

Dangote Sugar Refinery Plc.

Q1-18 performance supports our view on “strong test” in 2018; SELL

Update: DANGSUGAR published Q1-18 result last Friday, showing EPS grew 12% y/y but declined 59% q/q. The EPS growth came on the back of a higher gross margin compared to last year's one-off low, masking a disappointing revenue performance. **Should we adjust Q1-17 gross margin to Q1-18's 25% (which is also the average achieved in 2017FY), we have EPS of -55% y/y and -60% q/q.**

Volume still weak, despite lower price: According to management, Q1-18 sales volume was down 12% y/y (+2 q/q), despite selling price now lower by about 22% y/y. The volume outturn raises concern for 2018 revenue as a whole, given that the January-March quarter (and indeed, the first half) is seasonally strong for DANGSUGAR. On the 2017FY results call, management reiterated some of the volume concerns we had highlighted in previous notes – notably the activities of smugglers and the poor condition of the factory road – and added that the road to the North (accounting for 36% of revenue and where about the highest margin is derived) is equally deplorable, with negative impact on revenue.

Also of concern is that the NGN13,056/tonne average selling price computed by management in the latest result is way below the NGN14,000/tonne price it said it was able to achieve during the last call held earlier this month. We have consequently revised our 2018E volume growth forecast to 5% (previously 9.5%) and cut average selling price estimate to NGN13,000/tonne – while acknowledging that the possibility of price further reducing has increased with the poor volume outturn in Q1.

In-line gross margin estimate is unchanged: At 25%, the gross margin achieved in Q1-18 is about the 25.8% we estimated for 2018E. While noting that the downside risk to selling price, and consequently margin, has increased with this Q1 result, we should reiterate some tailwinds supporting our gross margin estimate as: (1) better energy mix, (2) stable and stronger exchange rate, (3) stable outlook of global raw sugar prices, and (4) positive mix from growing contribution of higher margin Savannah.

Opex must be reined in: Although opex declined by 1.3% y/y in Q1-18, the ratio to revenue increased by 141 bps y/y to 4.7%. With revenue now starting the year on an unimpressive note, we expect DANGSUGAR's management must seek strategies to contain operating expenses, without which earnings risk falling significantly below last year's. The group achieved 3.6% opex margin in 2017FY, and our estimate for 2018E is 3.7% (unchanged). DANGSUGAR's operating expenses have traditionally been lower in Q2 and higher in Q4, compared to other quarters.

Valuation: We revise TP lower to NGN17.42 (previously NGN17.97), reflecting the downward revision of revenue estimate. SELL rating maintained. On our estimates, DANGSUGAR is trading at 2018F P/E and EV/EBITDA multiples of 7.6x and 4.x respectively, consistent with its five-year historical averages of 7.9x and 4.4x, but below the 14.3x and 9.4x Middle Eastern peer averages.

SELL

Target Price (NGN)	17.42
Current Price (NGN)	21.40
Implied Return (%)	-18.58
Expected Dividend Yield (%)	6.55
Expected Total Return (%)	-12.03

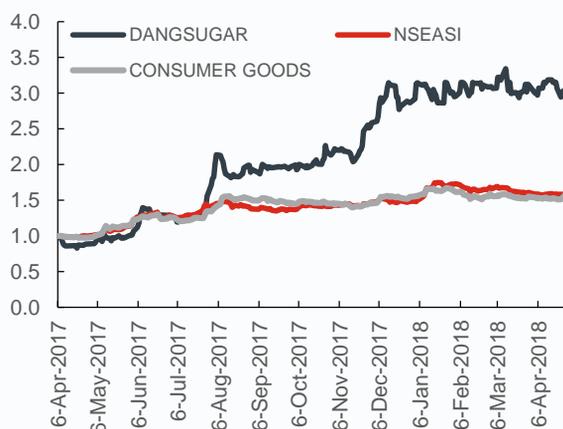
Company Data

NSE Code	DANGSUGAR
Bloomberg Code	DANGSUGAR:NL
Reuters Code	DANGSUGAR.LG
Sector	CONSUMER GOODS
Market Cap. (NGN'bn)	256.80
Free Float (%)	26.90

Ratios	Q1-2018	Q1-2017	2017FY
Gross margin	25.00%	13.17%	24.94%
Opex margin	4.72%	3.30%	3.66%
EBITDA margin	23.30%	11.47%	23.94%
EBIT margin	20.54%	9.99%	21.48%
PAT margin	12.83%	7.99%	19.46%
RoAE**	45.16%	23.85%	21.97%
EPS (NGN)	0.45	0.40	3.32

**12 months

Price movement (DANGSUGAR vs. Benchmark Indices)



Source: NSE, Bloomberg, Cordros research

Summary of Quarterly Results.

Income Statement (NGN'bn)	31-Mar-18	31-Mar-17	y/y	q/q	Q4:17	Q3:17	Q2:17
Revenue	41.14	59.53	-30.9%	-0.6%	41.39	44.35	59.15
Cost of Sales	30.85	51.69	-40.3%	-3.2%	31.88	29.77	40.10
Gross profit	10.29	7.84	31.2%	8.1%	9.51	14.59	19.05
OPEX	1.94	1.97	-1.3%	-10.8%	2.18	1.90	1.44
Other income	0.10	0.07	41.7%	-50.3%	0.21	0.06	0.05
EBIT	8.45	5.95	42.1%	12.0%	7.55	12.75	17.67
Investment income	0.87	0.97	-10.2%	-12.6%	1.00	0.71	0.69
Fair value adjustments	-0.88	0.12	-818.1%	-158.0%	1.52	0.67	0.16
Financial charges	0.05	0.00		-101.1%	-4.29	0.13	0.30
Profit before tax	8.39	7.04	19.2%	-41.5%	14.35	14.00	18.21
Taxation	3.11	2.28	36.4%	187.5%	1.08	4.58	5.87
Profit after tax	5.28	4.76	10.9%	-60.2%	13.26	9.42	12.34

Ratios	31-Mar-18	31-Mar-17		Q4:17	Q3:17	Q2:17
Gross margin	25.00%	13.17%		22.98%	32.88%	32.21%
OPEX margin	4.72%	3.30%		5.26%	4.29%	2.43%
EBITDA margin	23.30%	11.47%		23.52%	31.11%	31.41%
EBIT margin	20.54%	9.99%		18.23%	28.74%	29.87%
PBT margin	20.40%	11.83%		34.66%	31.56%	30.79%
PAT margin	12.83%	7.99%		32.05%	21.23%	20.87%
Tax rate	37.11%	32.43%		7.55%	32.72%	32.23%
RoAE	45.16%	23.85%				
EPS (NGN)	0.45	0.40		1.09	0.79	1.03

Source: Company Accounts, Cordros Research

Financial Statement (NGN'billion).

Income Statement (N'bn)							Profitability Ratios						
	2014a	2015a	2016a	2017a	2018e	2019e		2014a	2015a	2016a	2017a	2018e	2019e
Turnover	94.86	101.06	169.72	204.42	184.38	214.24	Gross profit margin	19.6%	20.5%	13.5%	24.9%	25.8%	25.9%
Cost of Sales	-76.23	-80.33	-146.74	-153.43	-136.89	-158.70	EBITDA margin	19.8%	21.1%	14.2%	25.1%	26.8%	27.0%
Gross profit	18.63	20.73	22.99	50.99	47.49	55.53	Operating profit margin	15.9%	15.7%	9.9%	21.5%	22.3%	22.3%
Operating expenses	-8.60	-6.21	-6.93	-7.48	-6.85	-8.08	PBT margin	16.1%	16.4%	11.6%	26.2%	25.3%	25.6%
Other income	5.07	1.33	0.75	0.40	0.40	0.41	Net profit margin	12.3%	11.4%	8.5%	19.5%	17.2%	17.4%
Operating profit	15.09	15.85	16.81	43.91	41.04	47.86	RoAE	23.7%	21.1%	23.2%	50.1%	32.4%	32.8%
Investment income	0.29	0.01	0.60	3.36	3.37	4.13	RoAA	13.2%	11.8%	10.3%	21.4%	16.3%	17.3%
Fair value adjustments	-	1.35	2.50	2.47	2.46	3.01							
Interest expenses	-0.11	-0.66	-0.30	3.86	-0.14	-0.14	Liquidity Ratios						
Profit before tax	15.27	16.55	19.61	53.60	46.73	54.87	Working capital (NGN'bn)	1.5	3.8	11.8	32.8	43.2	50.2
Tax expense	-3.64	-5.01	-5.22	-13.82	-14.95	-17.56	Current ratio	1.0x	1.1x	1.1x	1.3x	1.5x	1.5x
Profit after tax	11.64	11.54	14.40	39.78	31.78	37.31	Quick ratio	0.6x	0.7x	0.6x	0.8x	0.9x	0.9x
							Cash ratio	0.2x	0.2x	0.3x	0.4x	0.5x	0.5x
Financial Position (N'bn)							Efficiency Ratios						
	2014a	2015a	2016a	2017a	2018e	2019e		2014a	2015a	2016a	2017a	2018e	2019e
PPE	50.47	54.80	54.80	59.41	59.11	72.50	Fixed assets turnover	1.88x	1.84x	3.10x	3.44x	3.12x	2.96x
Other assets	0.19	0.00	0.00	0.00	0.00	0.00	Current assets turnover	2.48x	2.34x	1.51x	1.59x	1.44x	1.37x
Biological assets	1.12	1.55	-	-	-	-	Total assets turnover	1.02x	0.98x	0.96x	1.05x	0.95x	0.90x
Investment property	-	-	-	-	-	-	Inventory turnover	0.2x	0.2x	0.1x	0.1x	0.1x	0.1x
Deferred tax assets	2.49	2.97	10.10	7.17	7.14	8.75	Receivables turnover	0.2x	0.2x	0.1x	0.1x	0.1x	0.1x
Intangible assets	0.26	0.14	0.01	0.00	0.00	0.00	Payables turnover	0.3x	0.3x	0.2x	0.1x	0.2x	0.1x
Total Non-current assets	54.54	59.46	64.92	66.59	66.25	81.26	Days inventory outstanding	60	61	33	32	36	31
Inventories	15.10	15.55	47.41	47.66	47.41	58.15	Days collection/sales outstanding	75	72	43	36	40	34
Biological assets	0.68	1.89	3.01	2.81	2.79	3.42	Days payable outstanding	121	128	220	180	179	194
Trade and other receivables	14.01	14.70	17.73	20.91	20.80	25.51	Cash conversion cycle	14	6	-143	-112	-103	-129
Other assets	1.41	1.17	9.43	14.88	14.81	18.16							
Held for sale investment in subsidiary	0.86	0.86	-	0.87	0.86	1.06	Investment Ratios						
Bank/cash balances	6.20	8.99	35.02	41.37	41.16	50.48	Earnings per share (NGN)	0.97	0.97	1.20	3.31	2.6	3.1
Total current assets	38.26	43.17	112.60	128.49	127.83	156.78	Dividend per share (NGN)	0.40	0.50	0.60	1.75	1.4	1.6
Total assets	92.80	102.62	177.52	195.08	194.09	238.04	Payout	41.2%	51.8%	50.0%	52.9%	52.9%	52.9%
Current tax liabilities	5.94	5.54	6.60	17.72	15.68	19.74	Dividend yield	4.5%	8.3%	9.8%	8.8%	6.5%	7.7%
Retirement benefit obligation	1.53	1.08	1.03	0.98	0.87	1.10							
Trade and other payables	25.23	28.09	88.28	75.65	66.95	84.29	P/E	9.22x	6.24x	5.10x	6.05x	8.08x	6.88x
Borrowings	2.39	2.50	2.04	0.07	0.07	0.07	EV/EBITDA	5.39x	3.09x	1.67x	3.89x	4.39x	3.60x
Other liabilities	1.70	2.11	2.81	1.24	1.10	1.38							
Total current liabilities	36.78	39.33	100.75	95.66	84.67	106.58							
Borrowings	-	-	-	1.47	4.44	5.98							
Deferred tax liabilities	4.61	5.15	11.48	5.21	5.90	7.45							
Employees' gratuities/provisions	-	-	-	-	-	-							
Total non-current liabilities	4.61	5.15	11.48	6.68	5.90	7.45							
Total Liabilities	41.39	44.48	112.23	102.34	90.57	114.03							
EQUITY	51.41	58.15	66.15	92.74	103.51	124.01							

Source: Company Accounts, Cordros Research

Disclosures.

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