EDISON

Scale research report - Update

Tonkens Agrar

Food & beverages

23 April 2018

Value-added strategy drives H118 uplift

Management's strategy of generating more profit from its crops by selling processed onions and potatoes, supported by higher farm gate milk prices and an exceptional profit on the sale-and-leaseback of land, delivered a three-fold increase in profit after tax during H117/18. Management has raised FY17/18 guidance and now expects a year-on-year increase in both revenues and profit after tax.

Profit after tax trebles

Group revenues rose by €0.5m year-on-year during H117/18 to €8.2m. This was attributable to the successful expansion of sales of processed potatoes and onions. Improved milk prices were offset by extremely low prices for unprocessed potatoes. The cost of materials as a percentage of revenues dropped from 46.6% in H116/17 to 45.5%, as material costs grew more slowly than revenues. Personnel cost increases were limited to 2%. Profit after tax rose by €1.9m to €2.6m. This was partly the result of a more than 70% increase in the volumes of peeled potatoes processed, which is a high-margin activity, partly a €0.9m uplift in other income, which benefitted from the sale-and-leaseback of property. Net debt reduced from €17.7m at end June 2017 to €16.5m, cutting gearing from 193% to 140%.

Management raises FY17/18 guidance

In December management noted that it did not expect revenues to grow during FY17/18 or a further narrowing of losses because of weak potato prices. While management feels it is still too early to make reliable predictions about the harvest this year, farm gate milk prices remain favourable, German grain prices are stable and continued initiatives to attract new customers for processed products are helping boost volumes and plant utilisation in the warehousing and marketing segment. Management now expects FY17/18 sales to be higher than the prior year, resulting in a significant improvement in the result from operating activities and a net profit after tax for the period.

Valuation: Trading below net asset value

The shares have dipped from a peak of €7.40 in September but are still trading on multiples that are above the mean for our sample of agricultural producers. We note that at current levels the market capitalisation (€9m) is substantially below both the reported net asset value (€11.8m) and the reported value of land and buildings at the end of December 2017 (€13.9m).

Financial summary

Year end	Revenue (€m)	PBT (€m)	EPS (€)	DPS (€)	P/E (x)	Yield (%)
06/14	15.9	1.2	0.32	0.00	16.6	N/A
06/15	13.8	(1.2)	(0.43)	0.00	N/A	N/A
06/16*	14.8	(2.0)	(0.99)	0.00	N/A	N/A
06/17	15.4	(0.9)	(0.48)	0.00	N/A	N/A

Source: Company data. Note: *Restated for BilRuG.

Price	€5.30
Market cap	€9m

Share price graph

Share details

Code	GTK
Listing	Deutsche Börse Scale
Shares in issue	1.66m
Last reported (€m) net debt at end December 2017	16.5

Business description

Tonkens Agrar is engaged in the cultivation of crops including cereals, potatoes, onions and oil seed rape; the storage, processing and marketing of vegetables; milk production; and the production of renewable energy from biogas plants that run on waste produced by the group and from photo-voltaic installations. It farms c 3,500 hectares of high-quality land in the Saxony-Anhalt region of Germany.

Bull

- Demand for agricultural staples relatively unaffected by economic conditions.
- Demand for agricultural produce supported by rising global population.
- Vegetable processing improves margins.

Bear

- Output affected by weather conditions and pests.
- Profitability affected by commodity price fluctuations.
- Low free float (32.2%).

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Edison profile page

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Divisional analysis

Tonkens Agrar's c 3,500 hectares of high quality farmland in the Saxony-Anhalt region of Germany is the starting point for a vertically integrated agricultural production group. It peels and chops the potatoes and onions grown on the farm in-house, substantially adding value to the harvested vegetables. Manure from the dairy herd and residual material from harvesting and processing crops are used to generate electricity, creating an additional revenue stream that is relatively predictable and non-seasonal. Some of the maize grown on the farm is used as cattle feed.

Warehousing and marketing (37% H17/18 revenues)

Segmental revenues grew by 19% year-on-year during the six months ended December 2017. This reflects success in expanding sales of peeled and packaged potatoes and onions by over 70%. Output benefitted from prior-year investment in special storage containers and cooling systems so that potatoes could be stored for longer. Management remains focused on improving capacity utilisation by attracting additional larger customers.

Agriculture (27% H117/18 revenues)

Segmental revenues dropped by 21% year-on-year. Although Tonkens outperformed nationwide average crop yields, as in the previous year, it reported slightly lower harvest volumes for all crops apart from potatoes. This volume decrease was caused by unfavourable weather conditions with the harvest repeatedly interrupted by rain. Prices for cereals were similar to the prior year, but still unattractive. Oilseed rape prices were lower than the previous year and oversupply of potatoes resulted in extremely low prices for unprocessed potatoes that were below the cost of production.

Milk production (22% H117/18 revenues)

Segmental revenues increased by 29% year-on-year. This was primarily the result of an increase in farm gate milk prices, which rose from 22c per litre, below the cost of production, in July 2016 (start of H116/17), to 33c per litre in June 2017 (start of H117/18). As milk production in Germany grew by 5% between December 2016 and December 2018, farm gate milk prices have begun to reduce as the previous imbalance between supply and demand is evening out. Tonkens recently received 34c per litre compared with an average of 38c per litre during the six months ending December 2017. Further price movements are possible over the remainder of the financial year.

Renewable energy (13% H117/18 revenues)

Segmental revenues showed a very modest (2%) year-on-year decline. Management does not intend to expand this segment because of the uncertainty regarding subsidies for electricity produced from either biogas or solar panels. The activity is retained because the biogas plants represent a mechanism for generating a steady and predictable income from the residual materials from both agricultural production and vegetable processing as well as manure from the dairy herd. The waste product from the biogas plants, a mash, is used as a fertiliser on the group's farmland, reducing the amount that needs to be purchased.

Valuation

The shares have fallen from a peak of €7.40 in September but are still trading on multiples that are above the mean for our sample of agricultural producers. We note that the current market capitalisation (€9m) is substantially below both net asset value (€11.8m) and the value of land and buildings at the end of December 2017 (€13.9m).

Exhibit 1: Peer group companies

Company	Market cap (€m)	Historic EV/sales (x)	Historic EV/EBITDA (x)
Agrogeneration	39	1.4	4.4
Agroliga Group	6	0.4	1.9
Agromino	32	1.4	7.9
Austria Technologie & System	911	1.6	9.9
Firstfarms	37	2.7	11.8
Kre.Ka	1	1.0	-
Produce Investments	48	0.4	5.2
Mean		**1.3**	**6.9**
Tonkens Agrar	9	1.7	13.0

Source: Bloomberg. Note: Prices at 20 April 2018.

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