

Zeder Investments Ltd

Improved weather brightens prospects for subsidiaries

Background

Zeder is an investment holding company focused on the agricultural, food, beverages, grain and related industries. It holds 27.1% of Pioneer Foods, 26.7% of Quantum Foods, 39.8% of Kaap Agri and is the majority shareholder in Capespan, Zaad and Agrivision Africa.

Our Thoughts

Zeder's share price has been under pressure over the past two years. Much for the underperformance has been due the tough agricultural cycle however.

We value the group's investment portfolio at 845c/share. Nonetheless, we do not expect its shares to trade anywhere near that price. The market normally values investment companies at a discount to their net asset value (NAV) due to the perceived inefficiencies of an additional layer of management costs. Over the past two-and-a-half years, Zeder's shares traded at an average discount of 16% to its NAV. We applied this discount to arrive at a target price of 709c/share.

Pioneer Foods: This is Zeder's biggest investment and accounts for close to two thirds of our valuation for Zeder. Drought conditions over the two years have caused a lot of misery for Pioneer. Its latest interim earnings were 70% lower than the comparable half. Weather conditions have improved however, and SA is expected to have a bumper harvest. Soft commodity prices have softened significantly, reducing input costs for Pioneer. Soft commodities make up a significant portion of Pioneer's cost base, making the company highly sensitive to the agricultural commodity cycles. We also expect Pioneer to continue with capital projects and investments in production efficiencies – another area that we think may drive earnings growth. Given its lowly geared balance sheet, such initiatives can be achieved without stressing other metrics.

We expect Pioneer's earnings for FY18 to come in at between 800c/share and 815c/share. This puts its shares on a forward price:earnings (PE) ratio of around 14.5, which seems cheap relative to its historical average PE of 23. Our valuation provides for 20% upside in Pioneer's value.

Zaad: Things are also looking up for the unlisted Zaad, which is involved in the development and distribution of agri seeds in Africa, Europe and other emerging markets. The company is growing rapidly. It has grown headline earnings at an average of 42% a year over the past four years. Opportunities for further growth lie in the development of its proprietary seed genetics, an area the group is pursuing. We value Zaad at R2.19bn, which is in the ballpark of the valuation provided by Zeder. This valuation puts the counter on a 12-month justified forward PE of 13, which we think is appealing in relation to the kind of growth the company promises.

Capespan: The group's core business activities are focused on the production and trading of fruits worldwide. With annual revenue of over R8bn the group is a good cash generator. It is poised to post decent earnings growth in FY18, benefiting from the normalising rainfall pattern. We value the company at R1.89bn, which is 20% lower than Zeder's indicated value of R2.34bn. While the group has been growing its farming division to diversify its income streams, it is still heavily geared towards the trading business where margins are slim and can easily slip into losses. Our valuation puts the counter on a justified forward PE of 12.

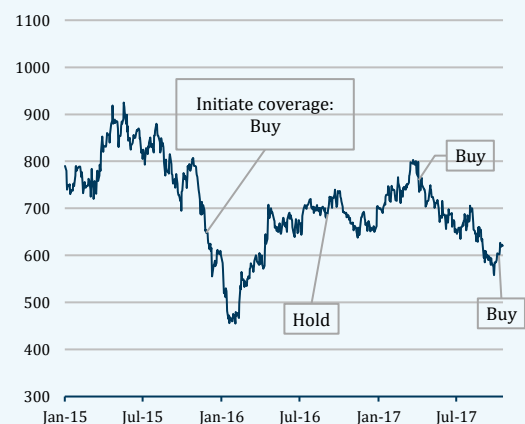
Kaap Agri: Kaap Agri is a retailer of a wide variety of products to the

Equity Research

BUY

12-month target price	709c
Spot share price	621c
12-month implied total return	14.3%

Zeder share price



Source: I-Net BFA

Key statistics

Market cap: R10.8bn
 Price:earnings ratio: N/A
 Forward PE ratio (FY17): N/A
 Risk: High
 12-month high: 810c
 12-month low: 540c
 Ave monthly volume: 28.9 million
 Financial year-end: 28 February

Latest event

Interim results
 Date announced: 14 October 2017

Share details

Company: Zeder Investments Ltd
 JSE Code: ZED
 Sector: Investment holding

Macroeconomic
drivers for
agriculture remain
strong

agricultural sector and the public. We expect the company's recent listing on the JSE to provide a platform to expand its operations from its Western Cape stronghold into other regions. The group is targeting growth of at least 15% a year in the medium term, which we think is attainable given the potential to grow its market share and make acquisitions. Its operating margin has been expanding over the past few years and there are opportunities for further margin gains through the optimisation of the supply chain and distribution centres. Despite what seems to be a decent outlook, our valuations show that the company, which is on a trailing PE of 12, is fully valued. Its short-term earnings will be compromised by the ongoing drought in the Western Cape.

Agrivision: We believe this asset, which focuses on large-scale commercial farming of wheat, soya beans and maize as well as milling in Zambia, has strong growth potential. Despite inevitable cyclicalities, its farming business of staple food has potential to offer attractive long-term returns. After rapid expansion over the past few years that has depressed its recent earnings, the company is geared to grow as management focuses now on achieving acceptable operational efficiencies. We value the company at R1.3bn.

Last month **Quantum Foods** reported that bird flu had affected at least two of its commercial layer farms in the Western Cape. It projects that the contagious strain is going to affect 17% of its national egg supply. This is going to offset any benefits likely to come from the declining input costs. Despite the setback, we expect to see some upward re-rating of the company, which is sitting on a PE of 11.

Performance Review

RESULTS IN BRIEF	1H17	Change	1H16	FY16
Recurring headline earnings (R'm)	115	-63%	314	821
Base management fee (R'm)	0	-100%	-75	-75
Attributable earnings (R'm)	127	-41%	214	-796
Heps (cents)	4.3	-70%	14.3	-47.5

Zeder's portfolio companies traded under challenging macro conditions over the six months to end-August. Its largest investment, Pioneer Foods, reported weaker interim earnings. Earnings growth from Kaap Agri and Quantum Foods was offset by declines from Pioneer Foods, Capespan, Zaad and Agrivision. Additionally, the first six months of Zeder's earnings reflect the annual input cost cycle associated with its unlisted agriculture and food business investments. Combined, these factors weighed heavily on its consolidated recurring headline earnings, which ended 63% lower than the corresponding half. Headline earnings plunged 69.9% to 4.3c/share (1H16: 14.3c/share).

Zeder's net asset value, calculated using the quoted market prices for all JSE-listed investments and market-related valuations for unlisted investments, decreased 9.5% during the reporting period to 772c/share (1H16: 840c/share) as at 31 August 2017.

Earnings likely to
improve in the next
reporting cycle

Bull Factors

- Improved weather conditions
- Defensive nature of agribusiness investments provides comfort over the long term
- New structure where the group no longer has to pay management fees to PSG to bolster profitability and cash flows

Bear Factors

- Inefficiencies that result from an extra layer of costs associated with investment holding companies remain and might serve as a deterrent for some investors
- Zeder's investments, particularly in markets outside SA, remain exposed to significant exogenous risk factors associated with agribusiness investments

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