

# Oceania Natural

**Consumer goods**
**3 April 2017**

## Variation from key operating milestones

Oceania Natural (ONL) is an early-stage New Zealand company involved in producing and distributing natural food and diet supplements sourced from New Zealand and the Pacific Islands, and sold both domestically and in the People's Republic of China. The company has announced that the board has approved a "one off" sale of manuka honey to a distributor at a reduced margin. As a result, operational performance is likely to vary by more than 10% from the targeted key operating milestones (KOMs) for the year to March 2017.

### "One-off" sale approved

As we noted in our January 2017 Spotlight report, ONL removed Q4 manuka honey sales to Chinese distributors from its FY17 KOM targets after being unable to reach agreement on selling prices with those distributors. This followed an extended period of competitive discounting for manuka honey products in Chinese markets. The board has now approved a "one off" sale of manuka honey to a distributor at a reduced margin. The effect of this is a switch from the direct sales channel to the distributor channel with a net expected over-achievement against the targeted revenue for FY17, but at a reduced gross margin.

### Distributor sales higher than target

Total revenue for FY17 is likely to be in the range of NZ\$2.25 -2.40m, compared to the FY17 KOM target of NZ\$2.22m, an increase of NZ\$30,000-180,000. Within this, distributor sales are expected to increase by NZ\$295,000-345,000 and direct sales to decrease by NZ\$165,000-265,000 compared with the KOM targets. The changes in expected revenue are set out in Exhibit 1 on page 2.

### Lower gross margin expected

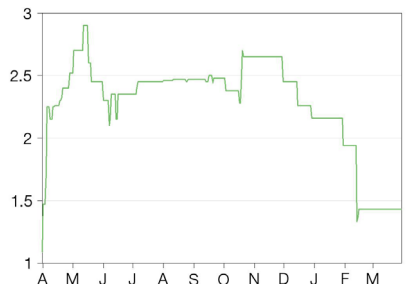
Although the "one-off" sale agreement has the effect of increasing total revenue, it will result in a lower gross margin due to the change in sales channels. This is expected to be in the range of 26-32% compared with the KOM target of 40%.

### Valuation: Share price implies 15-16x FY17e EV/sales

Since listing on the NXT on 31 March 2016, ONL's share price has more than doubled, although it is now just over half its October 2016 high. The current price implies an EV/sales multiple of 10.8x FY16 sales and 15-16x the expected FY17e sales. This is well ahead of the 2.3x average of its well-established listed peers (see Exhibit 2).

**Price** **NZ\$1.43**  
**Market cap** **NZ\$37m**

#### Share price graph



#### Share details

Code **ONL**  
 Listing **NXT**  
 Shares in issue **26.2m**

#### Business description

Oceania Natural is a producer, distributor and reseller of natural food and supplement products sourced from New Zealand and the Pacific Islands, sold predominantly into the People's Republic of China. Its chief products are manuka honey and related products, Noni juice and dietary supplements.

#### Bull

- Tapping into demand for clean NZ products.
- Huge market potential in China.
- Board has strong experience in consumer products companies.

#### Bear

- Price competition.
- Regulatory constraints in China.
- Small player competing with large incumbents.

#### Analysts

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#### Historical performance

Year end	Revenue (NZ\$000s)	EBITDA (NZ\$000s)	EBIT (NZ\$000s)	NPAT (NZ\$000s)	Net cash (NZ\$000s)	Net assets (NZ\$000s)
03/15	1,512	45	20	1	4	(65)
03/16	3,351	305	276	183	(736)	1,874

Source: Oceania Natural

## Expected outturn against key operating milestones (KOMs)

We set out below the expected outturn compared with the KOMs:

<b>Exhibit 1: Expected FY17 outturn against KOMs</b>			
NZ\$000s	KOM	Current expectation	+/(-)
Total revenue	2,220	2,250-2,400	30-180
Direct sales	1,615	1,350-1,450	(165)-(265)
Distributor sales	605	900-950	295-345
Gross margin (%)	40	26-32	(8)-(14)

Source: Oceania Natural, Edison Investment Research

### Peer comparison

ONL's listed peers are predominantly Australian and New Zealand honey and health products companies. They are well-established companies in more mature stages of their lifecycles. We note that multiples at Comvita are exceptionally high as a result of its own issues with sales channels into China combined with an exceptionally poor harvest in 2016/17.

Nevertheless, the average EV/sales multiple of this group of 2.3x (Exhibit 2) is well below the EV/sales multiple implied by ONL's current market capitalisation. With a market capitalisation of NZ\$37m and net cash of NZ\$1.4m at 30 September 2016, the EV/sales multiple on ONL's actual sales for FY16 is 10.8x, while the EV/sales multiple implied by ONL's range of expected FY17e revenue is 15-16x.

### Exhibit 2: Peer comparison based on 12-month forward consensus

Company	Country	Currency	Price	Market cap (m)	P/E (x)	EV/sales (x)	EV/EBITDA (x)	EBITDA margin (%)	Operating margin (%)
Blackmores	Australia	A\$	112.9	1,945	28.3	3.0	18.4	17.8	15.9
Capilano Honey	Australia	A\$	14.18	134	13.1	1.1	9.1	11.9	10.5
Comvita	New Zealand	NZ\$	8.6	365	74.8	2.8	24.7	11.3	6.3
<b>Average</b>					<b>39</b>	<b>2.3</b>	<b>17.4</b>	<b>13.7</b>	<b>10.9</b>

Source: Bloomberg; Note: Prices as at 30 March 2017.

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