Yale SCHOOL of MANAGEMENT
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Sleeman Breweries
April 23, 2002

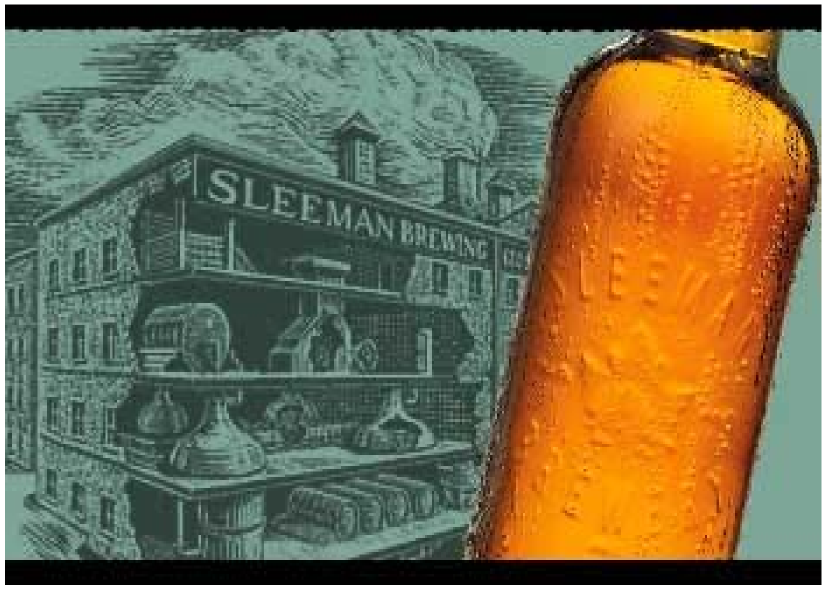
Time Frame – 12 months

Recommendation:

BUY

Types of Recommendations

Buy – 20% undervalued
Hold – Fairly valued.
Sell – 20% overvalued



*"**Cheap** Access to **Rich** Resources!!"*

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% Return over the last 12 months:
(all info as of April 23, 2002)

DJ Brewers and Distillers Index	**28.9%**
TSE 300	**-3.0%**
Russell 2000	**10.8%**
Sleeman Breweries (ALE on TSE)	**71.0%**
Current Share Price (CAD)	**$12.00**
Target Share Price	**$16.32**
Implied Return	**36.0%**

Sleeman Breweries – "Cheap Access to Rich Resources".

Recommendation: BUY

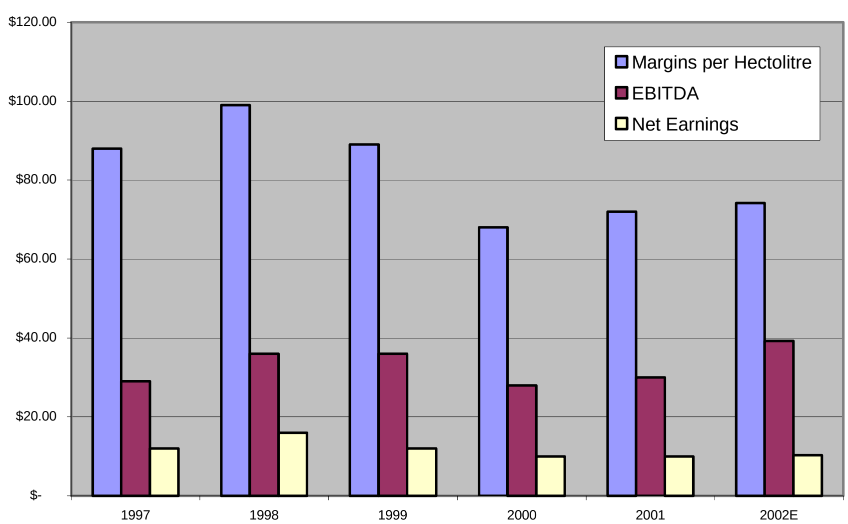
- **Leveraging synergies to create new international agreements**
- **Access to coveted North American markets**
- **New management underscores international outlook**
- **Long term acquisition target at a premium price**
- **Minimal risk in a mature industry, TSE as a whole 20% discounted**

Historical

- Sleeman is the third largest brewery in Canada. The company focuses on the premium and value sectors of the beer market. Similarly to the US market, two large breweries, Molson and Labatt, which together supply 90% of the market, dominate the Canadian market. Sleeman, as a third place player, is unlikely to be usurped or the make any material gain on Molson or Labatt and currently has 5% of the total market.

- Sleeman consolidated its position via an acquisition strategy throughout 1999-2001, acquiring Canada's regional brewing and distribution assets and bringing them under its umbrella. Sleeman successfully created synergies between these companies to increase production margins and gain market share in the Canadian premium and value sectors. The company has just started activities in the US, and distributes Sam Adams in Canada for the Boston Beer Company.

Margins per Hectolitre



- In 3Q 1999, Sleeman acquired Stroh-Canada and entered the value priced market, which led to a 47% sales increase in 2000. The large-scale acquisition was not seamlessly integrated and Sleeman saw a drop in their margins. Management was able to turn this around relatively quickly and by 2001, margins had improved, although not to the level before entering the value-priced segment. We believe that Sleeman is operating more efficiently, and expect to see improvements in margins over the next few years (please see DCF analysis for a better explanation). Management and other industry analysts are bullish on increased operating margins. In addition, we feel that increase in marketing and operating test markets in the US will exert some resistance to net income margins per hectoliter limited.

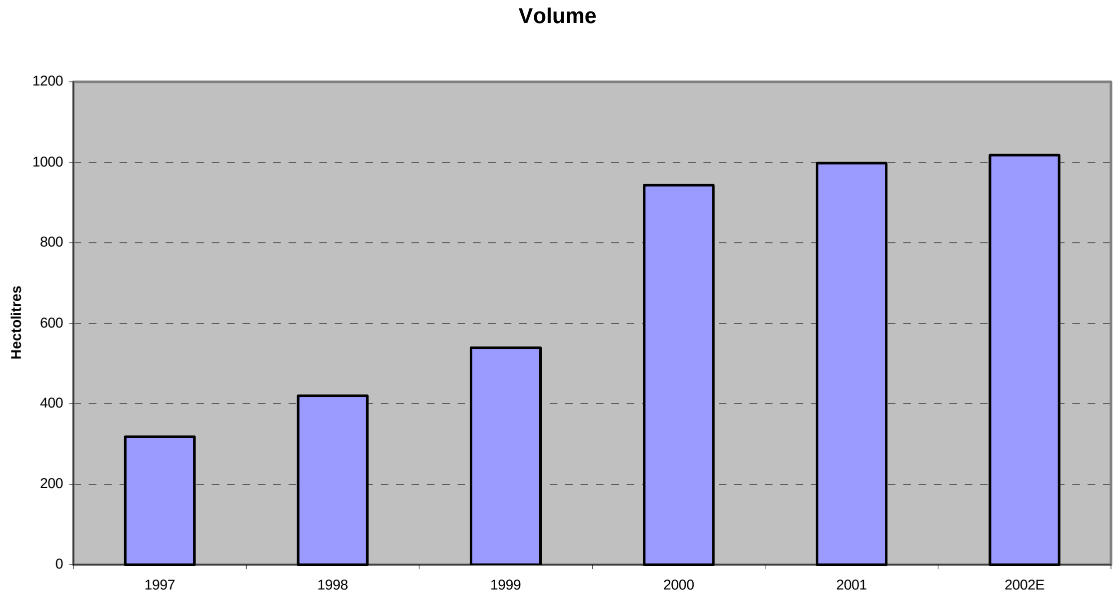
A Winning Business Strategy

- Sleeman has consolidated a large portion of the Canadian premium beer market and the question becomes "what next?". Sleeman does not have excess capacity, but does have the ability to efficiently increase capacity at several breweries. A strategy that the company is implementing is to continue its acquisition campaign and to expand existing facilities to build capacity, which can be leased to international strategic partners. Having capacity to produce foreign brands for the US and Canadian markets combined with Sleeman's in-house Canadian distribution system should lead to lucrative international agreements and in the long term, a premium acquisition price. **We are bullish on this strategy because the US and Canadian import markets are the fastest growing segment of the beer markets and importers are seeking brewing capacity to capture that trend; consolidation is happening on a global scale.**

- Sleeman actively courts importers and currently has representation and distribution agreements with Boston Beer Company, Scottish & New Castle, South African Breweries, and H.P Bulmer. In 2001, 1% of revenue was derived from these agency representation agreements, (agency brand fee), and based on management aggressive pursuit of these agreements, we expect that number to increase to 3% in 2002. Also, Sleeman is forging reciprocal agreements with international players to export Sleeman into new markets.

Growth

- The revenue growth target used in the DFC model is 7% for the next six years and 4% thereafter. We believe the 7% growth rate can be achieved by 4% increase in Canadian beer sales and a 3% revenue increase will be driven by agency licensing agreements and expansion in the US market. The 4% sales increase is a combination of a price increase and a minimal volume increase. To achieve this increase in growth does not require much movement between firms, Molson and Labatt will still have dominant combined market share of 88%. From 2000 to 2001, Sleeman achieved a total volume increase of 3%, a 7% net revenue increase, and a 6% operating profit increase, which helped to achieve a 9% rise in net income. We believe that in the next six years Canadian sales volume and operating profit will increase at a smaller rate then in 2001.



- The company has set a target of gaining 6%, and additional 1%, of the Canadian beer market by 2004. We believe this is possible given the trend in premium beer sales and will be captured via organic growth and continued acquisition. Sleeman stepped up the marketing of its core Sleeman brand in the Ontario market, adding at least $2.5 million to its advertising budget in 2001, supplemented by an expanded direct sales force. We expect the aggressive marketing campaign to contribute to a portion of the increased sales.

- Sleeman is well placed to capture part of the growing Canadian import market as a result of its extensive home grown Canadian distribution system. Sleeman is represented in all regions and territories in Canada and is a good alternative to those unable or unwilling to partner with Labatt or Molson. **Sleeman offers a cheap and strategic entry into the North American market.**

- In 2001 Sleeman entered the US market on a test basis and has proved successful in gaining a portion of the growing import segment in the US (see Strange Brew Industry Report April 17, 2002). Sleeman has been especially successful in the Midwest (Minneapolis) and to a lesser extent in the New England. 2002 test markets will continue with full roll out expected in 2003, if the results continue at their current levels**. The US market is ten times the size of the Canadian market; therefore even a modest market share can have a large effect on Sleeman's sales**. Full analysis of test market performance is not available, however, we believe the reciprocal agreement with Boston Beer Company and the relationship Sleeman has with City Brewing based in Wisconsin where it leases production facilities, are positive signals for a successful US rollout.

Sleeman Breweries – "Cheap Access to Rich Resources".

Management Underscores Commitment to International Scope

- The new President and COO of Sleeman was recently appointed this April. David Meyers took the position after leaving Remy Amerique, the US distribution arm of wine and spirits company Remy-Cointreau, which under his leadership, became the fastest growing importer of spirits into the US market. While this change in leadership may indicate that the company is not up for sale (the out-going COO would have stayed for a lucrative exit package) we feel that Meyer's strong international background is a signal that Sleeman is looking toward courting international agreements and aggressively pursuing reciprocal export agreements. Meyers understanding of the US beer distribution and sales market also bodes well for Sleeman's expansion into the competitive and lucrative US market.

- John Sleeman is Chairman of the company and it isn't until recently that there have been indications in the press and annual accounts that John Sleeman is interested in anything more then a 'mom and pop shop'. The hiring of Meyers, as well as a change in the strategy indicated in the annual accounts; give a strong indication that Mr. Sleeman recognizes the opportunity for global partnerships and further industry consolidation.

Attractive Buyout

- Sleeman is an attractive acquisition target for foreign companies looking for an entrance to the North American market at a relatively low price and multiple. While management does not seem willing to sell immediately, in the long term, the company has indicated it understands the dynamics of consolidation. Additionally, the controlling stake of the company is not in the hands of management, therefore a hostile take-over would be a possibility. Any take-over bid would likely be at a premium to the market, given the access Sleeman provides to the North American beer market. Our implied transaction value for Sleeman, which is based on the latest year-end results, indicates a value of between $12 and $13 per share. This value is based on transaction multiples (EV/Sales, EV/EBIT) complied from all world markets, and we feel **a higher multiple would be justified for a North American company, which we discuss in detail later in the valuation section of this report.**

Added Incentives

- The beer industry overall is mature. One factor of interest in this industry for portfolio managers is the low correlation to general economic performance (for instance Sleeman's low raw beta of 0.34). This industry represents a good diversification pick. An investment in Sleeman brings the added option of investing in a company that will exhibit above average industry growth in the near future.

- In addition, Canada historically trades at a 20% discount to the US market. In the long term, the two markets may converge. We have done our analysis with the assumption that the Canadian discount will apply in the investment horizon.

Debt Load

- When one first looks at Sleeman's balance sheet and compares it to its peers one area sticks out, the company's debt/equity ratio, which is currently 1.2 and is a result of the company's acquisition spree in recent years. However, there is little need for a potential investor to panic as the company has a high interest coverage ratio of 3 and is looking to pay down principal over the coming years with its expected strong and consistent cash flows.

Sleeman Breweries Valuation – Conservative, Robust and Convincing!!!!

- In our analysis we employed three valuation methods to arrive at our target share price of 16.35; discounted cash flow, comparable company analysis and transaction analysis.

	Implied Share Price
Discounted Cash Flow	19.93
Comparable Companies	16.37
Transaction Analysis	12.66
Average	16.32

Discounted Cash Flow (please see exhibit 1)

- For our DCF we used conservative revenue growth rates of 7% for the next six years and a 4% terminal growth value, just above the overall economy. (See "Growth" section above). Gross margins have recently slid from 50% in 1999 to 47% in 2001 as a result of incorporating recently acquired assets into the overall organization. We expect the gross margins to recover to just above their 1999 levels at 51%. In fact, further efficiency could be achieved.

- As for the operating expenses, Sleeman's has been reducing operating expenses to 27% of sales in 2001 from 30% in 1999. A large part of this decrease is attributable to coordinated marketing and advertising focus among the newly acquired breweries and brands and general economies of scale from increasing their size from coast to coast in Canada. As the company realizes even more efficiencies from recent transactions and from growth in the licensing area, which has a minor impact on operating expenses, we expect this portion of the income statement to fall to around 23% of sales. Since the company has relatively new operations throughout the country we see capital expenditures tailoring off in the near-term. However, in order to provide for future expansion plans with production foreign brands into the US we have used a conservative capex to sales ratio of 8%.

Comparable Company

- In our comparable companies analysis we looked at only three North American pure play brewers with mid to small market caps. This search gave us three competitors/comparables; Boston Brewing Company, Adolph Coors and Molson. On average, these companies trade at a significant P/Sales, P/EBITDA and a P/E premium to Sleeman. Although some might try and justify this premium by comparing Sleeman's size to its competitors they would be missing the bigger picture, which is Sleeman has more growth potential than any of these other companies in the coming years, due to its unique position to take advantage of licensing agreements in North America.

				Trading Range		Price/		
Company Name	**Ticker**	**Stock Price**	**Market Cap (million)**	**52 Wk High**	**52 Wk Low**	**Sales**	**EBITDA**	**Earnings**
Mid-Cap								
Coors	RKY	66.54	2,410	67.75	42.65	1.03	8.86	20.42
Molson	MOL.A	21.76	2,075	22.40	12.89	1.83	9.91	16.67
Small-Cap								
Boston Beer	SAM	14.24	229.4	18.16	8.56	1.24	12.60	42.05
				Average		1.37	10.46	26.38
Stock price is as of April 23, 2002				**Implied Value**				
				Sleeman Breweries		13	19	17
				Average	16.37			
				Based on year end results.				

Transaction Analysis

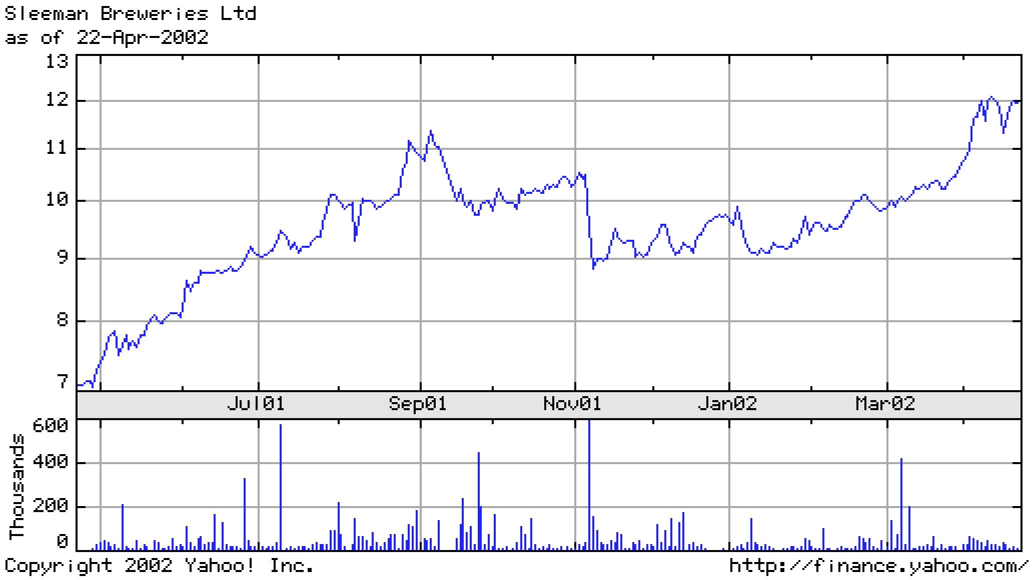
- In order to try and satisfy the takeover premium element, which should be reflected in Sleeman's stock price our group decided to incorporate transaction analysis valuation multiples in our analysis. The data was from a recent CIBC World Markets and looked at select large cap acquisitions of various target sizes over the last year and a half. To our surprise this analysis produced lower multiples that can be seen in the stock prices of most brewing industry participants currently. Although we did use these multiples to be conservative by giving our target share price a wider breadth of perspective, we feel that these valuations could actually be a little higher. For instance, the transaction analysis did not include any data past December 31, 2001 and the industry as a whole has been increasing in multiple value since then. Also, not one of the targets was a North American Brewer and these companies have higher multiples because of their natural access to the industries crown jewel; the American consumer.

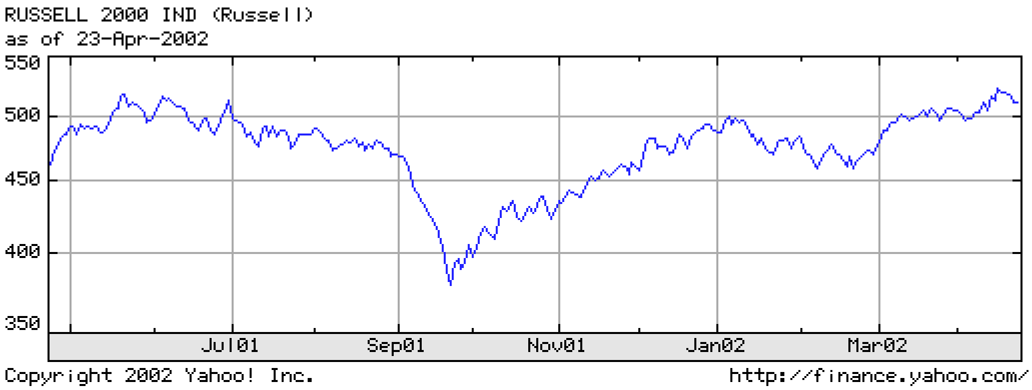
	EV/Sales	**EV/EBITDA**
High	3.1	13.0
Median	2.0	9.7
Low	0.5	6.6
Average	1.7	9.9
Sleeman Breweries		
EV	287,274	275,984
Less Debt	*87,996*	*87,996*
Equity	199,278	187,988
Shares O/S	15,297	15,297
Implied Share Price	13	12

Canadian Discount

- In both the DCF and comparable company analysis we tried to represent a Canadian discount factor in both methods. In our DCF's WACC we took into account the fact that Sleeman exists in a capital markets structure that is not as liquid as the US with the company's cost of debt and equity, respectively. As for the comparable company analysis we made sure to have one-third represented by Molson, another Canadian company.

Stock Graphs





Sleeman Breweries - Discounted Cash Flow Analysis

Exhibit 1

Canadian Dollars(000's)

					For the periods ending December 31,					
		1999	**2000**	**2001**	**2002E**	**2003E**	**2004E**	**2005E**	**2006E**	**2007E**
Revenues	$	96,111	134,439	143,637	153,692	164,450	175,962	188,279	201,458	215,560
% growth rate		*N/A*	*40%*	*7%*	*7%*	*7%*	*7%*	*7%*	*7%*	*7%*
Total revenues		96,111	134,439	143,637	153,692	164,450	175,962	188,279	201,458	215,560
COGS		48,157	70,082	75,937	75,309	80,581	86,221	92,257	98,715	105,625
Gross Profit		47,954	64,357	67,700	78,383	83,870	89,740	96,022	102,744	109,936
Gross Margin		*50%*	*48%*	*47%*	*51%*	*51%*	*51%*	*51%*	*51%*	*51%*
SG&A		28,407	37,894	39,248	38,423	41,113	42,231	45,187	46,335	49,579
		30%	*28%*	*27%*	*25%*	*25%*	*24%*	*24%*	*23%*	*23%*
EBITDA	**$**	**19,547**	**26,463**	**28,452**	**39,960**	**42,757**	**47,510**	**50,835**	**56,408**	**60,357**
Cash Taxes **41%**		7,936	10,744	11,552	16,224	17,359	19,289	20,639	22,902	24,505
Changes in Working Capital			(4,445)	(29)	-	-	-	-	-	-
Capital Expenditures		9,266	11,433	12,677	12,295	13,156	14,077	15,062	16,117	17,245
as a % of revenue		*10%*	*9%*	*9%*	*8%*	*8%*	*8%*	*8%*	*8%*	*8%*
Free Cash Flow to the Firm	$	2,345	(159)	4,194	11,441	12,242	14,144	15,134	17,390	18,607
as a % of revenue		*2%*	*0%*	*3%*	*7%*	*7%*	*8%*	*8%*	*9%*	*9%*
Terminal Value										**521,814**

Enterprise Value of the firm	**$**	**392,836**
Less: Debt		*87,996*
Equity Value		**304,840**
Shares Outstanding (000's)		15,297
Share Price	**$**	**19.93**

Notes

(1) *Despite 2-3% historical growth rate, Sleeman's focus on licensing agreements of importers and its entrance into the US market indicate a 7% growth rate over the next 6 years. A 4% terminal growth rate was assumed starting in year 2008.*

(2) *Increased efficiencies from operations in the near term, as a result of more integration, will increase gross margins.*

(3) *We expect working capital to remain unchanged despite firm growth because of greater efficiencies an increase in the portion of income derived from licensing agreements.*

(4) *Free cash flow margins will increase as are a result of all the above expected improvements and the general efficiency of the company*

Notes & Assumptions:

Revenue growth rate is based on			**7%**	
COGS	**49%**			
SG&A		**25%**		
Capital expenditures		**8%**		
Cost of debt.		**7%**		
Cost of equity.		**8%**		
Debt/BV of Equity	**Target**	**1.00**	**1.20**	**Current**
WACC		**8%**		
Terminal growth		**4%**		

Capital Structure As of December 31, 2001	
Short-term debt	16,063
Long-term debt	71,933
BV of Equity	73,088

Capital Asset Pricing Model	
10 year rate	5%
Beta	0.54
Equity Premium	5%
Beta unlevered	0.34

*Levered Beta formula:= {1+(1-T)B/S}*Beta-Unlevered.*

Disclaimer

Important Disclaimer

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