Equity Research Report — NIGERIA

FSDH SECURITIES LIMITED

Dangote Flour Plc: *Interim Results – Q3, Sept. 2009*

March 11, 2010 | **BUY** | **Fair Value: NGN 21.42** | **Current Price: NGN13.92**

Ticker	Dang Flour
Sector	Food/Beverages & Tobacco
Date of Incorporation	January, 2006
Date of Listing	February 04, 2008
Year End	December
No of Ordinary Shares	5,000,000,000
Capitalisation (N)	69,600,000,000
% of Market Cap.	1.23
52-Week High (N)	14.58
52-Week Low(N)	4.38
YTD Return (%)	40.18
52-Week Avg. Trade	2,629,632
Beta Value	1.56
Current EPS (N)	1.77
Current PE(x)	7.49

Valuation/Analyst Recommendation

In placing a fair value on the Ordinary Shares of **DANGFLOUR**, we estimated **TO**, Earning Before Interest Tax Depreciation and Amortization (**EBITDA**) and **PAT** for the period ended December, 2009. We project a **TO** of **N62.604bn,** based on a growth rate of **30.62%** over the previous year. We project **EBITDA** of **N16.277bn** based on EBITDA margin of **26%** and a **PAT** of **N10.154bn** based on a PAT Margin of **16.22%.** We used **5bn** Ordinary Shares in issue as at December 2009. The Earnings Per Share **(EPS)** generates **N2.03**. We estimated Dividend Per Share **(DPS)** of **N1.02** based on a dividend payout of **50%.** We note that DANGFLOUR already paid an interim dividend of 30kobo; therefore, we expect a final dividend of 72kobo. Applying Enterprise Value EV/EBITDA multiple of **8.12x,** a P/E multiple of **10x**, we arrived at **N22.32** per share using EV/EBITDA multiple and **N20.31** per share price using earnings multiple. Applying a weight of **55%** on **N22.32** and **45%** on **N20.31**, we arrived at **N21.42** per share, which is our fair value. The earnings yield and dividend yield based on our fair value generate **9.48%** and **4.74%** respectively. We therefore place a **BUY** on the shares of DANGFLOUR at the current market price.

Business Description

The principal activities of DANGFLOUR are milling, processing and marketing of branded flour.

Improved Customer Service for Growth:

The unaudited Q3, 2009 result of **Dangote Flour Mills Plc (DANGFLOUR)** for the period ended September 30, 2009 shows that its Turnover (TO) increased by **34.77%** to **N46.95bn**, compared with N34.84bn in the corresponding period of 2008. Profit Before Tax (PBT) increased significantly by **227.31%** between 2008 and 2009 to **N8.46bn** from N2.59bn in the corresponding period of 2008. The tax provision which increased marginally by 2.3% between 2008 and 2009 to **N846.13mn** from N827.46mn resulted in the Profit After Tax (PAT) of **N7.62bn,** from N1.76bn in 2008 representing a growth of **333.16%.** The PBT Margin in Q3, 2009 increased significantly over the corresponding period in 2008 and over the FY, 2008 figure.

The PBT margin increased significantly to **18.02%** in Q3, 2009 from **7.42%** as at Q3, 2008, and also up significantly from **6.61%** as at the end of the financial year in December, 2008.This shows that the company's total costs as a percentage of TO stands at **81.98%**, down from **92.58%** recorded in the corresponding period of 2008. PAT margin currently stands at **16.22%**, up from **5.05%** in the corresponding period of 2008, and also up from **6.24%** as at FY 2008.The result also indicated that the percentage of TO, PBT, and PAT in the Q3 2009 to the Full Year Audited TO, PBT and PAT for the period ended December, 2008 are: **97.97%**, **167.16%** and **154.77%** respectively. Given the current run rates DANGFLOUR should surpass its previous years performance with wide margins.

A cursory look at the balance sheet position as at Q3, 2009 compared with the position as at December 2008, shows that its fixed assets decreased marginally by 6.11% to N31.30bn from N33.34bn in FY, 2008, reflecting sale of obsolete assets while the net assets increased significantly by 32.54% to N31.47bn from N23.74bn as at FY, 2008. The growth in the net assets is on account of the improvement in the quarterly retained earnings; a reflection of the impressive performance in the profitability in the current financial year. Cash and bank balances increased from N6.94bn in FY, 2009 to N11.46bn in Q3, 2009. Short-term borrowing as at Q3, 2009 was down by 37.39% to stand at N14.08bn from N22.50bn as FY 2008. This drop in the short-term loan may be a deliberate effort to avoid excessive interest payments or banks are unwilling to renew the credit at maturity. DANGFLOUR's working capital position improved significantly from a negative position of N8.16bn in FY, 2008 to a negative of N48.02mn. Stocks however decreased by 41.18% to N7.80bn from N13.25bn in FY, 2008. The trade debtors decreased by 27.18% to N7.99bn from N10.97bn, while trade creditors increased by 34% to N18.73bn in Q3, 2009 from N13.97bn as at FY, 2008.

Our analysis of the operating environment shows that the manufacturing and distribution businesses in Nigeria are faced with infrastructure challenges (transportation and power). In order to meet their power needs, manufacturing companies in Nigeria invest heavily in alternative sources of power. The costs of acquiring and maintaining these equipments add in no small measure to the operating costs. Manufacturing firms sometimes shift some of these costs to their customers in form of increase in the price of goods, while firms bear a portion of it. The extent of the shiftability also depends on the elasticity of the product in question to price. Sometimes we notice a drop in demand, as a result of increase in price. In addition to the problem of infrastructure, the current financial crisis and the unwillingness of banks to lend has reduced credit to the real sector, while the available credit commands high interest rates, thus increasing financing costs for the manufacturers. The combination of these factors has limited the growth of the manufacturing sector in the country, despite the huge market potentials within and in the neighboring countries. In the last one year, the manufacturing sector has not witnessed significant improvement as the capacity utilization fluctuates between 35% and 40%. Its contribution to the Gross Domestic Product (GDP) as at September 2009 is 3.49%. This is considered too low for a country that has a huge consumption power like Nigeria; having an estimated market size of 150million. Also, there exists a growing middle class whose tastes and life style are changing for high quality consumer goods and products.

In 2009, **DANGFLOUR** commissioned the expansion of its Noodles factories in Ikorodu, Kano and Calabar. Furthermore, it continues with its production expansion capacities in its factories in Apapa, Calabar and Ilorin. The company planned to expand the current 4,800 metric tons of milling capacity per day to 7,300 metric tons. In order to diversify its production, it acquired controlling interest in **Dangote Pasta Ltd** and **Dangote Agro sacks Ltd**. Dangote Pasta Limited manufactures Spaghetti and Macaroni while, Dangote Agro Sacks Limited manufactures packaging materials. In turn, Dangote Agro Sacks holds 75% equity in Obajana Agro Sacks Limited. DANGFLOUR is also related to the following companies: Dangote Sugar Refineries Plc; Dangote Transport Ltd; Dangote Industries Ltd; Bluestar Shipping Company; Green View Development Nigeria Ltd; Dangote Salt Nigeria Ltd and Dangote Fisheries Nigeria Ltd. The products of DANGFLOUR include **Flour**, **Bran**, **Danvita & Semolina**, **Sacks**, **Spaghetti** and **Macaroni**. Its major competitors in the southern part of Nigeria are: Flour Mills of Nigeria and Honeywell Flour Mills. The shareholding structure as at December 31, 2008 shows that **Dangote Industries Ltd** held **73.35%** of the ordinary shares in issue, while other Nigerians held the remaining **26.65%**.

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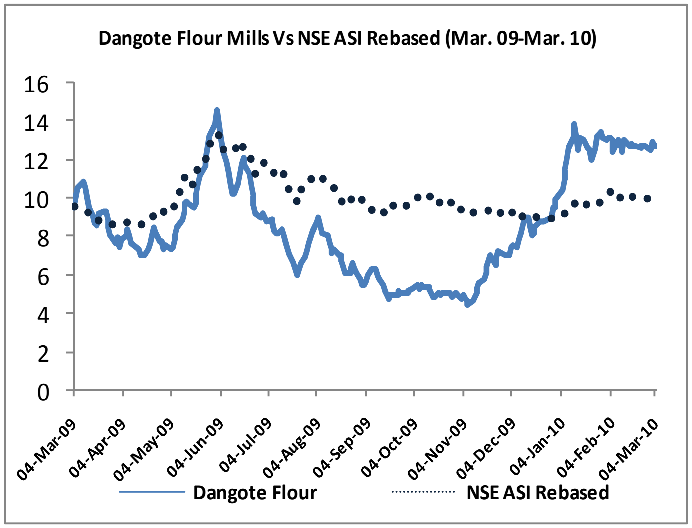
Industry Analysis (Nmn)							
Company	TO	PBT	PAT	PAT Margin (%)	ROE (%)	EPS*	PE*
Dangote Flour	47,927	3,168	2,990	6.15	12.10	1.77	7.03
NNFM	8,533	310	236	2.77	27.31	3.54	6.50
Flour Mills	180,068	5,470	3,892	2.16	11.16	6.83	7.87

*Source: Company Annual Reports, NSE FACTBOOK. * Current. NNFM (FY March 2009), Flour Mills (FY March 2009) & Dang. Flour (FY Dec 2008).*

Financial Performance (Nmn)							
	Q3 2009	Q3 2008	%Δ	FY 2008	FY 2007	%Δ	FY 2009E
Turnover	46,953	34,839	34.77	47,927	42,153	13.7	62,604
PBT	8,461	2,585	227.31	3,167	676	368.7	11,946
PAT	7,615	1,758	333.16	2,989	562	432.3	10,154
PBT Margin (%)	18.02	7.42	10.60	6.61	1.60	5.01	19.08
PAT Margin (%)	16.22	5.05	11.17	6.15	1.24	4.91	16.22



Directors As At December 31, 2008

Name	Position	Holding
Aliko Dangote	Chairman	32,283,333
Rohit Chaudhry	MD	-
Shuaibu Idris	Exe Director	100,000
Sani Dangote	Director	-
Olakunle Alake	Director	377,500
Uzoma Nwankwo	Director	271,500
Abdu Dantata	Director	-
Abdullahi Mahmoud	Director	43,750
Asue Ighodalo	Director	-
S.L. Teidi	Director	-

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