

MERISTEM EQUITY RESEARCH REPORT



REPORT DATE: APRIL 13, 2007

Recommendation: BUY

12-month Target Price: N31.41

EXECUTIVE SUMMARY AND INVESTMENT RATIONALE

- RT Briscoe (Nigeria) Plc is an automotive and technical equipment company located at 11, Fatai Atere Way, Matori Industrial Avenue, Oshodi, Lagos. The company was incorporated in March 09, 1957, converted to a public liability company in 1973 and listed on the floor of The Nigerian Stock Exchange on March 15, 1974.
- The Company, whose nature of business is sales and service of motor vehicles, technical equipment, including forklifts, industrial compressors, mining and drilling equipment and generating sets as well as equipment supply, site construction and maintenance for companies in the Oil & Gas, Power and Telecoms industries, has five subsidiaries namely **Briscoe Toyota, Briscoe Ford, Briscoe Properties, Atlas Copco** and **Briscoe Solutions Plus**. It has international affiliations with companies such as **Ford Motor Company, Toyota Japan, Atlas Copco Sweden & Atlas Copco Belgium**.
- **The company has about 363 million shares with ARM becoming a major shareholder after acquiring about 61.4% stake in the company from the former core investor -EAC Trading Ltd, A/S, Copenhagen, Denmark. However, as at 2006, ARM holding stood at 41%.**
- The company is operating in an auto and transport industry with bottom-lines been exposed to and contingent upon economic growth, good government policies, demographic and income distribution and other economic variables such as government spending, per capital income and other socio-political factors. The industry is not heavily regulated and it is more cyclical in nature.
- RT Briscoe has consistently grown its earnings and witnessed improved economic performance in 2006, turnover improved by about N5.4 billion or 70.12 per cent to N13.1 billion from N7.7

billion in 2005. Profit after tax jumped by N332.1 million or 166.38 per cent to N531.7 million from the previous year's figure of N199.6 million.

- The company, in 2002, embarked upon a restructuring exercise with divestment from a number of unprofitable enterprises and concentrating resources on value adding opportunities. The restructuring and the public offer of 2004 provided enough liquidity to finance increased working capital needs and prune down financial charges/operating costs via debt repayment. This put the company on a sound pedestal. The Company recently announced that Ford Motor Company will be investing about N600m in the company.
- With the government favourable disposition to auto industry, enlarged credit base of the economy resulting from banking consolidation (by facilitating banking loans to individuals to buy cars), and changing class status such as migration from low to medium class, the growth prospect of RT Briscoe remain very high. As an industry that is recovering, growth opportunities exist for a reasonable period of time.
- Risks attached to our analysis of RT Briscoe are the political upheaval, policy reversal and technological improvement in the transportation industry that affects demand for motor vehicles and changing customers taste. It is expected that the Company will be able to respond to these changes with increased diversification to other major revenue areas other than Motor Vehicles which presently contributes more than 90% to earnings
- RT Briscoe performance has been stable with earnings surprises in its audited result for the year ended 2006. Return On Assets (ROA) and Return On Equity (ROE) grew to 12% and 24% respectively, both of which are above the industry average. Turnover took a dramatic jump from N7,726 million to N13,162 million, a quantum jump of about 170%. With EBIT of N957,187 representing over 118% increase over the previous year, and trailing EPS of N1.46, the company is believed to be doing well.
- We project a change in capital structure to 80:20 from its current 42:58. This is premised on the fact that the current working capital financial need may be sustainable and financed with more equity than debt. We also anticipate a further reduction in debt to sales ratio and increased diversification of the company's business. We are of opinion that the current mix of differentiation and cost strategy would be sustained with more focus on differentiation strategy

- We hold a BUY recommendation for RT Briscoe given our forecast earning of N1.02b, an average growth rate of 45% in the next five years and 13% thereafter with a justified P/E of 17.09.

The Global Motor Industry

The industry is characterized by large multinational corporations such as **General Motors, Ford Motor Company, Honda Motor Corporation, Toyota Motor Corporation** and **DaimlerChrysler**. Over the past two decades, these companies have consolidated through buy outs of smaller car manufacturers or by strategic alliances to ensure they remain the top 5 auto manufacturers. With consolidation the companies have witnessed enormous economies of scale, cost savings in research and development, marketing and overheads as well as increasing their distribution networks.

With respect to production of cars, the United States of America is the world's largest car producer followed by Japan, Germany, China and South Korea. The industry is segmented with greater demand coming from the emerging markets of China, India and Indonesia. Growth in car demand and manufacture is growing in china at an extreme rate. It is expected that by 2010 China will be the second largest car maker in the world

Internationally, the market is extremely competitive and manufacturers have to be innovative in product design and differentiation in order to woo customers. The drive to win market share from competitors is all encompassing as all the manufacturers produce cars with relatively the same features. A growing demand of consumers is premised on a search for increased comfort and technology in passenger cars. Demand is on the rise for the finest interior and exterior fittings, Internet access and compatibility, in car audio and video adaptive speed control and global navigation and satellite tracking systems.

The need to satisfy customers' wants has led to manufacturers making many additions to their cars and thus making them bigger and heavier and this puts greater pressure on fossil fuel supplies. This contradicts the current socio-political call for the reduction in carbon emissions. For the most part, car makers have been able to make smaller, lighter, and more fuel efficient cars and engines. The rising oil price has also led to a reduction in demand for Jeeps and Sports Utility Vehicles (SUVs). The recent success of ethanol in Brazil as an alternative fuel points to a new direction in which the car industry will likely go in the future.

The Nigerian Car Market

As road transportation remains a major means of transportation in Nigeria there is a relatively high

demand for motor vehicles. The supply of vehicles has always been from Government companies such as PAN and ANAMCO, who assemble motor vehicles locally. Another source of industry supply is private car dealerships that import motor vehicles such as Toyota Nigeria Limited, Coscharis, RT Briscoe, Honda Place, Scoa Motors, CFAO motors, besides numerous importation through smuggling of used cars. Due to low purchasing power of the average Nigerian, most have been forced to purchase used cars (tokunboh).

The economy has grown in the last two years and has brought with it an emerging middle class. This middle class, along with Banks, Telecoms and Oil and Gas companies, are the main consumers of new cars. Generally speaking, the penchant has been for Toyota and Honda brands but brands such as Kia, Hyundai, Skoda, and Volkswagen are ever resurgent. The assembled brands of Peugeot (PAN) and Mercedes Benz (ANAMCO) used to be the market leaders, but the dearth of raw materials and increasing cost of production have made these cars more expensive than the imported Asian brands by local car dealerships

The major driver of the sector is the country's economic growth. Stronger purchasing power spawns greater demand for cars and this will continue as long as GDP growth is sustained. Continued growth in per capita income will also lead to a switch in dependence from used to brand new cars. The provision of credit facility by the Banking and Insurance sectors in providing car loans will go a long way in sustaining the industry demand level. Over 90% of the world's cars are purchased through a credit scheme or financing arrangement. Most Banks do provide some form of financing but it is not at the reach of the common man.

In Nigeria the two sectors (i.e Banking and Insurance) are evolving thereby paving way for industry sustainable growth. Government policy also plays an important role as the Government is constantly looking at the industry for restructuring purpose.

In a recent report by BMI, it was stated that Nigeria's six car assembling plants were operating well below capacity. These plants are all partially or fully owned by the Federal Government. The on going privatization has led to Government divestment from the sector but foreign investment is yet to flow into the sector. However, the growth prospects are enormous in a country of 150 million people where less than 5% are estimated to own a car. Prospects also lie in the West African sub region where regional economic integration and the opening up of borders are paving the way for Nigeria to become the manufacturing hub of West Africa.

For the private car dealerships such as RT Briscoe, increased market share and profitability is dependent on cost cutting, reduction in import prices and provision of the best deal for customers. Discounts and

credit plans that facilitate movement of volumes will endear customers; however this should not be done at a risk to working capital or by overleveraging the company.

Risk Profile

RT Briscoe main income comes from its automobile division where all its products are imported, the company is therefore exposed to foreign exchange risk. Another risk is over diversification into areas in which the company is largely inexperienced. In terms of the power and energy, the company faces strong competition from engineering firms and the major generator importers such as Marapco, Jubaili and John Holt. The influx of banks into the property sector also poses a risk as many banks are invested in mortgage finance institutions as subsidiaries. The company also faces competition for market share in its motor vehicles divisions from competitors such as Toyota Nigeria Limited and Bras Motors.

Other risks include but not limited to policy reversals, political upheaval and technological advancement. It is expected that the Company will be awake to these potential drivers of downward trend in profitability.

Future Outlook

As a company that's more cyclical in nature, better performance is expected in the nearest future. This is premised on stronger economic performance and a growing middleclass. RT Briscoe is a resilient company which has come from hard times to emerge stronger. In the near future, the company is expected to consolidate on the gains it has made through the expansion of its areas of operation. Its movement into technical solutions also brings about opportunities in the emerging Power and Telecoms sectors. The Motor car units of Toyota and Ford are expected to receive greater patronage as a result of the growth of the economy. In 2007 the purchasing power of Nigerians is expected to increase and bring with it a new middle class which would be interested in quality vehicles. The improved access to loans from banks will also help sales. Increase in revenue and bottom-lines is also expected from Briscoe Properties as the company's investments in real estate start to fully mature.

ANALYSIS OF FINANCIALS:

Revenue Growth:

RT Briscoe has been able to make a breakthrough in revenue generation following its recent business restructuring and strategic moves. The company recorded a significant leap in gross revenue by 70% to N13.16bn compared to its previous year's sales value of N7.73bn. This represents a 5-year 39.3% growth on Compounded Annual Growth Rate (CAGR) basis. **The improved records in sales could also be attributed to impressive performance of the company's brand new Briscoe Ford which contribution over 10% to its motor business after a year of operations.**

However, it is worth mentioning that the company's revenue base is highly skewed to its motors business division as this accounts for over 92% while the remaining is derived from Atlas Copco generators and construction & maintenance of cell sites for telecoms companies. Meanwhile, with its new strategic diversification into other sectors of the economy, there is an expected balance in the company's earnings structure. This is evident in the comparative analysis of 2005 and 2006 financials which revealed that motor business cornered about 94% of the total earnings as against 92% in 2005.

Profitability/Efficiency:

A review of the current financials of RT Briscoe revealed that the company's performance for the year ended December 2006 was quite commendable as it bears credence to the aftermath effect of its business restructuring exercise embarked upon about three years ago.

Gross profit increased by about 95% in 2006 from N896.8m in 2005 to N1.746bn. Similarly, gross profit margin rose to 13.2% in 2006 from 11.6% in 2005 while Profit After Tax (PAT) leaped significantly by 166% from N199.69bn in 2005 to N531.78bn. In the same vein, operating margin rose from 5.7% in 2005 to 7.3% in 2006 while net profit margin increased from 2.6% in 2005 to 4.0% in 2006

Return on Owners' Equity (ROE) rose from 11% in 2005 to 24% in 2006 while Return on Assets (ROA) employed increased to 12.4% in 2006 from 8.3% recorded in prior year. Further analysis revealed that the surge in ROE was a resultant effect of benefits accruable

from the company's increased leverage. This however affected the equity composition of capital employed as it declined from 66% in 2005 to about 58% on 2006. Furthermore, days in receivables declined from approximately 50 days in 2005 to about 39 days in 2006.

Without losing sight of the characteristic low-margin return of the Automobile/ Trye Industry, one would submit that the company fared better in profitability performance indicators than previous years..

The company's effective management is more prominent from its asset utilisation as its **Asset Utilisation ratio** increased to 3.11 from 2.77 in 2005. Meanwhile, its debt increased by 78% in 2006 from N1.37bn to N2.44bn in 2005.

In terms of cost management, our analysis revealed that RT Briscoe's 2006 enjoyed a good mix of increased revenue drives and cost reduction measures. Expenses ratio declined considerably from 113% in 2005 to 45% in 2006 while total expenses ratio (including finance cost) came down from 69% in 2005 to 16%.

Liquidity/Financial Soundness:

RT Briscoe good performance can also be linked to its improved liquidity status after its recapitalization exercise in 2004. The company's z-score, which is a measure of financial soundness, hovered between 3.02 and 3.57 in 2002 and 2006 respectively. This implies that the company has always been in safety zone.

A z-score in the range of 1.80 and 2.99 is said to portray a high-risk financial zone while 3.00 and above implies a very low risk and safety/comfort zone.

The company however recorded a current ratio of 1.74 and quick ratio of 0.82 (compared to benchmark of 1) in 2006, a lower figure when compared to 2005 figure of 2.19 and 1.27. Though the 2006 figures are very close to the benchmark ratios, the reduction in ratios might be attributed to increased leverage to financing increasing activities of the company in 2006. Increase in debtors and stocks is lower than increase in leverage as

receivables rose only by 48% from N1.185bn in 2005 to N1.759bn in 2006 while its payables grew by 256% to N157m from N44m over same period.

Gearing:

The company seems to maintain a debt-equity capital structure of 42%-58%. It also enjoys cheap funds from trade payables and other payables. Meanwhile, it is worth mentioning that the company enjoys the benefit of leverage as returns to ordinary shareholders increased from 11% in 2005 to 24% in 2006.

We, however, opine that given the increased business expansion and growth opportunities in the focused sectors, embarking on equity financing will be a laudable option thereby making substantial savings from finance obligation which rose from N136m in 2005 to N212m in 2006.

VALUATION:

We have employed a number of valuation metrics in arriving at an appropriate intrinsic value for RT BRISCOE PLC. We used Discounted Cash Flow (DCF) model, Dividend Growth Valuation Method and a couple of relative valuation metrics such as Price to Book Value (P/B), Price to Sales (P/S) and Price to Earnings (P/E) Multiples.

Meanwhile, after attaching appropriate weights to each valuation metric, we are more over weight on DCF and dividend valuation methods as we believe they are better measures of the company's intrinsic value. Subsequently, we arrived at a fair value of N31.41.

TECHNICAL ANALYSIS OF RT BRISCOE: 2004 – 2007.

RT Briscoe until recently has been a 'Sleeping Beauty'. Historically, RT Briscoe used to be a favoured stock in the Nigerian Stock Market.

After the hybrid offer of 2004 which saw RT Briscoe shares at an offer price of N5.00 go for a discount of about 44% below the market price of N7.22, the share price has been

fluctuating between the support and resistance levels of N3.95 and N7.30 until August 2006 when the hitherto highest peak of N7.38 became the lowest trough in recent times.

Ever since, the stock has rallied consistently on the heels of the impressive performance partly attributed to the strategic alliance with Ford Motors (Briscoe Ford) and partly due to strategic change in business model which led to diversification into other sectors of the economy. Lo and behold, the stock reached an all-time high of N32.61 on the close of trading on the March 16, 2007 following a fantastic twin-benefits declaration of 50k and 1 for 4 scrip issue before it was market down on the March 19, 2007.

RT BRISCOE - TECHNICAL CHART



RT BRISCOE (NIGERIA) PLC

KEY STATISTICS -2006 FINANCIALS

Sector - Automobile

NSE Symbol - RTBRISCOE

Valuation Metrics

Trading Information

Market Capitalisation (Nbn)	9.40	Volatility - Beta (β)	0.48
Trailing P/E	17.09	52-Week Change	
PEG Ratio (5 yr expected) (%)	1.07	52-Week High (March 15,2007) (Ngn)	31.06

Price/Sales	0.71	52-Week Low (April 4, 2006) (Ngn)	4.32
Projected Growth Rate in (%)		Trailing Market Price (April 11,2007) (Ngn)	25.90
Financial Highlights		Share statistics	
Fiscal Year End	31-Dec	Average Volume Traded (1 month)	311,819
Most Recent Quarter (mrq)	FY-2006	Average Volume Traded (5 days)	410,899
Profitability		Shares outstanding (million)	363.07
Return on Capital Employed (ROCE) %		Float * (%)	39.79
Return on Equity (ROE) %	24.1	Shareholders above 5%*	%
Return on Assets (ROA) %	20.0	ARM Company Ltd	41.41
Z-Score	3.77	Chief M.Ade Ojo	10.53
Per Share Statistics:		Classic Motors Limited	8.27
Sales Per Share (Ngn)	36.25	* source = December 2006 financial reports	
Tailing Book Value Per Share (Ngn)	6.08	Earnings, Dividend and Bonus Updates	
Trailing Earnings Per Share (Ngn)	1.46	Latest Dividend Per Share (Ngn)	0.50
Latest Dividend Per Share (Ngn)	0.50	Dividend Cover	2.92
Financial Soundness/Liquidity Metrics		Trailing Earnings Yield (%)	5.64
Z-Score	3.57	Last Script Issue	1 for 4
Current Ratio	1.74	Payout Ratio (%)	34.25
Acid Test Ratio	0.82	Declaration Date	6-Mar-07
Operating Cash Flow to Net Income	0.61	Ex-dividend Date	19-Mar-07
Income Statement		Payment Date	27-Apr-07
Revenue (Nbn)	13.16	Balance Sheet	
Operating Profit (Nbn)	2.69	Shareholders Fund(Nbn)	2.21
Profit Before Tax (Nm)	745.27	Shareholders Fund Growth (%)	18.85
Profit After Tax (Nm)	531.78	Total Assets (Nbn)	4.78
Total Expenses(Nbn)	1.08	Total Assets Growth (%)	43%
		Total Liabilities (Ngn)	2.45
		Total Liabilities Growth (%)	73%

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