

18 August 2010

## Landkom

Year End	Revenue (\$m)	PBT* (\$m)	EPS* (c)	DPS (c)	P/E (x)	Yield (%)
12/08	10.6	(57.4)	(29.1)	0.0	N/A	N/A
10/09	14.6	(27.5)	(11.9)	0.0	N/A	N/A
10/10e	26.8	(5.8)	(1.4)	0.0	N/A	N/A
10/11e	34.7	(3.6)	(0.8)	0.0	N/A	N/A

Note: \*PBT and EPS are normalised, excluding intangible amortisation and exceptional items.

## Investment summary: Harvest data reassures

In the face of fairly gloomy headline news from the region about poor crop yields due to unusual weather patterns, Landkom has announced initial harvest figures that are only marginally below our expectations of yield and are well ahead in terms of prices achieved and cost reductions. This confirms the news from the recent interim results announcement that the changes made by the new management team are beginning to have an impact. The harvest of the remainder of the crops will suffer some impact as a result of the weather, so, although we have increased our estimates slightly, we have remained reasonably cautious about the eventual out turn. This remains a key period for the new management and the indications are that the positive progress will show through in the full year numbers.

## Crop management results in relative out-performance

The yields achieved on the winter rapeseed are in line with last year's yields. Although this is marginally below our initial estimate, it is 60% higher than the yields achieved in the Ukraine as a whole – these were hit by a combination of unsuitable weather and weak farming practices. This confirms that the improved agricultural management regime is having the anticipated positive effect.

## Cost control drives profit potential

Containment of direct costs was promised as part of the improvement in farm management. This objective has also been exceeded and while relative yields have improved the costs of achieving them have been cut substantially.

## Valuation: Raised estimates support positive price trend

The unsettled weather conditions in the region mean that yields on the remainder of the harvest are not yet certain, but, in compensation, commodity prices have been driven up. This, combined with the success in cost control, means that we have increased our estimates for the next two years. We have, however, born in mind the remaining uncertainties and have made the adjustments with a reasonable amount of caution. The positive general direction of the news flow does, though, continue to support our view that the upward trend in the share price is on the right track.

Price 10.5p  
Market Cap £46m

## Share price graph



## Share details

Code LKI  
Listing AIM  
Sector Food Producers  
Shares in issue 435.01m

## Price

52 week High Low  
14.3p 5.00p

## Balance Sheet as at 30 April 2010

Debt/equity (%) N/A  
NAV per share (c) 12.4  
Net cash (\$m) 2.1

## Business

Landkom International is involved in arable farming in Ukraine.

## Valuation

	2009	2010e	2011e
P/E relative	N/A	N/A	N/A
P/CF	N/A	N/A	30.0
EV/Sales	2.5	2.1	1.7
ROE	N/A	N/A	N/A

## Geography based on revenues

UK Ukraine  
0% 100%

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## Rapeseed harvest

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Landkom announced the results of the winter rapeseed harvest, which has produced 39,500 tonnes of crop from 14,615 hectares of harvested land. These numbers are virtually the same as those achieved last year, representing a yield of 2.7 tonnes per hectare. Although we had been anticipating a modest increase in the yield this year, these numbers are highly creditable given the well publicised weather problems in the region (Russia and Ukraine) and are substantially above the average, of 1.7 tonnes per hectare, achieved in Ukraine in 2010.

This relative success is evidence that the improved agronomic disciplines, put in place by the new management, are having the desired impact on productivity. Indeed, this has been achieved with a significantly lower direct cost of inputs. In line with previous indications, we had been anticipating that these costs would be reduced by around 35%, but this target has been exceeded as direct costs were down by 41%.

Lower yields in the market as a whole have helped push up commodity prices and Landkom has successfully exploited this position through a mixture of forward and spot selling. As a consequence, it has managed to improve on the price it had achieved at the time of the final results with contracts for around 92% of the harvest (the amount dried and certified so far) generating an average ex works/ex VAT price of \$323 per tonne.

## Other crops

As with rapeseed, the weather is having a dampening impact on crop yields, but is driving up prices. At present, Landkom has completed around 95% of its winter and 27% of its spring wheat harvests. The yields are not yet clear as the crop has not yet been dried. However, we are now expecting these yields to be below those used in our estimates. This trend will be broadly in line with that suffered in Russia and in the rest of the Ukraine but, as with rapeseed, we would anticipate that Landkom's yields will be better than the market average.

The lower yield will be counterbalanced by the rising prices, which are currently indicating an ex works/ex VAT price of around \$158 per tonne or nearly 70% higher than the average achieved last year. In addition, the company's efforts to reduce input costs for rapeseed have, as expected, been mirrored across the business. Thus the anticipated cut of 35% has again been exceeded with winter wheat cost falling by half and costs across all winter crops being down by 39%.

The harvest for wheat should be completed in the next two weeks, sunflower by the end of September and both maize and soya by the end of October. The unstable weather conditions make yield estimates more difficult and we have therefore maintained a fairly cautious view of the eventual outturn, which should be confirmed by announcements in the autumn.

## Strategic outlook

Plans for the year ahead remain in line with expectations. Land under cultivation will be expanded above 50k ha and kept within the working capital constraints created by self generated cashflow. In addition the company may be able to ease its constraints on capex slightly, enabling it to erect its second 20k tonnes storage silos and boosting its in-house storage capacity to 75k tonnes.

## Upgraded estimates

### Exhibit 1: Upgrades

Note: Figures in \$m except per share data (c).

	EPS			PBT			EBITDA		
	Old	New	% chg.	Old	New	% chg.	Old	New	% chg.
<b>2010e</b>	(1.8)	(1.4)	-	(7.4)	(5.8)	-	(1.0)	0.6	-
<b>2011e</b>	(1.1)	(0.8)	-	(4.8)	(3.6)	-	2.2	3.4	+54

Source: Edison Investment Research

The successful result of the rapeseed harvest, being the largest of Landkom's crops, combined with the better than expected prices achieved has more than compensated for low yields, and the tighter control of costs has encouraged us to increase our estimates for the current year. This swings the figures from a small EBITDA loss in 2010 to a small profit. We have, however, been reasonably cautious because uncertainties remain about the eventual yields on the other crops due to the negative mixture of heat and rain – these have been causing significant concerns about wheat harvests, in particular, in the region.

We have also improved our 2011 outlook as we would expect the cost control to be sustained and that yields will recover slightly. The latter assumes that the unusual weather conditions this year are not repeated.

## Exhibit 2: Financials

	US\$'000s	2007	2008	2009	2010e	2011e
Year end 31 October		IFRS	IFRS	IFRS	IFRS	IFRS
<b>PROFIT &amp; LOSS</b>						
<b>Revenue</b>		<b>1,567</b>	<b>10,645</b>	<b>14,553</b>	<b>26,782</b>	<b>34,675</b>
Cost of Sales		2,786	(47,354)	(36,613)	(30,547)	(35,517)
Gross Profit		4,353	(36,709)	(22,060)	(3,765)	(843)
<b>EBITDA</b>		<b>(1,426)</b>	<b>(56,123)</b>	<b>(20,891)</b>	<b>574</b>	<b>3,437</b>
<b>Operating Profit (before GW and except.)</b>		<b>(1,913)</b>	<b>(57,071)</b>	<b>(27,445)</b>	<b>(5,926)</b>	<b>(3,563)</b>
Intangible Amortisation		0	0	0	0	0
Exceptionals		0	0	(14,505)	0	0
Other		0	0	0	0	0
<b>Operating Profit</b>		<b>(1,913)</b>	<b>(57,071)</b>	<b>(41,950)</b>	<b>(5,926)</b>	<b>(3,563)</b>
Net Interest		589	(369)	(66)	150	0
<b>Profit Before Tax (norm)</b>		<b>(1,324)</b>	<b>(57,440)</b>	<b>(27,511)</b>	<b>(5,776)</b>	<b>(3,563)</b>
<b>Profit Before Tax (FRS 3)</b>		<b>(1,324)</b>	<b>(57,440)</b>	<b>(42,016)</b>	<b>(5,776)</b>	<b>(3,563)</b>
Tax		0	(236)	(20)	0	0
<b>Profit After Tax (norm)</b>		<b>(1,324)</b>	<b>(57,676)</b>	<b>(27,531)</b>	<b>(5,776)</b>	<b>(3,563)</b>
<b>Profit After Tax (FRS 3)</b>		<b>(1,324)</b>	<b>(57,676)</b>	<b>(42,036)</b>	<b>(5,776)</b>	<b>(3,563)</b>
Average Number of Shares Outstanding (m)		101.0	197.7	230.8	418.8	435.0
EPS - normalised (c)		(1.3)	(29.1)	(11.9)	(1.4)	(0.8)
EPS - FRS 3 (c)		(1.3)	(29.1)	(18.2)	(1.4)	(0.8)
Dividend per share (c)		0.0	0.0	0.0	0.0	0.0
<b>BALANCE SHEET</b>						
<b>Fixed Assets</b>		<b>13,515</b>	<b>48,829</b>	<b>40,546</b>	<b>35,046</b>	<b>31,046</b>
Intangible Assets		169	492	27	27	27
Tangible Assets		13,346	48,337	40,519	35,019	31,019
Investments		0	0	0	0	0
<b>Current Assets</b>		<b>103,323</b>	<b>35,979</b>	<b>10,171</b>	<b>24,288</b>	<b>27,225</b>
Stocks		8,573	20,625	9,264	10,190	11,719
Debtors		2	390	401	7,000	9,000
Cash		87,646	4,230	222	6,798	6,006
Other		7,102	10,734	284	300	500
<b>Current Liabilities</b>		<b>(3,630)</b>	<b>(8,562)</b>	<b>(7,537)</b>	<b>(7,000)</b>	<b>(9,500)</b>
Creditors		(3,567)	(7,716)	(6,665)	(7,000)	(9,500)
Short term borrowings		(63)	(846)	(872)	0	0
<b>Long Term Liabilities</b>		<b>(125)</b>	<b>(156)</b>	<b>(350)</b>	<b>(280)</b>	<b>(280)</b>
Long term borrowings		(125)	(156)	(66)	0	0
Other long term liabilities		0	0	(284)	(280)	(280)
<b>Net Assets</b>		<b>113,083</b>	<b>76,090</b>	<b>42,830</b>	<b>52,054</b>	<b>48,491</b>
<b>CASH FLOW</b>						
<b>Operating Cash Flow</b>		<b>(16,178)</b>	<b>(68,318)</b>	<b>(9,622)</b>	<b>(6,636)</b>	<b>2,208</b>
Net Interest		589	1,528	(913)	150	0
Tax		0	0	0	0	0
Capex		(14,505)	(40,041)	(967)	(1,000)	(3,000)
Acquisitions/disposals		0	(465)	266	0	0
Financing		117,552	23,066	7,292	15,000	0
Dividends		0	0	0	0	0
Net Cash Flow		87,458	(84,230)	(3,944)	7,514	(792)
<b>Opening net debt/(cash)</b>		<b>0</b>	<b>(87,458)</b>	<b>(3,228)</b>	<b>716</b>	<b>(6,798)</b>
HP finance leases initiated		0	0	0	0	0
Other		0	0	0	0	0
<b>Closing net debt/(cash)</b>		<b>(87,458)</b>	<b>(3,228)</b>	<b>716</b>	<b>(6,798)</b>	<b>(6,006)</b>

Source: Edison Investment Research, Landkom accounts

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