower entry levels of around S\$1.37.

**Lee Wen Ching**

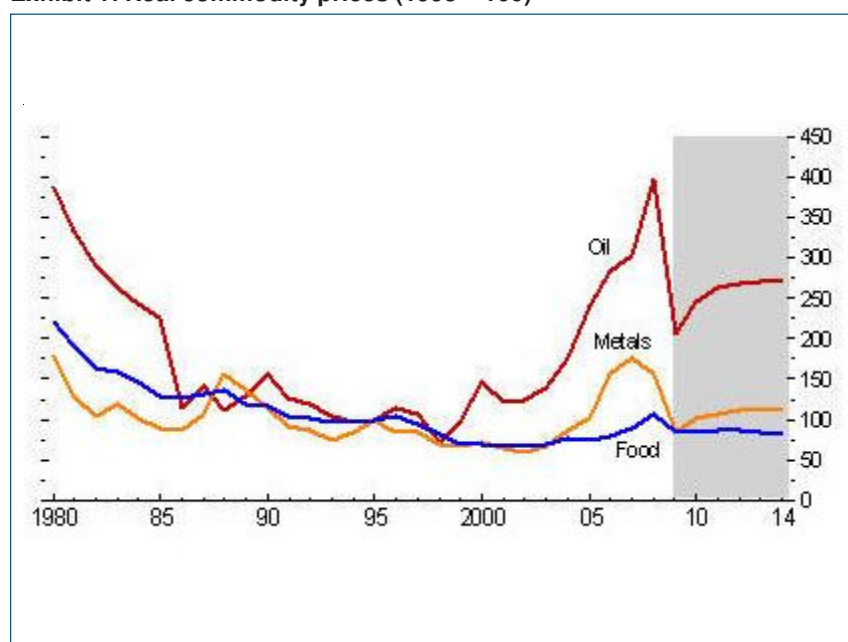
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Year to 30 Jun	Turnover (S\$m)	EBIT (S\$m)	Net Profit (S\$m)	EPS (cents)	EPS Growth (%)	PER (x)	Div Yield (%)
FY 07	5,455.5	273.6	109.0	6.7	20.8	21.4	2.4
FY 08	8,111.9	366.5	167.7	10.1	49.6	14.3	1.7
FY 09F	9,186.0	566.9	286.7	10.8	7.5	13.3	2.9
FY 10F	9,942.3	505.7	235.1	13.7	26.6	10.5	2.4

Please refer to the important disclosures at the back of this document.

Exhibit 1: Real commodity prices (1995 = 100)



Source: IMF estimates

## Olam's Key Financial Data

### EARNINGS FORECAST

Year Ended 30 Jun (\$ m)	FY07	FY08	FY09F	FY10F
Sale of goods	5,455.5	8,111.9	9,186.0	9,942.3
Other income (including buy-back of CB)	22.1	40.5	101.0	0.0
Cost of goods sold	4,275.9	6,519.2	7,293.7	7,894.2
Gross Profit	1,201.7	1,633.2	1,993.3	2,048.1
Shipping and logistics	661.9	879.5	918.6	994.2
Commission and claims	68.2	61.0	73.5	79.5
Employee benefit expense	95.5	169.2	192.9	208.8
Depreciation	17.2	33.8	39.3	41.2
Net measurement of derivative instruments	0.2	-11.0	0.0	0.0
Forex gains	-43.7	-21.5	0.0	0.0
Other operating expenses	128.7	155.7	202.1	218.7
EBIT	273.6	366.5	566.9	505.7
Share of JV/associates profit	0.4	0.2	0.0	0.0
Finance costs	147.1	201.4	233.6	232.3
Profit before tax	126.2	165.0	333.3	273.3
Tax	-17.2	2.7	-46.7	-38.3
Profit for the year	109.0	167.7	286.7	235.1
Minority interests	0.0	0.0	0.0	0.0
Reported net profit	109.0	167.7	286.7	235.1
Core net profit	109.0	150.8	185.7	235.1
Core EPS (S cents)	6.7	10.1	10.8	13.7
<b>Profitability Ratios</b>				
Gross margin (%)	21.9%	20.0%	21.5%	20.6%
PBT margin (%)	2.3%	2.0%	3.6%	2.7%
Net profit margin (%)	2.0%	2.1%	3.1%	2.4%

**BALANCE SHEET**

<b>As at 30 Jun (S\$ m)</b>	<b>FY07</b>	<b>FY08</b>	<b>FY09F</b>	<b>FY10F</b>
Cash and cash equivalents	237.6	339.1	641.6	789.3
Inventories	1,163.2	1,790.2	1,653.5	1,590.8
Trade receivables	508.2	724.4	643.0	696.0
Other current assets	942.8	2,759.9	2,736.8	2,790.2
Property, plant, and equipment	129.3	403.4	424.1	442.9
Other non-current assets	196.5	213.3	525.2	525.2
<b>Total assets</b>	<b>3,177.6</b>	<b>6,230.3</b>	<b>6,624.1</b>	<b>6,834.4</b>
Debt	1,919.9	2,984.6	3,114.6	3,097.5
Current liabilities excluding debt	825.0	2,607.3	2,656.1	2,707.2
Non-current liabilities excluding debt	0.0	0.0	0.0	0.0
<b>Total liabilities</b>	<b>2,744.8</b>	<b>5,591.9</b>	<b>5,770.7</b>	<b>5,804.7</b>
Shareholders equity	432.7	638.4	853.4	1,029.7
Minority interests	0.0	0.0	0.0	0.0
<b>Total equity</b>	<b>432.7</b>	<b>638.4</b>	<b>853.4</b>	<b>1,029.7</b>
<b>Total equity and liabilities</b>	<b>3,177.6</b>	<b>6,230.3</b>	<b>6,624.1</b>	<b>6,834.4</b>
NAV per share (S cents)	27.8	37.3	49.8	60.1
NTA per share (S cents)	21.6	29.7	42.2	52.5

**CASH FLOW**

<b>Year Ended 30 Jun (S\$ m)</b>	<b>FY07</b>	<b>FY08</b>	<b>FY09F</b>	<b>FY10F</b>
Operating profit before working cap. changes	284.6	371.5	606.2	546.8
Working capital changes, taxes and interests	-445.2	-1,083.0	9.8	-263.2
<b>Net cash from operations</b>	<b>-160.6</b>	<b>-711.5</b>	<b>616.0</b>	<b>283.6</b>
Purchase of property, plant and equipment	-45.8	-74.2	-60.0	-60.0
Other investing flows	-215.5	-141.3	-311.9	0.0
<b>Investing cash flow</b>	<b>-261.4</b>	<b>-215.5</b>	<b>-371.9</b>	<b>-60.0</b>
Financing cash flow	362.8	952.2	58.3	-75.9
Forex	-20.6	-48.6	0.0	0.0
<b>Net cash flow</b>	<b>-79.8</b>	<b>-23.4</b>	<b>302.4</b>	<b>147.7</b>
Cash at beginning of year	267.4	187.6	164.3	466.7
Cash at end of year	187.6	164.3	466.7	614.4
Bank overdrafts	50.0	174.9	174.9	174.9
Cash and cash equivalents at end of year	237.6	339.1	641.6	789.3

**Key Ratios**

PER (x)	21.4	14.3	13.3	10.5
Price/NAV (x)	5.2	3.9	2.9	2.4
EV/EBITDA (x)	14.3	12.8	8.1	8.7
Dividend yield (%)	2.4	1.7	2.9	2.4
ROE (%)	25.2	23.6	21.8	22.8
Net gearing (%)	388.8	414.4	289.8	224.2

*Source: Company data, OIR estimates*

**SHAREHOLDING DECLARATION:**

The analyst/analysts who wrote this report holds NIL shares in the above security.

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