Equity Research Report

Dangote Sugar Refinery Plc

Positioned for Growth

May 10, 2016

Executive Summary

- DangSugar performance improved in Q1 2016. This is attributed to the higher sales volume and higher price during the period
- The company progressively increased its selling prices in HY1 2015 to offset the increase in cost of sales brought about by currency devaluation and gas shortages
- The company plans to expand the retail sugar market share to 5% in the next three years
- DangSugar is also partnering with sugar cube manufacturers to supply its sugar to the 100,000 tonnes p.a. market
- The company continues to improve on its efficiency by redeveloping its sequencing strategy towards self-sufficiency in the production of refined sugar from cane
- The company has taken advantage of the import substitution strategy of the Federal Government of Nigeria to ensure self-sufficiency in sugar production
- We estimate a dividend per share of N0.59 for the FY 2016
- Our fair value of the shares of Dangote Sugar Refinery is **N9.70**
- We place a **BUY** on the shares at the current price of N5.85 per share

1.0 Q1 2016 Performance Analysis:

Table 1:	
Rating	BUY
Current Price	N5.85
Fair Value	N9.70
Price Target	N8.50
Horizon	One year

The improvement in the T/O can be attributed to the higher sales volume and higher prices during the period.

The unaudited Q1 2016 result of DangSugar for the period ended March 31, 2016 shows that its Turnover (T/O) increased by 44.82% to N32.62bn, compared with N22.52bn recorded in the corresponding period of 2015. The improvement in the T/O can be attributed to the higher sales volume and higher prices during the period. The price at which it sells its refined sugar to customers increased by 21.8% per 50kg to an average of N7,574, compared with N6,218 in Q1 20115. The Gross Profit increased by 22.62% to N6.77bn in Q1 2016, with cost of sales impacted by increased import tariffs, higher freight expenses and production costs mainly driven by increased Low Pour Fuel Oil (LPFO) use. **The distribution and administrative expenses as a percentage of T/O decreased from 7.55% in 2015 to 4.67% in 2016. This was because of the decreases in personnel cost and management fee**.

The other income decreased by 93.08% to N93.07mn in 2016 from N1.34bn in 2015. The Earnings Before Interest and Tax (EBIT) increased to N5.33bn in 2016, an increase of 3.49% from N5.15bn in 2015. The company recorded a finance cost of N146.36mn in 2016, from N664.89mn in 2015. The Profit Before Tax (PBT) stood at N5.11bn in 2016, an increase of 34.62% from N3.80bn recorded in the corresponding period of 2015. The tax provision increased by 24.59% to N1.77bn from N1.42bn in 2014. The Profit After Tax (PAT) stood at N3.34bn in 2016 from N2.37bn recorded in the corresponding period of 2015, representing an increase of 40.63%.

The company's profit margins dropped in Q1 2016 compared with Q1 2015.

The company's profit margins dropped in Q1 2016 compared with Q1 2015. The Operating Profit Margin decreased in 2016 to 16.09% from 16.96% in 2015. The PBT margin also decreased to 15.68% in 2016 from 16.86% in 2015. The PAT margin decreased to 10.24% in 2016, down from 10.54% in 2015.

The result also indicates that the percentage of T/O, PBT, and PAT in the Q1 2016 to the Audited T/O, PBT and PAT for the period ended December 2015 are: 32.28%, 30.90% and 28.94%, respectively.

Table 2: Quarterly Performance (N'bn)					
	Q1 2016	Q4 2015	Q3 2015	Q2 2015	Q1 2015
Turnover	32.62	28.01	21.93	28.60	22.52
PBT	5.11	2.32	4.42	6.00	3.80
PAT	3.34	2.20	3.02	3.94	2.37
Source: Company Annual Account					

A cursory look at the balance sheet position as at Q1 2016 compared with the position as at FY 2015 shows a marginal decrease in the company's fixed assets. The total fixed assets decreased by 0.78% to N58.99bn in Q1 2016 from N59.46bn in FY 2015. The stock decreased by 22.58% to N12.04bn in Q1 2016 from N15.55bn in FY 2015. The cash and bank balances recorded an increase by 97.26% from N8.99bn in FY 2015, to N17.74bn in Q1 2016. The trade debtors and other receivables increased in Q1 2016 by 13.23% to N16.65bn from N14.70bn in the FY 2015, while trade creditors and other payables decreased by 3.30% to N27.17bn from N28.09bn as at FY 2015. Working capital stood at N7.64bn in Q1 2015, while net assets for the period increased by 5.74% to stand at N61.49bn from N58.15bn in the FY 2015.

The trade receivables and prepayments increased in 2016 by 13.23% to N16.65bn from N14.70bn in Q1 2015 period.

The total assets of the company which stood at N108.25bn as at Q1 2016 were financed by a mix of equities and liabilities in the ratio of 56.80% and 43.20% respectively. Our analysis of the liabilities shows that the short-term liabilities stood at N41.61bn, accounting for 88.99% of the total liabilities, while the long-term liabilities which constituted solely of deferred taxation stood at N5.15bn, accounting for 11.01% of the total liabilities. The short term liabilities constituted mainly of Trade and other payables and short term borrowings.

Table 3: DangSugar Sugar Sale – Metric Tonne			
	2015	2014	Change (%)
Refined Sugar Produced	762,710	838,993	9.09%
Refined Sugar Sold	782,120	781,324	0.10%
	Q1 2016	Q1 2015	
Refined Sugar Produced	195,591	185,015	5.72%
Refined Sugar Sold	211,793	171,924	23.19%
Source: Company Press Release, FSDH Research Analysis			

2.0 FY 2015 Performance Analysis:

The turnover in FY 2015 increased by 6.54% to N101.06bn.

The audited Full Year 2015 (FY 2015) result of Dangote Sugar Refinery Plc (DangSugar) for the period ended December 31, 2015 shows that its Turnover (T/O) increased to N101.06bn, from N94.86bn in 2014. This represents an increase of 6.54%. The average price increase in the period and the subsequent increased market share from the price cut on its products led to the increase in the T/O. The company progressively increased selling prices in HY1 2015 to offset the increase in cost of sales brought about by currency devaluation and gas shortages. In September 2015, DangSugar reduced the price of its 50kg sugar by 28.13% to N5,750, from N8,000. The price reduction was aimed at protecting its market share and discouraging sugar smugglers. The trade receivables decreased by 7.25% in FY 2015. This indicates that the company recorded improved cash sale in 2015, compared with 2014. The geographic segments performance indicates that Lagos contributed 44.25% (N44.71bn); North contributed 38.83% (N39.24bn), West 11.94% (N12.06bn), and East 4.99% (N5.04bn). The cost of sales increased by 5.38% to N80.33bn from N76.23bn recorded in 2014. The cost of sales increased at a lower rate than the increase in the T/O, leading to improvement in the gross profit margin. The devaluation of the currency offset some of the benefits of a drop in the price of raw sugar. The distribution and administrative expenses as a percentage of T/O decreased from 8.77% in 2014 to 6.14% in 2015. This was because of the decrease in personnel cost and, selling and distribution costs.

Other Operating Income decreased significantly to stand at N1.33bn as at 2015, representing a decrease of 59.43% compared with N3.29bn recorded in 2014. The major contributor to the decline in Other Operating Income was Miscellaneous Income, which decreased by 51.80% to N962.59mn in 2015, from N2bn in 2014. There was also no Insurance Claims in 2015, compared with N1.27bn recorded in 2014.

The PBT stood at N16.55bn in 2015, an increase of 8.35% from N15.27bn recorded in the corresponding period of 2014.

The Earnings Before Interest and Tax (EBIT) increased to N15.85bn in 2015, an increase of 16.63% from N13.59bn in 2014. The increase in T/O in the face of a drop in the operating expenses led to the growth in the EBIT. The company recorded a net finance cost of N653.01mn in 2015, from net finance income of N179.51mn in 2014. The 2015 Miscellaneous Income include provisions no longer required, electricity issued to sister companies and rental income from sister companies. The Profit Before Tax (PBT) stood at N16.55bn in 2015, an increase of 8.35% from N15.27bn recorded in the corresponding period of 2014. The tax provision recorded an increase of 37.83% to N5.01bn from N3.64bn in 2014. The Profit After Tax (PAT) stood at N11.54bn in 2015 from N11.64bn recorded in the corresponding period of 2014, representing a marginal decrease of 0.87%.

Table 4: Financial Performance (N'bn)

	FY 2015	FY 2014	Change
T/O	101.06	94.86	6.54%
EBIT	15.85	13.59	16.63%
PBT	16.55	15.27	8.35%
PAT	11.54	11.64	(0.87%)

Source: Company Annual Accounts and FSDH Research Analysis

Table 5: Quarterly Result Highlights (N'bn)

	Q4 2015	Q3 2015	Q2 2015	Q1 2015	Q4 2014	Q3 2014
Turnover	28.01	21.93	28.60	22.52	21.06	24.20
PBT	2.32	4.42	6.00	3.80	1.30	3.71
PAT	2.20	3.02	3.94	2.37	2.49	2.31

Source: Company Annual Accounts and FSDH Research Analysis

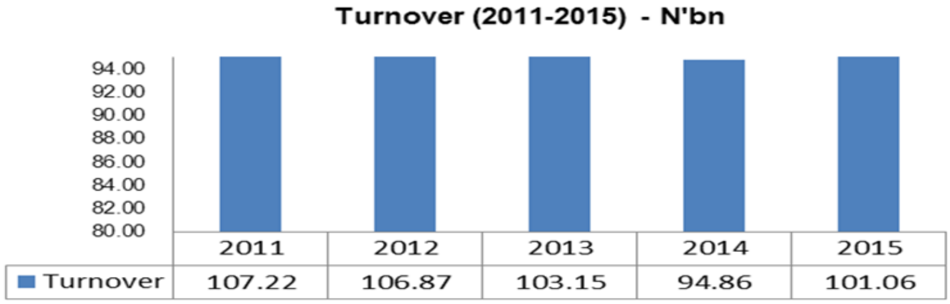
The company's profit margins improved in 2015, compared with 2014 except the PAT Margin.

The company's profit margins improved in 2015, compared with 2014 except the PAT Margin. This is a reflection of the impact of the decrease in operating cost/expenses and the increased tax provision in 2015. The Gross Profit Margin increased to 20.51% in 2015 from 19.64% in 2014. The EBIT Margin increased to 15.69% from 14.33%. The PBT Margin in 2015 increased marginally over the 2014 figure. The PBT margin increased to 16.38% in 2015 from 16.10% in 2014. There was a decrease in the PAT margin in 2015 due to the 37.83% increase in tax. The PAT Margin decreased to 11.43% in 2015, down from 12.28% in 2014.

Table 6: Profitability Margins

	FY 2015	FY 2014	FY 2013
GP* Margin	20.51%	19.64%	23.85%
EBIT Margin	15.69%	14.33%	14.39%
PBT Margin	16.38%	16.10%	15.77%
PAT Margin	11.43%	12.28%	10.64%

*Source: Company Annual Accounts and FSDH Research Analysis; *GP – Gross Profit*

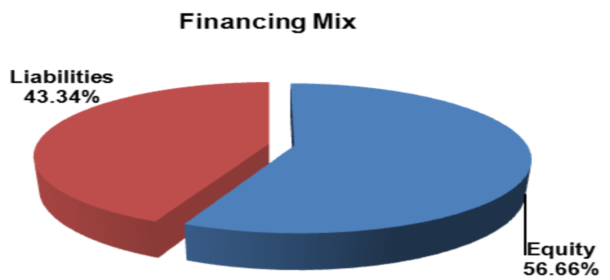


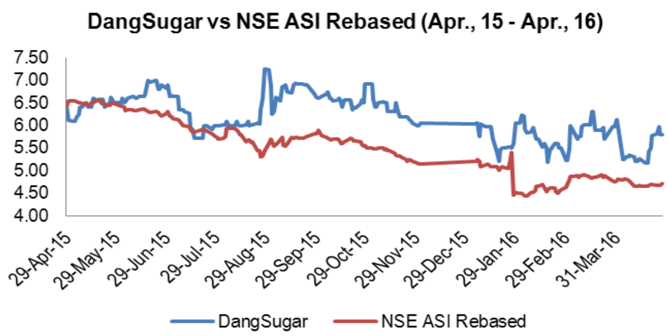
The trade debtors decreased in 2015 by 7.25% to N6.34bn from N6.84bn in the FY 2014 period.

A cursory look at the balance sheet position as at FY 2015 compared with the position as at FY 2014 shows an increase in the company's fixed assets. The total fixed assets increased by 9.02% to N59.46bn from N54.54bn in FY 2014. The growth was as a result of the increase of N4.33bn in Property, Plant and Equipment, and the N430mn increase in Biological Assets. The stock increased to N15.55bn from N15.10bn in FY 2014. The cash and bank balances recorded an increase of 44.99% from N6.20bn in FY 2014 to N8.99bn in 2015. The trade debtors decreased in 2015 by 7.25% to N6.34bn from N6.84bn in the FY 2014 period. The trade creditors also decreased by 27.08% to N16.46bn from N22.57bn as at FY 2014. The working capital stood at N2.98bn, up from N622.95mn recorded in FY 2014, while net assets for the period increased by 13.10% to stand at N58.15bn from N51.41bn as at FY 2014.

The total assets of the company which stood at N102.62bn as at FY 2015 were financed by a mix of equities and liabilities in the ratio of 43.34% and 56.66% respectively.

The total assets of the company which stood at N102.62bn as at FY 2015 were financed by a mix of equities and liabilities in the ratio of 56.66% and 43.34% respectively. Our analysis of the liabilities shows that the short-term liabilities stood at N39.33bn, accounting for 88.42% of the total liabilities, while the long-term liabilities stood at N5.15bn, accounting for 11.58% of the total liabilities. **DangSugar received a loan of N2.5bn from a related party, Dangote Industries Limited for Short Term Working Capital purpose over a period of 90 days.** This is renewable at an interest rate of 13.5%. The loan is not secured by the assets of the company.





3.0 Analysis of the Statement of Cash Flows:

DangSugar generated a net cash flow of N2.79bn in 2015, an improvement over the net cash flow of N2.25bn used up in 2014. The cash generated from operation were mainly responsible for the net cash flow for the year. The cash profit generated from the core operation stood at N21.64bn in 2015 from N20.12bn in 2014. The ratio of the cash generated from core operation to the revenue increased to 21.41% in FY 2015 from 21.21% in 2014. This means that more of its revenue translated into cash in 2015 than in 2014. This is good for the company and it helped to reduce the incidence of bad debt.

The cash generated from operating activities increased from N20.12bn in 2014 to N21.64bn in 2015 while the net cash generated after tax increased from N15.50bn to N15.63bn.

The cash generated from operating activities increased from N20.12bn in 2014 to N21.64bn in 2015 while the net cash generated after tax increased from N15.50bn to N15.63bn. The net cash generated from the operating activities was sufficient to cover the investment need in property, plant and equipment of the company. It was also sufficient to cover dividend payment and interest expenses. However, the payment could barely meet up the investment need in capital expenditure, interest payments and dividend payment. DangSugar borrowed N2.5bn to shore up its cash flow during the period to cover the internally generated cash.

Table 7: Cash Flow Analysis – N'bn	2015	2014
Cash Profit from Core Operating Activities	21.64	20.12
Changes in Working Capital	2.27	3.61
Cash from Operating Activities	20.98	20.01
Income Tax Paid	(5.35)	(4.52)
Net Cash From Operating Activities	15.63	15.50
Net Cash Used In Investing Activities	(8.16)	(12.01)
Net Cash Used in Financing Activities	(4.69)	(5.74)
Cash Generated for the Year	2.79	(2.25)
Ratio of Cash Profit from Core Operating Activities to Revenue	21.41%	21.21%
Ratio of Net Cash from Operating Activities to PPE	188.27%	126.84%

Source: Company Annual Account – 2015 and FSDH Research Analysis

4.0 Drivers of Performance:

DangSugar performance in 2015 was buoyed by its improved operational efficiency.

DangSugar performance in 2015 was buoyed by its improved operational efficiency. The company increased its average price of sugar in 2015 compared with 2014. The company recorded a volume pick up in Q4 2015 as it deliberately reduced its margins by 28% to wade off competition and stop the activities of smugglers. The company also added 100 trucks to its fleet for improved delivery of its products to customers. The management of the company also highlighted that a combination of lower production and higher unit costs resulted in an increase in to conversion costs in 2015. However, the effect of lower raw sugar costs offset some of these higher costs.

The company's production was constrained in the first nine months of 2015. The heavy traffic jams at the Apapa area where its refinery is located, restricted movement of its delivery trucks. However, there was improvement in Q4 2015 because of the efforts of the Lagos State Government at easing traffic in the area. The collapsed bridge at its Northern distribution channel has also been rebuilt, which has improved delivery time of its products in the North.

5.0 Strategic Focus:

DangSugar's strategy is to become a global force in sugar production.

DangSugar's strategy is to become a global force in sugar production. It is working within the Nigeria's National Sugar Master Plan to end importation and produce 1.5 million metric tonnes of sugar from cane to sell in Nigeria and neighbouring countries. As part of this plan it acquired Savannah Sugar Company in Adamawa State in December 2012 and is currently improving its farm acreage and upgrading the factory. It also intends to augment Savannah's 32,000 hectares in Adamawa state by acquiring and planting a further 150,000 hectares across Nigeria, supporting the new plantations with modern production facilities that are located closer to the consumer. DangSugar has also began the construction of a 1-tonne bagging facility at the refinery to enhance bulk deliveries to our corporate customers, which will reduce costs and improve revenue.

DangSugar continues to improve on its efficiency by redeveloping its sequencing strategy towards self-sufficiency in the production of refined sugar from cane. The company has indicated that it remains committed to executing its "Sugar for Nigeria" project, which will replace the current production at its plants in the next four to five years. The first phase of its backward integration plans is ongoing, which now includes the Savannah rehabilitation, Guyuk and Zaria projects. The Group's retail business (250g, 500g and 1kg packages) continues to grow (up 62% at N1.99bn in 2015 compared with N1.23bn in 2014), representing 2% of the Group's total refined sugar sales.

There is a plan to expand the retail sugar market share to 5% in the next three years.

There is a plan to expand the retail sugar market share to 5% in the next three years. DangSug is also partnering with sugar cube manufacturers to supply its sugar to the 100,000 tonnes p.a. market. The overriding objective is to serve the growing market via its packaged sugar product range as the Nigerian consumer becomes more sophisticated in their shopping habits. DangSug opines that hygiene has become a major concern among consumers, with preference for packaged sugar sold in supermarkets to "scoop and tie" products largely sold in the open markets.

6.0 Business:

DangSugar is currently the market leader in the domestic sugar market in Nigeria.

DangSugar is currently the market leader in the domestic sugar market in Nigeria. It is however faced with increasing competition in recent times. DangSugar's core competences comprises of three key areas:

- Refining of raw sugar to make vitamin A fortified and non-fortified white sugar.
- Marketing and distribution of Dangote Vitamin A fortified refined white sugar packaged in 50kg, 1kg, 500g and 250grams.
- Cultivation and milling of sugarcane to finished sugar from SSCL.

In addition to these core competences DangSugar provides key value added support services for its customer's advice including logistics, supply-chain management, credit and risk, sales and merchandising.

The company provides its core competencies from the Dangote Sugar Apapa refinery and gets some of its raw materials from SSCL. The Apapa refinery is located at Apapa Wharf in Lagos, with a dedicated jetty that berths large shipments of raw sugar from Brazil. The facility was commissioned in 2000, with an initial refining capacity of 600,000MTPA. Over the years, the facility has undergone two major upgrades that have turned it into one of the largest sugar refineries in the world with 1.44MTPA refining capacity. Over 2013-14, the facility benefited from further upgrades that now enable it to achieve more efficient sugar yields. The Apapa refinery is supported by warehouses located strategically across the country and served by over 400 trucks.

DangSugar acquired 95% of SSCL in December 2012 as part of its backward integration initiative.

DangSugar acquired 95% of SSCL in December 2012 as part of its backward integration initiative. SSCL is a cane sugar production operation located on 32,000 hectares of land in Numan, Adamawa State, Nigeria, with a milling capacity of 50,000 tonnes of sugar per annum. At present, however, SSCL produces refined sugar from just 6,750 hectares of sugar cane cultivated on its sugarcane fields. As part of DangSugar's growth strategy, SSCL is undergoing rehabilitation and expansion so that more of its land can be planted and harvested effectively. The expansion of SSCL will increase sugar milling capacity to 260,000 tonnes of sugar per annum on approximately 25,000 hectares of cultivated land. DangSugar's growth strategy will also see the development of new independent sugar sites similar to the Savannah model in Taraba, Jigawa, Kebbi and Kwara/Kogi.

As at the December 31, 2014 Dangote Industries limited had a majority shareholding in Dangote Sugar of approximately 67.66% with 8,119,200 ordinary shares. Aliko Dangote also had a substantial shareholding of 5.44% with 653,095,014 ordinary shares.

Table 8: Directors' Shareholding as at December 31, 2014*

Director	Position	Holdings
Alhaji Aliko Dangote	Chairman	653,095,014
Mr Graham Clark (Australian)	MD/CEO	Nil
Engr.Abdullahi Sule	Non-Executive	1,547,987
Alhaji Sani Dangote	Non-Executive	Nil
Mr. Olakunle Alake	Non-Executive	6,864,000
Ms. Bennedikter Molokwu	Non-Executive	1,483,400
Dr. Koyinsola Ajayi (SAN)	Director	Nil
Mr. Uzoma Nwankwo	Director	384,692
Alhaji Abdu Dantata	Director	1,044,000
Mrs Maryam Bashir	Director	Nil

Source: Company Annual Accounts; *As at December 31, 2014

Table 9: Shareholding Structure as at December 31, 2014*

Name	No. Of Ordinary Shares	% of Shareholding
Alhaji Aliko Dangote	653,095,014	5.44%
Dangote Industries Limited	8,119,200,000	67.66%
Nigerian Public	3,227,704,986	26.90%
Total Number of Shares	12,000,000,000	100.00%

Source: Company Annual Accounts; *As at December 31, 2014

Table 10: Company Summary

Ticker	DangSugar
Sector	Consumer Goods
Sub-sector	Food Products
Date of Incorporation	January 04, 2005
Date of Listing	March 18, 2007
Financial Year End	December
Number of Fully Paid Share	12,000,000,000
Current Capitalization(NGN)	70,200,000,000
NSE Capitalization (NGN)	8,821,941,167,825
% of NSE Capitalisation	0.80%
52 Week high NGN	7.26
52 Week low NGN	5.17
YTD Return (%)	4.48
52 Weeks Average Volume Traded	1,467,757
Trailing EPS NGN	1.04
Trailing P/E Ratio (X)	5.62

As at May 10, 2016
Source: Company Annual Account – 2015 and FSDH Research Analysis

7.0 Product Analysis:

Dangote Sugar refines raw sugar and sells it in two grades: Vitamin A fortified sugar and Unfortified Industrial sugar.

Dangote Sugar refines raw sugar and sells it in two grades: Vitamin A fortified sugar and Unfortified Industrial sugar. The Vitamin A fortified sugar is an all-purpose white sugar ideally used for baking and sweetening of beverages. The Dangote unfortified sugar is a specially processed sugar grade used by manufacturing companies. The refined grades are sold in 50kg, 1kg, 500g and 250g packages under the brand name Dangote Sugar.

Competitors in this market include BUA Sugar refinery and Flour Mills of Nigeria (FMN). FMN products in the market include Golden Penny Premium white granulated sugar, Golden Penny Premium White Granulated Sugar, BTB sugar for beverage manufacturers, BTB sugar fortified with vitamin A for bakers, biscuit manufacturers and confectioners and Golden Penny Premium white sugar cubes.

As part of its effort to develop the local capacity in sugar refining in Nigeria, the FGN has banned the importation of refined sugar into Nigeria.

In addition to refining sugar, DangSugar provides key value added support services for its customers including logistics, supply-chain management, credit and risk advice, sales and merchandising. **As part of its effort to develop the local capacity in sugar refining in Nigeria, the FGN has banned the importation of refined sugar into Nigeria.**

8.0 Customer Analysis:

DangSugar sells unfortified sugar mainly to pharmaceutical, food and beverage manufacturers, while Vitamin A-fortified sugar is sold to distributors who sell to small wholesalers, confectioners and other smaller value-adding enterprises who provide the distribution network to the Nigerian retail market. The company sells a small amount of sugar directly to retail customers. Sales to distributors account for 70% of the company's revenue while sales to blue chip companies that buy unfortified sugar exclusively accounts for 30% of the company’s revenue. There is also a single customer who buys industrial unfortified sugar that represents more than 10% of total sales.

Both the Nigerian retail market and the bigger blue chip companies have been hit by the fall in disposable income and the declining purchasing power in the economy.

The devaluation of the Naira has also affected most of the blue chip companies, resulting in rising finance and operating costs. These factors affecting key customers resulted in the slowdown in sales for DangSugar. In HY 2015, the quantity of refined sugar sold fell by 12.6% to 367,026 metric tonnes from 420,862 metric tonnes. The factors mentioned above are responsible for this development.

9.0 Analysis of Revenue and Profitability by Geographical Region:

As at FY 2015, DangSugar made 44.25% of its revenue from Lagos with revenue totalling N44.71bn, representing the biggest contribution to revenue during the period.

As at FY 2015, DangSugar made 44.25% of its revenue from Lagos with revenue totalling N44.71bn, representing the biggest contribution to revenue during the period. Followed by the Northern Region where revenue stood at N39.24bn, representing 38.83% of total revenue for the period. The western and eastern regions contributed 11.93% and 4.99% respectively to total revenue in FY 2015.

In a similar vein, DangSugar made 49.20% (N10.20bn) of its Gross Profit (GP) in Lagos, representing the biggest contribution to gross profit during the period. Followed by the Northern Region of Nigeria where GP stood at N6.63bn, representing 31.98% of the total GP for the period. The western and eastern regions contributed 13.27% and 5.55% respectively to total GP in FY 2015.

Given the large contribution the North makes to the company's revenue and profit, the continued insurgency in the North East of Nigeria presents a threat to the company's revenue. Thus the successful resolution of the crisis will positively affect the performance of the company going forward.

Table 11: Composition of Total Revenue and Profit – FY 2015 (N'bn)

Region	Revenue	Contribution to Total Revenue	Gross Profit	Contribution to Total Gross Profit
Lagos	44.71	44.25%	10.20	49.20%
North	39.24	38.83%	6.63	31.98%
West	12.06	11.93%	2.75	13.27%
East	5.04	4.99%	1.15	5.55%
Total		**100.00%**		**100.00%**

Company Annual Account and FSDH Research Analysis

10.0 SWOT Analysis:

10.1 Strengths:	10.2 Weaknesses:
❖ Upgrade of facilities and compliance with international standards on safety ❖ Largest refinery in Sub-Saharan Africa ❖ Strong brand name ❖ Technical and financial relationship with parent company ❖ Securing raw materials via backward integration. ❖ Consistent dividend payment ❖ Growth strategy to capitalize on the Government's "Nigerian Sugar Master Plan" project ❖ Leader in the industry	❖ Key-man risk ❖ Declining profit margin
10.3 Opportunities:	**10.4 Threats:**
❖ Large market size in Nigeria and neighbouring countries ❖ The CBN efforts to improve funding to the agriculture sector ❖ Government policy which bans the importation of processed sugar ❖ Expected growth in the global sugar consumption ❖ The Federal Government of Nigeria's support of the sugar industry as demonstrated by the Sugar Master Plan	❖ Foreign exchange rate instability ❖ Weak consumer income and spending ❖ Shortage of gas supply ❖ High cost of LPFO fuel ❖ Insurgency in the North East of Nigeria ❖ Patronage of cheaper and unlicensed sugar in the market.

11.0 Forecast:

Our Forecast Drivers

We considered the following factors in arriving at our five year forecasts:

Positive Factors:

- The competitive position of the company in the industry
- The Federal Government of Nigeria's ban on the importation of processed sugar
- The expansion strategies of the company
- The expected growth in global sugar consumption
- Large refining capacity
- Its backward integration strategy.

Negative Factors:

- Foreign exchange instability
- The weak consumer income and spending power
- Insurgency in the North East of Nigeria
- High cost of Low Pour Fuel Oil (LPFO)
- Activities of some smugglers in the industry.

We estimate a dividend per share of N0.59 for FY 2016.

We are of the opinion that the impact of the positive factors would be higher on both the revenue and the profitability of the company than the negative factors. We therefore estimate a Turnover of N135.86bn, N163.03bn, N187.48bn, N215.23bn and N245.34bn for the periods ending December 2016, 2017, 2018, 2019 and 2020. We estimate EBIT of N23.25bn, N29.86bn, N36.59bn, N46.31bn and N65.06bn. We estimate EBITDA of N24.27bn, N31.16bn, N38.27bn, N48.48bn and N67.89bn for the same period using EBIT margins of 17.12%, 18.32%, 19.52%, 21.52% and 26.52% respectively. Our PBT forecasts for the periods are: N24.77bn, N32.50bn, N40.18bn, N51.16bn and N71.85bn. Adjusting for tax, our PAT forecasts are N17.17bn, N22.52bn, N27.84bn, N35.45bn and N49.79bn. PAT margin for the period are 12.64%, 13.82%, 14.85%, 16.47% and 20.29%. Our forecast final dividend for the FY 2016 is N0.59 per share.

Table 12: Income Forecast (2016-2020)						
N'bn	Dec-15A	Dec-16F	Dec-17F	Dec-18F	Dec-19F	Dec-20F
Turnover (Net Sales)	101.06	135.86	163.03	187.48	215.23	245.34
Cost of Sales	(80.33)	(109.94)	(130.30)	(147.97)	(165.57)	(178.91)
Gross Profit	20.73	25.91	32.73	39.51	49.66	66.43
Admin, Selling & Distribution Expenses	6.21	(5.87)	(6.72)	(7.36)	(8.44)	(7.17)
Depreciation	(0.58)	(1.02)	(1.30)	(1.67)	(2.17)	(2.83)
Other Operating Income	1.33	3.21	3.86	4.44	5.09	5.80
EBIT	15.85	23.25	29.86	36.59	46.31	65.06
EBITDA	16.43	24.27	31.16	38.27	48.48	67.89
Net Finance Cost	(0.65)	1.52	2.64	3.59	4.84	6.79
PBT	16.55	24.77	32.50	40.18	51.16	71.85
Taxation	(5.01)	(7.61)	(9.98)	(12.34)	(15.71)	(22.06)
PAT	11.54	17.17	22.52	27.84	35.45	49.79

Source: Company Annual Account – 2015 and FSDH Research Analysis

Table 13: Ratio Analysis (2015 - 2020)						
	Dec-15A	Dec-16F	Dec-17F	Dec-18F	Dec-19F	Dec-20F
EBITDA Margin	16.26%	17.87%	19.12%	20.41%	22.53%	27.67%
EBIT Margin	15.69%	17.12%	18.32%	19.52%	21.52%	26.52%
PBT Margin	16.38%	18.23%	19.94%	21.43%	23.77%	29.28%
PAT Margin	11.41%	12.64%	13.82%	14.85%	16.47%	20.29%
EPS(N)	0.96	1.43	1.88	2.32	2.95	4.15
DPS(N)	0.50	0.59	0.78	0.96	1.22	1.72
Dividend Payout	41.61%	41.43%	41.43%	41.43%	41.43%	41.43%
Earnings Yield *	15.94%	14.75%	19.35%	23.92%	30.46%	42.78%
Dividend Yield *	8.29%	6.11%	8.02%	9.91%	12.62%	17.72%
P/E Ratio*	6.27	6.78	5.17	4.18	3.28	2.34
Number of Shares ('bn)	12.00	12.00	12.00	12.00	12.00	12.00
ROCE	25.04%	30.16%	31.59%	31.82%	32.67%	35.70%
ROE	19.84%	24.36%	26.25%	26.71%	27.68%	30.54%
Collection Days	23	21	21	21	21	21
Payment Days	75	85	85	85	85	85
Inventory Turnover (x)	5.17	6.11	6.11	6.11	6.11	6.11
Asset Turnover (x)	0.98	1.00	1.01	1.00	0.97	0.90
Current Ratio (x)	1.10	1.31	1.51	1.72	1.97	2.28
Quick Ratio (x)	0.70	1.00	1.19	1.39	1.63	1.96
Debt Ratio (Total Liabilities /Total Assets)	0.43	0.48	0.47	0.45	0.42	0.40

At Our Fair Value of N9.70
Source: Company Annual Account – 2015 and FSDH Research Analysis

Table 14: Statement of Financial Position Forecast (2016 - 2020)						
N'bn	**Dec-15A**	**Dec-16F**	**Dec-17F**	**Dec-18F**	**Dec-19F**	**Dec-20F**
Property, Plant and Equipment	54.80	54.17	56.09	57.91	59.69	61.45
Biological Assets	1.69	1.69	1.69	1.69	1.69	1.69
Deferred Tax Assets	2.97	2.97	2.97	2.97	2.97	2.97
Long Term Assets	**59.46**	**58.83**	**60.74**	**62.57**	**64.35**	**66.10**
Inventory	15.55	17.99	21.32	24.21	27.09	29.27
Trade receivables	6.34	7.69	9.23	10.62	12.19	13.90
Prepayments & Other Receivables	8.08	12.15	14.58	16.77	19.25	21.95
Other Assets	4.20	2.16	2.16	2.16	2.16	6.06
Cash and Bank Balances	8.99	37.12	52.86	71.73	96.88	135.79
Current Assets	**43.17**	**77.12**	**100.15**	**125.49**	**157.58**	**206.97**
Total Assets	**102.62**	**135.94**	**160.90**	**188.06**	**221.92**	**273.07**
Trade Payables	16.46	25.64	30.38	34.50	38.61	41.72
Employee Benefits	1.08	1.78	2.34	2.89	3.69	5.18
Accurals and Sundry creditors	1.75	12.11	14.53	16.71	19.18	21.86
Taxation	5.54	7.61	9.98	12.34	15.71	22.06
Other Liabilities	11.99	11.71	9.14	6.61	2.98	-
Borrowings	2.50	-	-	-	-	-
Current Liabilities	**39.33**	**58.84**	**66.38**	**73.06**	**80.16**	**90.82**
Working Capital/ Net Current Asset	**3.84**	**18.27**	**33.77**	**52.43**	**77.41**	**116.15**
Capital Employed	**63.30**	**77.10**	**94.52**	**115.00**	**141.76**	**182.25**
Deferred Taxation	5.15	6.64	8.71	10.77	13.71	19.26
Long Term Liabilities	**5.15**	**6.64**	**8.71**	**10.77**	**13.71**	**19.26**
Total Liabilities	**44.48**	**65.48**	**75.09**	**83.83**	**93.88**	**110.08**
Total Net Assets	**58.15**	**70.46**	**85.81**	**104.24**	**128.05**	**162.99**
Paid Up Share Capital	6.00	6.00	6.00	6.00	6.00	6.00
Share Premium	6.32	6.32	6.32	6.32	6.32	6.32
Revenue Reserve	46.08	58.45	73.86	92.37	116.28	151.38
Total Reserves	**52.40**	**64.77**	**80.18**	**98.69**	**122.60**	**157.70**
Total Equity	**58.15**	**70.46**	**85.81**	**104.24**	**128.05**	**162.99**
Total Equity & Liability	**102.62**	**135.94**	**160.90**	**188.06**	**221.92**	**273.07**
Source: Company Annual Account – 2015 and FSDH Research Analysis						

12.0 Valuation

In arriving at a fair value for the ordinary shares of the company, we used the Discounted Free Cash Flow (DCF) model. We applied a terminal growth rate of 4.68%, which is the average growth rate for the real Gross Domestic Product (GDP) growth rate for the Nigerian economy in the last four years. We used a beta value of **0.73x** based on the 5-year daily historical returns on the company share price and the Nigerian Stock Exchange All Share Index (NSE ASI). We used the yield of **11.65%** as our risk free rate, and market premium of **11.15%**. Applying the foregoing parameters on the Capital Asset Pricing Model (**CAPM**), the cost of equity generates **19.84%**. Using 12bn shares in issue the DCF model generated **N9.70** per share, which is our fair value.

The fair value for Dangote Sugar Refinery is N9.70

The current market price of DangSugar shares is N5.85. The highest and the lowest closing price in the last 52 weeks are N7.26 and N5.17 respectively. The 2016 forward earnings yield and dividend yield based on our fair value are: 14.75% and 6.11% respectively. The capital appreciation for the stock of Dangote Sugar Refinery Plc shows an upward potential of 65.79%. This is higher than our minimum equity return benchmark of 16.65%. **We therefore place a BUY rating on the shares of Dangote Sugar Refinery Plc at the price of N5.85 as of May 10, 2016. Meanwhile, our target price for the shares of DangSugar in the next one year is N8.50**

12.1 Risks to Price Target:

The following risks may affect the attainment of our target price:

- Increase in the yield on fixed income securities
- Drop in market liquidity
- Issuance of new equity
- Reduction in dividend payment

Table 15 : Comparable Analysis (N'bn) - 2015		
Company	DangSugar	Flour Mills**
Turnover (Net Sales)	101.06	308.76
Gross Profit (GP)	20.73	35.37
EBIT	15.85	10.22
PBT	16.55	7.72
PAT	11.54	8.47
GP Margin	20.51%	11.45%
EBIT Margin	15.69%	3.31%
PBT Margin	16.38%	2.50%
PAT Margin	11.41%	2.74%
ROE	19.84%	9.69%
Net Assets	58.15	87.41
Net Assets Per Share (N)	4.85	33.31
PE Ratio	5.62	2.71
Earnings Yield*	17.81%	36.91%

**As at May 10,2015 **Flour Mills year end is in March 2015*
DangSugar is a mono-product while Flour Mills produces a variety of food products, inclusive of sugar.
Source: Company Annual Account – 2015 and FSDH Research Analysis

Table 16 : Analyst Rating	
Rating	Criteria
BUY	Fair value of the stock is ≥ 16.65%* compared with the current market price.
HOLD	Fair value of the stock ranges between -10% and 16.65% of the current market price.
SELL	Fair value of the stock is > 10% below the current market price.

16.65% is our estimated minimum equity return. It is the combination of our risk free rate and risk premium. Our risk free rate is the average yield on a five-year FGN Bond. We adopted a 5% risk premium and set the risk free rate every quarter.

Fair Value: This is the value of the ordinary shares of the company using the valuation method appropriate for the company. It is the intrinsic or true value of the stock based on the fundamentals of the company. The market price may either trade at a premium or discount to the intrinsic value.

Price Target: This is the price that we believe the shares of the company will trade within our time horizon. Other risk factors may affect the attainment of this price. This price may or not be different from the intrinsic value.

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