

May 18, 2022



Earnings Note

Event

In its recently released financial statements for Q1 2022, Dangote Sugar Refinery (DSR) recorded a 7% YoY increase in profit after tax to N8.87bn despite a 40% YoY revenue growth to N94.45bn.

Higher Commodity Prices Exert Margin Pressures

The rising cost of raw sugar in the global market amid higher crude oil prices and global supply chain disruptions – both developments majorly driven by geopolitical tensions in the Eastern Europe resulted in cost pressures for DSR. Raw material costs, which accounted for 85% of total cost of sales, grew by 59% YoY to N63.57bn in Q1 2022.

In response to the higher input cost, we believe that DSR partially raised prices to ease the burden. However, from our analysis, we posit that the entire cost burden was not passed on to consumers. Hence, gross margin declined by 600 basis points to 21% in Q1 2022. We attribute the inability to pass on overall burden to consumers to rising competitive pressures amid capacity ramp-up by other competitors in the industry.

Profit before tax margin declined by c. 300 basis points to 15%, despite the Group's operating efficiency efforts (evidenced by c. 100 bps reduction in operating expense margin).

Outlook

Uncertainty about the duration of the geopolitical conflict between Russia and Ukraine poses a significant downside risk to the earnings growth capacity of DSR. A prolonged stand-off could keep crude oil prices higher, and that implies a sustained scarcity of raw materials for DSR as raw sugar suppliers tend to produce less in times of higher oil prices.

This major challenge informed the Group's decision to invest in backward integration, which is still ongoing. The Group is expected to benefit from these investments in the long term.

Valuation

Following appropriate adjustments, we have a revised forward EPS of N2.37 ([previously](#): N2.61) informed by higher cost. Our reviewed fair value estimate of N20.62 trades at a 21% discount to the current market price. Incorporating a forecasted dividend yield of 7% sums up to a total return of 28%. Hence, we recommend a **BUY**.

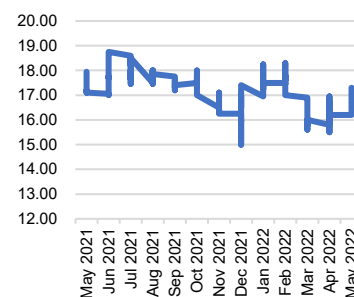
BUY

Fair Value Estimate:
N20.62

Stock Data

Current price (N)	17.00
Shares Outstanding (mn)	12,147
Market Cap (N'mn)	206,497
52-week high (N)	18.75
52-week low (N)	15.00
Trailing EPS (N)	1.82
Forward EPS (N)	2.37
Forward PE (X)	7.18
Justified PE Multiple (X)	8.71

Price movement



Stock Data	FY 2020	FY 2021	FY 2022F
P/E	6.94x	9.36x	7.18x
P/BV	1.66x	1.61x	1.42x
PBT Margin	21%	12%	11%
PAT Margin	14%	8%	8%
RoE	26%	17%	21%
Dividend Yield	9%	6%	7%

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Financial Performance Summary

Income Statement (N'mn)	Q1 2022	Q1 2021	% Change
Revenue	94,449	67,394	40%
Cost of Sales	(74,986)	(49,349)	52%
Gross Profit	19,463	18,044	8%
Other income	69	100	-31%
Operating income	19,531	18,144	8%
Selling and distribution expenses	(261)	(124)	110%
Administrative expense	(2,243)	(2,136)	5%
Operating expenses	(2,504)	(2,260)	11%
Operating profit	17,027	15,884	7%
Fair value adjustment	(729)	(650)	12%
Investment income	810	127	539%
Financial Charges	(3,505)	(3,412)	3%
Profit before tax	13,603	11,949	14%
Tax	(4,733)	(3,647)	30%
Profit after tax	8,870	8,302	7%
Balance Sheet Information (N'mn)	3M 2022	FY 2021	% Change
Assets			
Non-current assets			
Property, plant and equipment	149,936	104,737	43%
Total non-current assets	149,936	104,737	43%
Current assets			
Inventories	54,717	55,640	-2%
Biological assets	2,686	3,678	-27%
Trade and other receivables	57,857	57,530	1%
Other assets	992	849	17%
Assets held for sale	869	869	0%
Cash and cash equivalents	128,594	68,637	87%
Total current assets	245,715	187,203	20%
Total Assets	395,651	291,941	36%
Liabilities			
Non-current liabilities			
Deferred tax liabilities	10,432	9,580	9%
Lease liabilities	823	1,337	-38%
Borrowings	699	984	-29%
Total non-current liabilities	11,954	11,902	0%
Current liabilities			
Current tax liabilities	15,182	4,525	236%
Lease liabilities	1,589	1,130	41%
Borrowings	232	148	57%
Trade and other payables	224,936	138,214	63%
Employee benefits	763	963	-21%
Other liabilities	3,494	2,045	71%
Total current liabilities	246,196	147,025	67%
Total liabilities	258,150	158,927	62%
Net Assets	137,501	133,013	3%

Source: Company Accounts, WSTC Research

Financial Projections

Income statement (N'mn)	FY 2020	FY 2021	FY 2022F	FY 2023F	FY 2024F	FY 2025F	FY 2026F
Revenue	214,298	276,055	379,791	474,738	569,686	655,139	720,653
EBITDA	55,610	48,292	61,659	84,722	106,518	129,691	142,717
EBIT	47,911	39,020	49,060	68,156	86,633	129,691	142,717
Profit before taxation (PBT)	45,622	34,021	42,278	60,515	77,861	119,654	131,809
Net profit (PAT)	29,775	22,052	28,749	41,151	52,945	81,364	89,630
EPS (₹)	2.45	1.82	2.37	3.39	4.36	6.70	7.38
DPS (₹)	1.50	1.00	1.20	1.36	1.74	2.68	2.95
Balance sheet (N'mn)	FY 2020	FY 2021	FY 2022F	FY 2023F	FY 2024F	FY 2025F	FY 2026F
Current assets	176,299	214,828	279,210	339,580	415,511	493,206	565,214
Non-current assets	101,734	144,678	185,250	201,915	210,514	220,670	232,047
Total assets	278,032	359,506	464,459	541,495	626,025	713,876	797,262
Current liabilities	142,049	218,543	303,939	353,465	400,185	426,878	452,318
Non-current liabilities	11,271	12,331	15,287	16,222	17,547	18,518	19,380
Long-term debt	984	764	2,848	3,561	4,273	4,914	5,405
Shareholders' equity	124,712	128,631	145,234	171,808	208,293	268,479	325,564
Book value per share (₹)	10.27	10.59	11.96	14.14	17.15	22.10	26.80
Cash flow statement (N'mn)	FY 2020	FY 2021	FY 2022F	FY 2023F	FY 2024F	FY 2025F	FY 2026F
Cash from operating activities	60,200	129,247	67,653	76,376	88,134	112,639	122,714
Cash from investing activities	(26,168)	(51,292)	(52,252)	(32,747)	(27,517)	(31,749)	(34,821)
Cash from financing activities	(13,783)	(19,806)	(15,066)	(21,520)	(24,666)	(30,978)	(43,594)
Net increase/ (decrease) in cash	20,249	58,149	335	22,110	35,951	49,912	44,298
Free Cash Flow to Equity	32,499	76,281	11,563	36,201	51,445	70,082	75,633
Ratio analysis (%)	FY 2020	FY 2021	FY 2022F	FY 2023F	FY 2024F	FY 2025F	FY 2026F
EBITDA margin	25.95	17.49	16.24	17.85	18.70	19.80	19.80
Operating margin	22.36	14.13	12.92	14.36	15.21	19.80	19.80
ROE	25.57	17.41	21.00	25.96	27.86	34.13	30.18
ROA	12.62	6.92	6.98	8.18	9.07	12.14	11.86
Dividend payout ratio (%)	61.19	55.08	50.70	40.00	40.00	40.00	40.00

Source: Company Accounts, WSTC Research

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WSTC uses a 3-tier recommendation system for stocks under coverage: Buy, Hold, and Sell.

- Buy Rating: estimated fair value is $\geq 15\%$ above current market price.
- Hold Rating: estimated change in price is between -10% and 15% of current market price.
- Sell Rating: estimated change in price is $\leq -10\%$ of current market price.

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