

DANGOTE SUGAR REFINERY (DSR)

Executive Summary

Dangote Sugar Refinery (DSR) started off as a sugar division within Dangote Industries Limited (DIL) in March 2000. The parent company, DIL had been involved in the sugar business since 1978 through the importation and trading of white sugar before commencing sugar refining in 2001. Since then, the company has helped to reduce the country's dependence on refined sugar importation. All the white sugar produced by the company is sold in Nigeria, but the products find its way to neighboring West African countries through informal cross-border trading. The company imports raw sugar from Brazil, refines it into Vitamin A fortified white sugar and sells across Nigeria. The factory has undergone two expansions that have increased installed capacity to about 1.44million metric tones from an initial installed capacity of 600,000 metric tones of raw sugar per annum. The factory's capacity utilization is currently above 75%, making DSR the largest sugar refinery in sub Saharan African and one of the largest in the world.

The company's operations comprise two key business areas which include: i) Refining Process; ii) Marketing & Distribution to a variety of customers which can be grouped into large industrial users (this group typically accounts for 18% of the company's sales) and the wholesale distributors, (this group accounts for about 82% of the company's sales).

The company intends to diversify into the upstream segment of the sugar business by acquiring and developing Savannah Sugar Company Limited (SSCL), a subsidiary of DIL, to create synergies and increase overall capacity. SSCL currently produces white sugar from own grown sugarcane. On successful combination, the potential synergies between DSR and its intended merger partner, SSCL, will see it become a formidable institution within the Sugar industry in Nigeria and beyond.

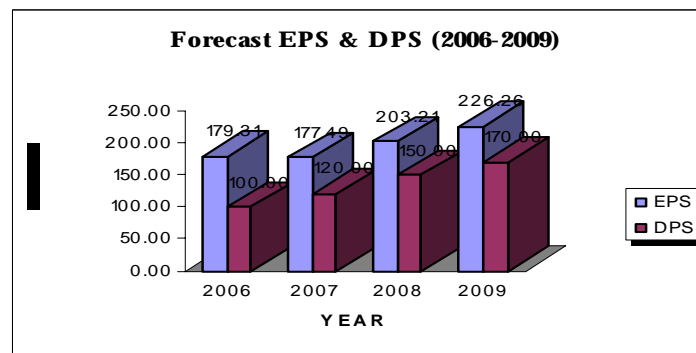
Board of Directors/Management

The Board of DSR is made up of 9 members comprising 2 Executive Directors and 7 Non-Executive Directors. Alhaji Aliko Dangote CON, is the Chairman of the Board. A graduate of Business Studies from Al-Azhar University, Cairo, Egypt (1977), he is an entrepreneur and the Founder/Chief Executive Officer of Dangote Group. He has bagged several awards in recognition of his contribution to the growth of the Nigerian economy. Other members of the Board include: Dr. Konyinsola Ajayi, Mr. Olakunle Alake, Alhaji Sani Dangote, Alhaji Abdu Garba Dantata, Ms Bennedikta China Molokwu, Mr Uzoma Nwankwo and Mr. Suleiman Oladapo Olarinde. The Management team is led by Mr. Narendra Kumar Somani as the Managing Director. Mr. Somani is an Indian national with over 30 years management experience in running conglomerates and multinational organizations. Prior to joining DSR, he was the Group Chief Executive Officer of the Churchgate Group from 2002 to 2005 having earlier served as the Group General Manager of the same company from 1980 to 1989.

AUTHORISED SHARE CAPITAL	N 6,000,000,000 divided into 12,000,000,000 Ordinary Shares of 50k each
ISSUED AND FULLY PAID	N5,000,000,000 divided into 10,000,000,000 Ordinary Shares of 50k per share
METHOD OF OFFER	Offer for Sale
OFFER SIZE	3,000,000,000 Ordinary Shares of 50k per share
UNITS OF SALES	A minimum of 500 units and multiple of 50 units thereafter
MARKET CAPITALISATION AT OFFER PRICE	N180,000,000,000
PREFERENTIAL ALLOTMENT	A maximum of 1,800,000,000 shares representing 60% of the Offer, will be preferentially allotted to identified investors
UNDERWRITING	The offer is fully underwritten by the Joint Underwriters on a stand-by basis
OFFER PRICE	N18.00
OFFER OPENS	November 15, 2006
OFFER CLOSES	December 22, 2006
LISTING OF SHARES ON NSE	March 19, 2007

Recommendation: BUY

Forecast Offer Statistics				
Year Ending	2006	2007	2008	2009
PBT (N'b)	17.93	23.67	27.09	30.17
PAT (N'b)	17.93	17.75	20.32	22.63
EPS (kobo)	179.31	177.49	203.21	226.26
EY* (%)	9.96	9.86	11.29	12.57
DPS* (kobo)	100	120	150	170
DY* (%)	5.56	6.67	8.33	9.44



Source: Offer Prospectus
* At Offer Price

Score Card

- DSR has perfected and patented its Vitamin A fortification technology to comply with the policy of NAFDAC, which is a requirement in Nigeria. None of the white sugar exporting countries has this requirement.
- DRS has the largest sugar refinery in Sub-Saharan African and one of the largest in the world.

Strengths & Opportunities

- Aggressive, experienced, dynamic and focused management team.
- Vitamin A fortification requirement by NAFDAC is supported by the United Nations and is a technology DSR has perfected and patented.
- Tariff protection by the Federal Government promotes white sugar production rather than importation.
- Technology driven and high quality customer service.

Threats & Weaknesses

- Declining Profitability Margin.
- Perception as a family owned business with 100% family ownership before the Offer and over 70% after the Offer. However, DSR has experienced and well tested professionals in charge of running the day to day affairs of the business.
- DSR is a mono-product company in an environment where the sugar consumption per capital is low (7kg/capital). However, DSR intends to leverage on the free-trade zone of ECOWAS to increase its market size.
- DSR may lose market share through the entry of competition into the market.

Shareholding Structure

Shareholders	Number	%
Dangote Industries Limited	9,900,000,000	99
Alhaji Aliko Dangote CON	100,000,000	1
Total	10,000,000,000	100

The financial information analyzed here is the segmented sugar division of Dangote Industries Limited (DIL) for the period of 2001-2005. Morrison Odede & Co and Akintola Williams Deloitte were the joint auditors for the years ended December 31 2004 and 2005 while Messrs Lanre Odede & Co were the auditors of the company for the years ended 31 December 2001, 2002 and 2003.

Analysis and Recommendation

DSR relied mainly on retained earnings to support its growth over the last five years. This strategy accounts for the non-payment of dividend within this period and has helped the company to maintain consistent growth. Consequently, total assets have grown from N7.7billion in 2001 to N44.49billion in 2005, translating to a Compound Annual Growth Rate (CAGR) of 55.09%.

The proportion of cost of sales and operating expenses to total sales increased marginally by 4.83% between 2004 and 2005. The increase was achieved mainly from the increase in the cost of sales which increased by 72.30% while the operating expenses increased by 12.27%.

A review of the profitability figures of DSR shows an impressive performance in the last five years. Turnover illustrates a CAGR of 41% while PAT shows a CAGR of 58.22%. In the immediate past two years, turnover increased by 59.93% from N36.58billion in 2004 to N58.49billion in 2005, gross profit however increased by 30.29% as a result of 72.30% increase in the cost of sales. Operating profit maintained an increase of 34.83% within the two years while profit before and after tax increased by 27.25% from N7.37billion in 2004 to N9.38billion in 2005. Return on total assets increased marginally by 0.65% from 20.43% in 2004 to 21.08% in 2005. Return on equity however declined by 2.07% from 29.09% in 2004 to 27.02% in 2005 while return on capital employed (ROCE) declined by 0.77% from 34.11% in 2004 to 33.34% in 2005.

DSR remained strong in term of its ability to meet its short term financing obligations. The current ratio which indicates the proportion of its current assets to current liabilities stood at 3.09 in 2005, an improvement over 2.00 in 2004, while the quick ratio increased to 2.77 in 2005 from 1.72 in 2004. In a similar development, the proportion of working capital to sales increased to 34.65% in 2005 from 29.28% in 2004.

A comparative analysis of DSR with selected companies in the Food/ Beverages & Tobacco sub sector (Nestle, Nigerian Bottling Company & Flourmills) shows that it is one of the leaders amongst its peers. It has the highest CAGR in Turnover, PAT, and EPS of 41%, 58.22%, 58.16% respectively between 2001 and 2005. DSR recorded the highest PBT and PAT as well as PAT margin amongst the selected companies.

Based on the last full year audited accounts of DSR (2005) and the Offer price of N18.00 per share using the adjusted EPS of N0.938 (on 10billion ordinary shares) the current PE ratio is 19.19x. This is lower than the industry average P/E ratio of 32.12x. Based on the forecast of DSR and our forecast for the selected companies (as shown in our table below), the PE ratio for DSR at the end of 2006 would be 10.04x (at the offer price), the lowest among the companies selected. Our computed fair value of DSR is N25.65 per share, which arrives at a forward PE ratio of 14.30x. DSR intends to pay a cash dividend of N1.00 per share for the financial year ended 31 December, 2006. It is not clear from the Offer document if new investors will qualify for this cash dividend. Discounting the dividend, we project a return of 42.50% from capital appreciation when the stock is listed on the floor of The Nigerian Stock Exchange. We are of the opinion that the Offer is issued at a discount and therefore recommend a **BUY** for the stock at the current price.

Profit & Loss Account as @ 31 st December, 2005 (N'b)						
	2005	2004	% Change	2003	2002	2001
Turnover (Net Sales)	58.49	36.58	59.93	27.88	13.54	14.81
Cost of Goods Sold	44.46	25.80	72.30	21.54	11.29	11.92
Gross Profit	14.04	10.77	30.29	6.34	2.25	2.89
Operating Expenses	2.43	2.17	12.27	0.74	0.50	0.58
Operating/Trading(Loss)/Profit	11.60	8.61	34.83	5.60	1.75	2.31
Other Income	0.35	56.01	(99.38)	25.47	20.67	7.55
OPBIT	11.60	8.66	33.97	5.62	1.77	2.31
Interest Expenses & Similar Charges	2.22	1.29	72.35	1.08	0.55	0.74
OPBT(Net Operating income)	9.38	7.37	27.25	4.55	1.22	1.57
Taxation (N'm)	-	-	-	3.22	-	72.60
Profit After Tax	9.38	7.37	27.25	4.54	1.22	1.50
Retained Profit	9.38	7.37	27.25	4.54	1.22	1.50

Balance Sheet as @ 31st December, 2005 (N'b)						
	2005	2004	% Change	2003	2002	2001
Fixed Assets	14.53	14.68	(1.02)	15.08	15.78	3.98
Current Assets	29.95	21.40	39.97	15.91	4.23	3.71
Stock & Work in Progress	3.09	2.96	4.49	0.31	3.61	2.35
Debtors & Prepayments	26.86	16.17	66.15	13.77	(0.47)	0.57
Cash Balances	4.49	2.28	(99.80)	1.83	1.10	0.80
Total Assets	44.49	36.08	23.29	30.99	20.01	7.69
Current Liabilities	9.68	10.69	(9.44)	13.03	6.59	6.41
Bank Borrowings (Secured)	-	-	-	12.29	5.07	3.59
Trade & Other Creditors	9.68	10.69	(9.44)	0.74	1.52	2.82
Total Liabilities	9.68	10.69	(9.44)	13.03	6.59	6.41
Working Capital/Net Current Assets	20.27	10.71	89.31	2.88	(2.36)	(2.70)
Total Assets Less Current Liabilities	34.80	25.39	37.07	17.97	13.42	1.28
Provision for Liabilities & Charges	0.09	0.05	-	-	-	-
Net Assets	34.72	25.34	37.02	17.97	13.42	1.28
Capital & Reserves						
Revaluation Reserve	10.92	10.92	-	10.92	10.92	-
General Reserve	23.79	14.41	65.08	7.04	2.50	1.28
Shareholders' Funds	34.72	25.34	37.02	17.97	13.42	1.28

Key Ratios						
	2005	2004	% Change	2003	2002	2001
Gross Profit Margin (%)	24.00	29.45	(5.46)	22.74	16.60	19.50
Operating Profit Margin (%)	19.84	23.53	(3.69)	20.08	12.94	15.58
Profit After Tax Margin (%)	16.04	20.15	(4.12)	16.30	9.01	10.12
Return on Equity (%)	27.02	29.09	(2.07)	25.29	9.09	117.23
Return on Total Assets (%)	21.08	20.43	0.65	14.66	6.09	19.49
Return on Capital Employed (%)	33.34	34.11	(0.77)	31.30	13.21	180.98
Current Ratio	3.09	2.00	1.09	1.22	0.64	0.58
Quick Ratio	2.77	1.72	1.05	1.20	0.09	0.21
Working Capital to Sales (%)	34.65	29.28	5.38	10.35	(17.41)	(18.25)
Adjusted Earnings Per Share(kobo)	93.80	73.71	20.09	45.44	12.19	14.99
Adjusted Earnings Yield (%)	5.21	4.10	1.12	2.52	0.68	0.83
Adjusted Net Asset Value (N)	3.47	2.53	0.94	1.80	1.34	0.13

Source of Information: Offer Prospectus and the Annual Account of the companies mentioned

(Information relating to Flourmills was as at 31 March, 2006 while Nestle and NBC were as at 31 December, 2005).

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COMPARATIVE ANALYSIS				
COMPANY	DSR	NESTLE	NBC	FLOURMILLS
Turnover (N'b)	58.49	34.34	55.44	86.57
CAGR % (Turnover)	41.00	24.89	12.25	18.92
PBT (N'b)	14.04	7.91	3.58	6.31
PAT (N'b)	9.38	5.30	2.31	4.65
PAT Margin (%)	16.04	15.44	4.17	5.37
CAGR,% (PAT)	58.22	20.67	(6.43)	33.05
Shares in Issue (b)	10.00	0.53	1.30	1.16
ROCE (%)	33.33	148.68	14.23	24.02
Return ON Equity (%)	27.09	311.76	12.37	30.26
Net Asset P/S (N)	3.47	3.21	14.31	9.81
Price @ YR End	18.00	187.00	65.36	28.50
Current Price (N)	18.00	227.63	46.45	65.00
EPS @ YR End	0.94	10.04	1.78	4.01
CAGR % EPS	58.16	20.39	(12.74)	9.20
Current EPS	0.94	11.16	1.04	3.26
P/E Ratio @ YR End	19.19	18.63	36.72	7.11
Current P/E Ratio	19.19	20.40	44.66	19.94
P/E Ratio (Dec, 06)	10.04	18.83	29.97	19.76