Delta Half Year Ended 30 September 2015 Analysis

Market Data			
Current Share Price(Usc)			81.07
Shares in Issue			1,244,313,975.00
Market cap(US$)			1,008,765,340.00
YOY high(Usc)			116
YOY Low(Usc)			81
YTD			-20.51%
YOY			-29.50%
EPS			2.89
P/E			10.95
Income Statement	**FY2015**	**FY 2014**	**% Change**
	US$'000	**US$'000**	
Revenue	269,021.00	291,471.00	-7.7%
Operating profit	43,467.00	54,422.00	-20.1%
Profit After tax	35,733.00	43,298.00	-17.5%
Operating margin	16.2%	18.7%	-13.5%
Net Profit margin	13.3%	14.9%	-10.6%
Financial Position			
Total Assets	675,288.00	680,801.00	-0.8%
Total Liabilites	212,133.00	246,881.00	-14.1%
Attributable Equity	463,145.00	424,695.00	9.1%
Cashflows and Ratios			
Cashflows from Operations	46,880.00	53,713.00	-12.7%
Cashflows from Investing	(14,584.00)	(13,317.00)	9.5%
Cashflows from Financing	(30,043.00)	2,561.00	-1273.1%
ROE	7.72%	10.38%	-25.7%
ROA	5.72%	6.93%	-17.4%
Current Assets to CLs	2.98	1.81	65.0%
Total asset turnover	0.40	0.43	-6.9%

Delta Revenue Down 8%

Revenue took an 8% knock to $269million from the previous year due to continued tightening in the operating environment that led to a decline in the revenue contributions from the Group's high margin products that is Largers (-9%) and Sparkling Beverages (-12%). Revenue support came from the Sorghum beer which indicated a 1% increase despite a decline in volumes of 12% due to the premium pricing of Chibuku Super. Shown below is the volume, revenue and operating income of Delta's performance drivers;

	Volume	Revenue	Operating Income
Larger Beer	-2%	-9%	4%
SBs	-13%	-18%	-48%
Sorghum Beer	-12%	1%	-24%

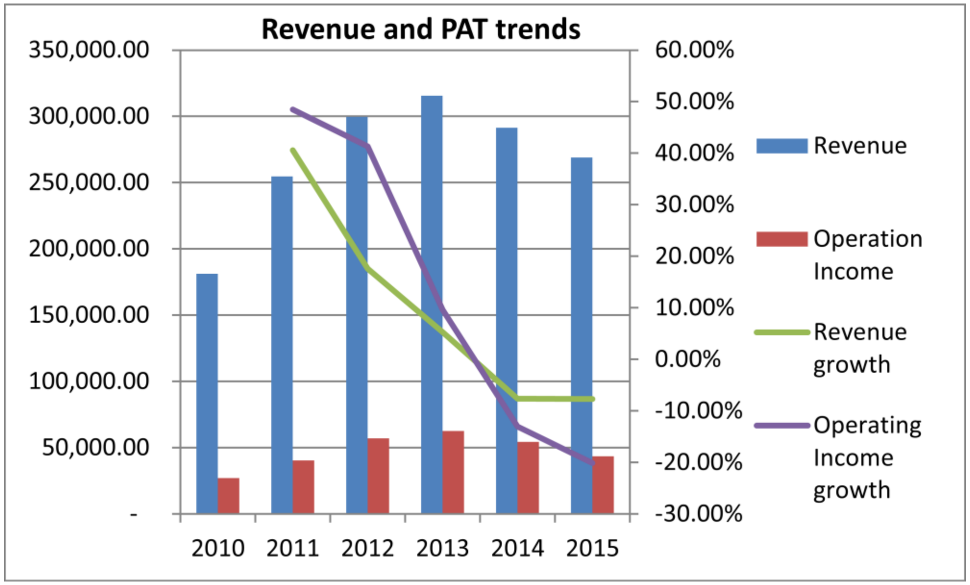
Source: Delta HY 2016 Results

The decline in Larger revenues of 9% was much higher than the decline in volumes sold due to the decrease in the volumes sold of mainstream beer which was then offset by a volume increase in low value beer that is the Eagle brand. Ultimately Largers posted a positive growth in operating income due to effective cost management. Sparkling Beverages had the worst performance on a volume, revenue and operating income basis as they were largely affected by low disposable incomes, increased competition from imported products and highly priced inputs. On the other hand Sorghum beer recorded a 1% increase in revenues despite a 12% drop in volumes due to the premium pricing of Chibuku Super. The product was however not profitable due to the higher costs of logistics as the product had to be freighted from one site. Sorghum beer is however the greatest contributor to the Group's Operating Income (47%)

Operating Profit was down 20% to $35.7 million whilst operating and net profit margins declined by 13.5% and 10.6% respectively.

The decline in net income margin was lower due to lower interest costs and a higher share of associate profits due to the inclusion of Nampak profits.

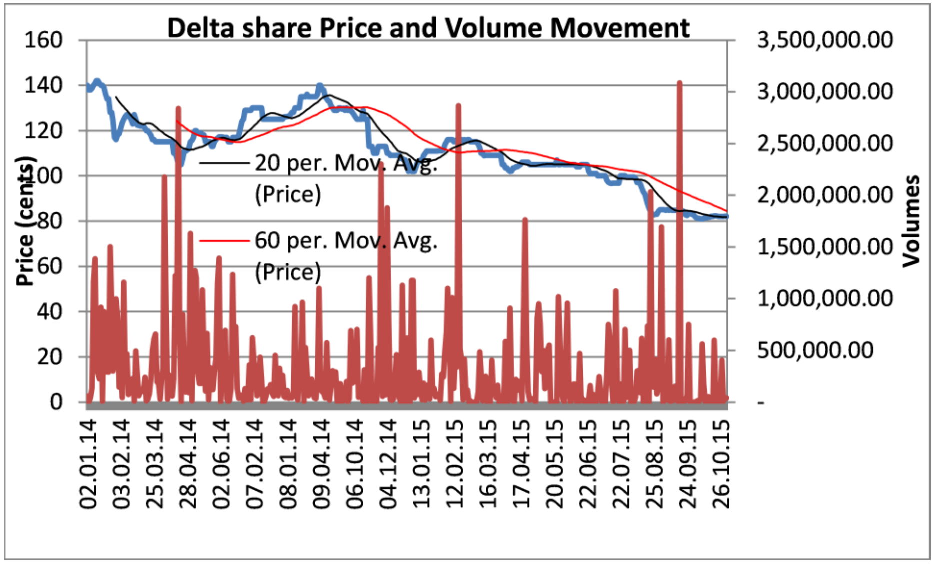
Despite a decline in net cash flow from operations, The Group continues to indicate strong cash flows and good quality of earnings as indicated by the FCO/Net Income ratio of 1.31. The significant change in the cash flows from financing activities was due to the periodic payment of dividends and the absence of any offsetting borrowings in the period under review. The improvement in the liquidity ratio was attributed to the absence of short term borrowings as the business in currently sitting on a cash balance of $135million. EPS was down 19% to 2.89c and the company declared an interim dividend of 1 .4cents per share which gives a dividend cover of 2.1x



Source: Delta Financial Results

The graph indicates a general negative trend in both the revenue and profit after tax growth since 2012. The period under review however shows a stabilization in the revenue growth trend due to the attempts by the company minimise the bleeding in revenues. These attempts have however come at the cost of sacrificing margins which have led to the persistent decline in operating income.

Technical Analysis



The graph indicates a steady decline in the share price of the counter since a peak of 140c in April 2014. The high volume movement in the period under review indicates selling pressure that has forced down the share prices to the current support price of 81c. The short term moving average has been trending below the long term moving average since May 2015 and is currently indicating signs of cutting the long term average from above thus indicating a BUY signal.

Investment case

- The Group continues to record strong cash flows with its balance sheet currently indicating a cash balance of $135.9million. This has eliminated the need to take on short term borrowings and as such the Group boasts of strong solvency ratios and financial strength.
- Despite the decline in earnings, the Group has maintained an attractive dividend payout which is currently 48%.
- Delta is a Market leader in the beverages industry and has managed to maintain market shares in Sorghum and Larger beer.
- The management is continuously active in channeling resources to remain profitable through instituting price cuts to remain competitive, and addition of Chibuku Super plants to increase capacity and production. The Fairbridge plant is now operating at full capacity and

2 more plants are expected to be operational by August 2016.

- Addition of new beer styles to widen product offering of high margin products, to take advantage of changing consumer tastes and to widen revenue streams.
- Positive performance from associate companies, with a particular emphasis on Afdis which continues to record positive growth in volumes, revenues, and profitability. Schweppes has recently launched a new water brand named Bonaqua at competitive prices.
- The size of the company allows it to have strong bargaining power and is currently working with value chain partners to correct input costs.
- Operating and net profit margins remain at attractive levels.
- It is a highly liquid counter.
- It's a bell weather stock whose product demand is highly inelastic despite the competitive pressures from imports.
- Its management team has a good track record and is highly experienced.

Investment Concerns

- Declining volumes across all products due to lower discretionary income among consumers.
- The company's products have a strong correlation with economic performance which is currently depressed. Therefore the company can only do so much to remain competitive and profitable.
- The unrelenting operating environment is slowly seeking to eclipse the significance of Delta mainstream's products like Lagers and SBs leaving it to slowly depend on low margin products like Chibuku.
- The strengthening dollar is increasing pressure for Delta by making imports relatively cheaper and therefore forcing the company to continuously cut prices to remain competitive.
- The stable dividend payout indicates that the company has reached maturity and has limited growth opportunities.
- Power shortages are increasingly disrupting production and product enjoyment by customers as many traders have to go for hours with no electricity.
- Rising license to trade issues with Delta drivers that have resulted in delayed deliveries to traders.

Valuation and Recommendation

We expect revenue support to emanate from the introduction of new beer styles, Larger beer price cuts that were instituted in October, an increase in the distribution fleet and higher Sorghum beer production. However given the increased consumer strain, the continued weakening of the rand against the US dollar together with the declining trend in revenues, we expect a slight reprieve in the negative growth of revenue to -6% in the second half. We expect operating margins to rise to 17% given the cost cutting measures that are being instituted whilst the pretax margin is expected to record a slight increase to 18% given the reduction in finance costs and the good performance from its associate company Afdis. Ultimately an EPS of 5.65c is expected in the full year ended which is 24% lower than the prior period.

Inspite of the lower EPS forecast, Delta remains grossly undervalued in comparison to its regional peers which have an average P/E of 23x owing largely to different operating environments. Three methods where used in the valuation of the counter to come up with a forward fair price of 76.11c per share which is 6% lower than the current price of 81c. We therefore give a **HOLD r**ecommendation as we have a firm belief that despite the current indication of a slight overvaluation at the current prices the counter's strong investment case will lead to a solid recovery upon an economic turnaround.

Method	Price	Weight	Weighted Price
P/E Multiple	131.61	0.33	43.87
NAV per share	40.84	0.33	13.61
Costant Dividend Growth	55.88	0.33	18.63
			76.11