

Price	₦10.35
52-week range	₦8.50-15.80
Market Cap. (₦bn)	124,200
1-month Avg. Vol	529,323
Curr. PE	6.2x

Dangsuga.NL - Share Price Trend



Analyst

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Dangote Sugar Refinery Plc. (DSR.NL)

Initial View

Volumes recovery muddled by biological asset gains

- Dangote Sugar refinery (DSR) released its 9M 19 result yesterday, with reported EPS down 12.6% YoY to ₦1.23 following lower finance income and cost pressures relative to same period in the prior year. Similarly, EPS over Q3 19 dropped by 6.7% YoY muddled by the dip in biological asset gains and lower interest income, both of which trumped gains from improved operating performance. Noteworthy, excluding the revaluation gains from both periods, Q3 19 earnings is up by 5% YoY. Relative to our estimates, sales and EPS came in lower by 2.5% and 7.7% respectively.
- Hurray, as sugar sales picks up:** Coming from downbeat levels in 2018, we are quite impressed by DSR's growth in volume since Q2 19. Going by our estimates, volumes grew by 16.1% YoY in Q3 19 (Q2 19: 13.4% YoY) assuming flat prices between Q2 and Q3. This is quite impressive coming from a double-digit decline in volumes recorded all through 2018. Most of the gains emanated from its northern operation where it had to combat with influx of smuggled sugar into the country. While we recognise DSR's effort in confronting its devil in the north, we do not rule out the plus from the border closure which was implemented towards the end of August as a further support to sales. On cost, average raw sugar prices over Q3 19 was up by 7.8% YoY driving an increase in input cost (+12.6% YoY) – albeit, the faster increase in sales left margins in a favourable position.
- Biological asset gains muddles improved operating performance:** Atypical to the prior quarter, DSR recorded an improvement in operating performance over Q3 19, with gross and EBIT margin expanding 55bps and 12bps YoY to 21.3% and 15.1% respectively. Improved margins were largely supported by higher sugar sales (+13.4% YoY) observed over the period which overshadowed increase in input cost (+12.6% YoY). However, the significant drop in gains from fair value adjustment on biological assets, left PBT lower 5.8% YoY. For context, excluding the revaluation gains, PBT would have been higher by 5% YoY, despite the dip in finance income. Largely reflecting lower cash balance (with ending cash balance as at 9M 19 printing at ₦11.6 billion – a reflection of the company's struggle to generate funds from operations), finance income declined to ₦5.5 million (Q3 18: ₦481.8 million). Notably, 9M FFO printed at ₦27.4 billion from ₦37.4 billion recorded in 2018, with cash margin contracting 467bps to 9.8% YTD.

- Though earnings declined over the period, we are quite impressed by the gradual recovery in the company's market share, which we believe would be sustained in the near-term supported by the border closure. While we do not rule out the plausibility of an increase in raw sugar prices, we think the growth in sales would be able to sustain the improved margins seen thus far. Our FVE of ~~₹14.02~~ **₹14.02** coupled with our expected dividend yield of 10%, presents 46% upside using last closing price, which translates to a BUY rating. DSR currently trades at a P/E of 6.2x which is at a discount to Bloomberg MENA peer average of 21.7x, respectively.

Summary of Results

	Q3 19	YoY growth	QoQ growth	9M 19	9M 18	YoY growth
Revenue	37,061	13.4%	-12.2%	117,425	116,756	0.6%
Cost of sales	29,157	12.6%	-13.5%	88,406	86,670	2.0%
Gross profit	7,904	16.4%	-7.3%	29,019	30,086	-3.5%
Operating expenses	2,326	21.9%	8.3%	6,238	6,140	1.6%
Operating profit	5,578	14.3%	-13%	22,781	23,945	-4.9%
Net interest expense	(14)	NA	NA	509	1,999	-74.6%
PBT	5,936	-5.8%	-6%	22,968	26,207	-12.4%
PAT	3,726	-6.7%	-6%	14,703	16,710	-12.0%

	Q3 19	Q3 18	Change(pps)	9M 19	9M 18	Change(pps)
Gross margin	21.3%	20.8%	0.6%	24.7%	25.8%	-1.1%
EBIT margin	15.1%	14.9%	0.1%	19.4%	20.5%	-1.1%
PBT margin	16.0%	19.3%	-3.3%	19.6%	22.4%	-2.9%
PAT margin	10.1%	12.2%	-2.2%	12.5%	14.3%	-1.8%
Effective tax rates	37.2%	36.6%	0.6%	36.0%	36.2%	-0.3%

Source: ARM Research *unless otherwise stated

ARM ratings and recommendations

ARM now employs a two-tier rating system which is based on systemic importance of the security under review and the deviation of our target price for the stock from current market price. We characterize systemic importance as a function of a stock's ranking among the group of top 20 stocks by NSE market capitalization over a trailing 6-month period (minimum) to the review date. We adopt a 5-point rating system for this category of stocks and a 3-point rating system for stocks outside this group. The choice of top 20 stocks arises from the consideration that this group of stocks constitutes >75% of overall market capitalization and stocks outside this group are generally less liquid and individually account for <<1% of market capitalization. For stocks in both categories, the basis for ratings subject to target price deviation is outlined below:

TOP 20		NON-TOP 20	
Rating	Deviation	Rating	Deviation
STRONG BUY	>20%	BUY	>20%
OVERWEIGHT	10% — 20 %	NEUTRAL	5% — 20 %
NEUTRAL	0% — 10 %	SELL	<5%
UNDERWEIGHT	-5% — 0%		
SELL	<-5%		

RECOMMENDATION KEY	
Rating	Recommendation
BUY	Accumulate security to a substantial extent constrained only by portfolio diversification considerations
OVERWEIGHT	Accumulate security to an extent moderated by cognizance of its benchmark weight
NEUTRAL	Maintain status quo for security with respect to current holding—i.e. keep if already holding and don't buy otherwise—subject to reas portfolio constraints
UNDERWEIGHT	Minimize exposure to security taking cognizance of its index weighting
SELL	Sell-off security completely from portfolio

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