Astral makes hay while the sun shines

Well-positioned to weather stormy seas ahead.
Sasha Planting | 17 November 2015 00:10
Investors who bought into Astral Foods on the back of a superb trading update in early November will have made a 17% loss as the share fell from R171.50 at the time, to R153 on Monday.

This just goes to show that markets are forward looking, not backward looking, says Anthony Rocchi, a portfolio manager with Rexsolom Invest.

And what the market sees is trouble. While Astral and peers like Sovereign Foods and RCL Foods have all delivered better results thanks to benign trading conditions and after four tough years, the clouds are once again building on the horizon.

These include slowing economic growth and a drought that has already driven maize futures prices to R3000/ton. In addition the renewal of the African Growth and Opportunity Act (AGOA) resulted in an annual quota of 65 000 tons of US poultry, free of anti-dumping duties. This is likely to negatively impact local producers as high levels of poultry imports continue unabated.

There is also a strong likelihood that brining regulations will be introduced in the foreseeable future, which could result in lower volumes for the industry, and higher selling prices for the consumer.

Astral is the dominant player in its sector and over the last two to three years has made use of its strong balance sheet to acquire good assets at good prices. These have contributed to a healthy set of results for the year to September 30.

Revenue from the poultry, feed and other Africa businesses increased by 17% to R11.3 billion while profit before tax leapt by 133% to R1.09 billion.

The poultry division, the biggest producer of revenue and earnings, was a key contributor to the results. The acquisition of Quantum's Western Cape broiler operations in 2014 added an estimated 10% to group volumes in the year, and contributed to the impressive 25% revenue growth in Astral's poultry division, says Dirk van Vlaanderen, investment analyst at Kagiso Asset Management.

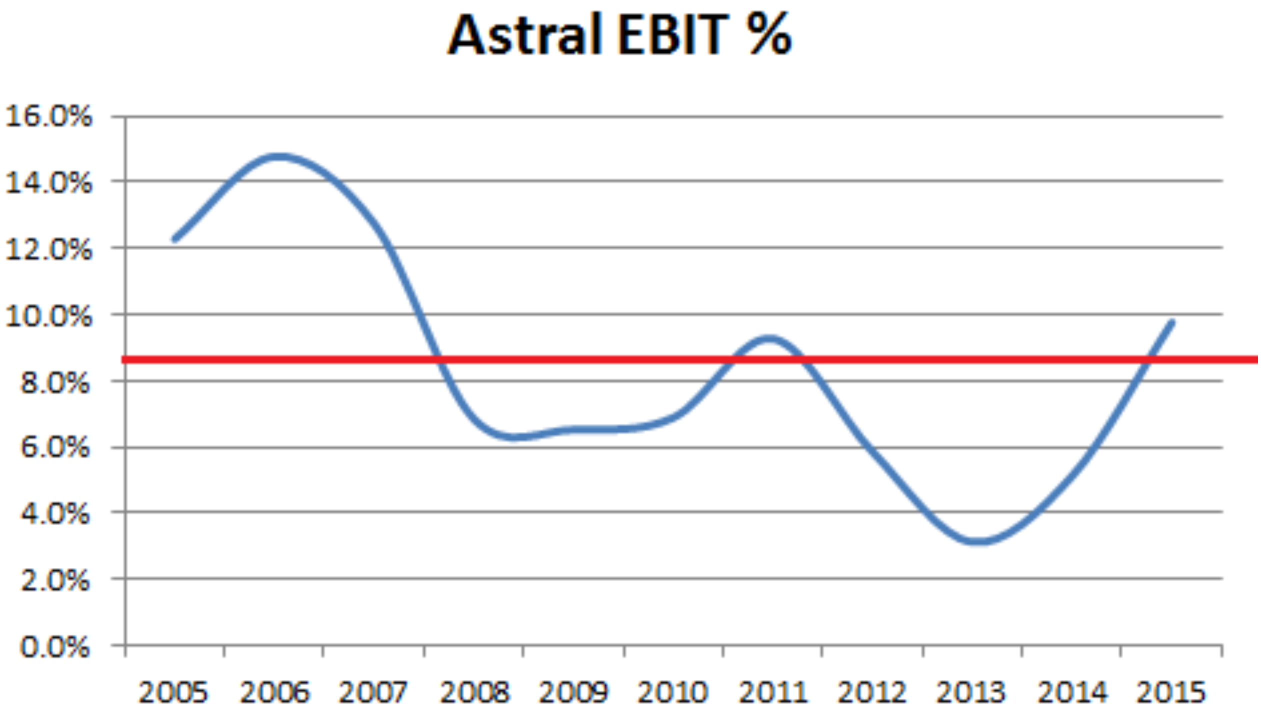
Improved pricing also helped drive revenue growth, adding 12% to the top-line as the anti-dumping duties imposed on some EU nations resulted in a reduction in cheap imports and firmer market pricing, he says.

The increase in headline earnings from R329.7 million for the previous year, to R779.6 million for the 2015 financial year, is mainly attributable to a material improvement in poultry's profits (which rose to R661m from R104m). These are due to significantly lower feed prices.

However feed prices are already under pressure. "Maize futures prices are already trading at over R3 000/ton," says Rocchi. "Poultry producers make comfortable margins around R1800/ton. Higher prices are likely to push them back onto the chains because they cannot push their prices up to the same extent."

The only disappointment in the results came from the tiny Africa division, which saw operating profit fall to R16.6 million from R34.8 million, impacted by weaker currencies of other African countries.

Good control of costs meant that operating margins (of 9.8%) have now surpassed levels that were last seen in 2011.



Source: Rexsolom Invest

Diluted earnings per share rose by 127% to 2009c.

Astral is a hugely cash generative company and this year was no exception. Cash generated from operating activities rose to R995.5 million, a 41.4% increase on the previous year's R704.1 million.

Astral shareholders will be delighted by the company's ever improving dividend yield, which saw shareholders receive 575c/share for the year, bringing the full year dividend to R11.50, and driving the dividend yield up to 7.5%.

While the future does not look bright, the company is resilient, with low debt levels and good fundamentals. "Astral weathered the last storm because of strong free cash flows and an integrated business model which sees them sell feed and poultry," says Rocchi. He gives the company a free cash flow (FCF) score of 2.11 over the last ten years. This means that for every one rand invested in capex and acquisitions the company generated R2 in cash from operations. "It is essential to look for a company with a positive FCF score. One is good, two is above average."

The share ended the day marginally up at R152.81.