Dangote Cement Plc

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Nigeria | Equities | Industrial Goods | November 8, 2019 — PAC RESEARCH

FX Loss and Sales Promotion Expenses Weigh on Impressive Q3 Performance

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Price:	
- Current	**₦145.80**
- Target	**₦202.84**
Recommendation:	**BUY**

** As at Friday November 8, 2019*

INVESTMENT SUMMARY

The total cement volumes sold by Dangote Cement in nine-month to September 2019 increased slightly by 1.07% to 17.96 million tonnes (vs. 17.77million reported in nine-month to September 2018). However, the increase in volume did not translate to higher revenue as total group revenue fell marginally by 0.80% to ₦679.79 billion in 9M'19 (vs. ₦685.29 billion in 9M'18). The marginal fall in the group revenue can be mainly attributed to the lower revenue from Pan-African operations as most currencies lost value against the Naira. This resulted in reduced net prices when the sales in local currencies were converted to Naira. In general, the group manufacturing costs increased slightly by 0.81% to ₦290.02 billion in 9M'19 (vs. ₦287.68 billion in 9M'18), as a result of inflationary pressures in the Nigeran home market. General administration costs remained broadly flat at ₦38.36 billion in 9M'19 (vs. ₦38.11 billion in 9M'18), while selling expenses increased by 25.56% to ₦121.98 billion (vs. ₦97.15 billion in 9M'18). Consequently, EBITDA fell by 10.10% to ₦303.22 billion in 9M'19 (vs. ₦337.30 billion in 9M'18).

The non-operating performance of the company was poor, reflecting in higher net finance costs of ₦33.80 billion in 9M'19 (vs. net finance cost of ₦19.50 billion in 9M'18). With unimpressive overall performance, profit before tax fell by 20.09% to ₦197.68 billion (vs. ₦247.36 billion in 9M'18). On the back of tax exemptions on three production lines in Nigeria, the company made a lower provision of ₦43.33 billion for tax (vs. ₦89.09 billion in 9M'18) and this led to a marginal fall of profit after tax, as it fell by 2.48% to ₦154.35 billion in 9M'19 (vs. ₦158.28 billion in 9M'18). However, the company's 12-month trailing EPS rose by 85.41% to ₦22.67, from ₦12.23 recorded in the previous period. We downgrade our target price per share to ₦202.84 (Previous Target Price: ₦214.44) and maintain a **BUY** recommendation on the company shares.

Fig. 1: Quarterly results highlights

	3Q2019	2Q2019	3Q2018	Q/q Δ	Y/y Δ
Revenue (₦'mn)	212,061	227,573	202,851	-6.82%	+4.54%
Op. Profit (₦'mn)	60,986	82,114	66,343	-25.73%	-8.07%
Net profit (₦'mn)	35,110	58,986	45,113	-40.48%	-22.17%

Source: NSE, Bloomberg, PAC Research

Fig. 2: Stock data

FYE	December
Price Mov't: YtD / 52wk	-23.14%/-28.88%
52-week range	₦136.10- ₦215.00
30-day Average vol.	5,175,181
Shares Outstanding ('mn)	17,040.51
Market Cap. (₦bn)	2,484.51
EPS (₦) - 12months trailing	22.67
DPS (₦) - FY2018	16.00

Source: NSE, Bloomberg, PAC Research

Fig. 3: Key ratios

	9M'19	9M'18
Gross profit margin	57.34%	58.02%
Net profit margin	22.71%	23.10%
Equity multiplier	1.92x	2.17x
Asset turnover	0.41x	0.40x

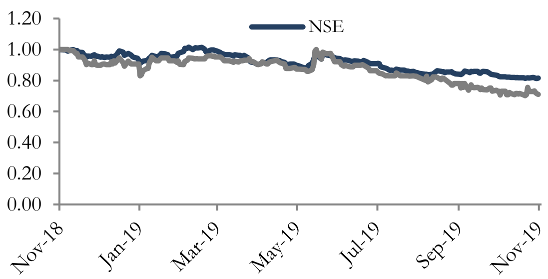
Source: NSE, PAC Research

Fig. 4: Valuations

	FY2017	FY2018	FY2019E	FY2020F
P/E	12.16x	6.37x	12.05x	10.23x
P/B	3.18x	2.52x	2.62x	2.60x
Div Yield (%)	7.20	10.97	7.54	8.57
Pay-out Ratio	87.60%	69.85%	90.89%	87.71%
EV/EBITDA	6.97x	6.12x	6.63x	6.01x
Ev/Revenue	3.36	2.96	2.99	2.88
Sales Per Share	47.27	52.89	53.15	55.28
P/S Ratio	3.08	2.76	2.74	2.64

Source: NSE, PAC Research

Fig. 5: DANGCEM vs NSE, 52-wk Movement (Rebased)



Source: Bloomberg, PAC Research

Revenue falls slightly by 0.80% despite the increase in cement volume: In nine-month to September 2019, total cement volumes sold by Dangote Cement across the group increased marginally by 1.07% to 17.96 million tonne (vs. 17.77 million tonne in nine-month to September 2018). Total volume sold in Nigeria remained almost flat at 10.82 million tonnes in 9M'19 (compared with 10.76 million tonnes in 9M'18), while Pan-African cement volumes increased by 1.68% to 7.14 million tonnes in 9M'19 (vs. 7.03 million tonnes sold in 9M'18). The increased cement volume sold in Pan-Africa can be mainly attributed to higher volume in Tanzania, Sierra Leonne and Senegal, which were partially offset by lower cement demand in South Africa and Ghana.

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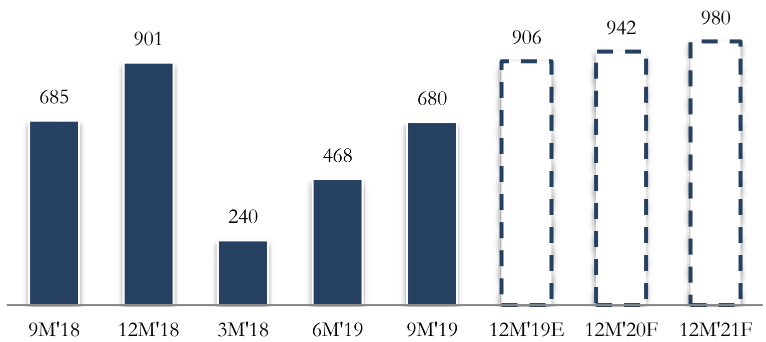
However, the increased cement volume across board did not translate to higher revenue for the group as overall revenue fell slightly by 0.08% to ₦679.79 billion in 9M'19 (vs. ₦685.29 billion in 9M'18). Revenue in Nigeria declined by 0.73% to ₦467.88 billion in 9M'19 (vs. ₦471.33 billion in 9M'18) and this can be partly attributed to the discount sales from the on-going promo in Nigeria. Pan-African revenue fell by 0.52% to ₦213.20 billion in 9M'19 (vs. ₦214.31 billion in 9M'18), due to loss of value of most Pan-African currencies against Naira and this resulted in reduced net prices when sales in local currencies of Pan-African operations were converted to Naira.

Fig. 6: Revenue – 9M'18-12M'21F (Billion NGN)



Source: NSE, Bloomberg, PAC Research

Group manufacturing costs rise by 0.81% year-on-year due to inflationary pressures in Nigerian home market: In general, the manufacturing costs of the company increased by 0.81% to ₦290.01 billion in nine-month to September 2019 (vs. ₦287.68 billion in nine-month to September 2018), mainly as a result of inflationary pressures in the Nigerian home market. Although, total cement volumes sold in Nigeria remained relatively flat in 9M'19 when compared with the corresponding period of the previous year, manufacturing costs increased by 8.60% to ₦140.40 billion (vs. ₦129.30 billion in 9M'18) due to general increase in the prices of inputs during the period.

However, Pan-African manufacturing costs declined by 5.60% to ₦149.60 billion in nine-month to September 2019 (vs. ₦158.40 billion recorded in nine-month to September 2018), mainly as a result of lower sales in Ghana and South Africa.

The administrative expenses of the company remained broadly flat at ₦38.36 billion in 9M'19 (vs. ₦38.11 billion in 9M'18). However, selling and distribution expenses increased significantly by 25.56% to ₦121.98 billion in 9M'19 (vs. ₦97.15 billion in 9M'18), due to higher haulage expenses and higher promotion & advertisement expenses. Although the volume sold in Nigeria remained relatively constant in 9M'19, there was an upsurge in the percentage of sales distributed by trucks to customers, as opposed to sales by self-collection in the previous years. In addition, sales promotion schemes, which drove up the selling and distribution cost up in Nigeria in the third quarter of 2019, contributed to the increase in aggregate selling and distribution expenses.

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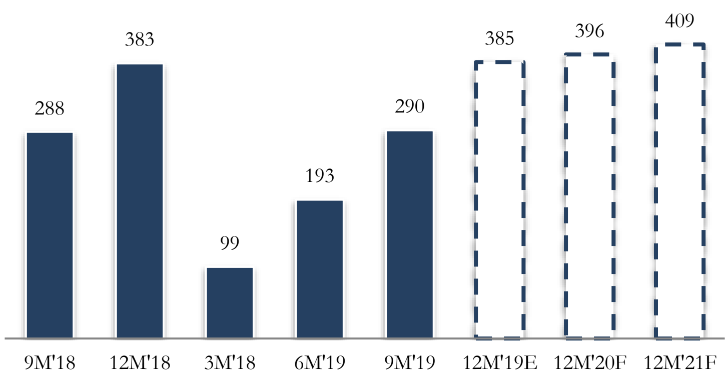
Fig. 7: Manufacturing Costs – 9M'18-12M'21F (Billion NGN)



Source: NSE, Bloomberg, PAC Research

Tax exemption benefits lessen the impact of unimpressive operating and non-operating performance of the company on the bottom line: During the period under review, non-operating performance was poor as net finance cost increased significantly by 73.38% to ₦33.80 billion in 9M'19 (vs. ₦19.50 billion in 9M'18). The higher net finance cost can be mainly attributed to the foreign exchange losses in Pan-African operations. With unimpressive operating and non-operating performances, profit before tax declined significantly by 20.09% to ₦197.68 billion 9M'19 (vs. ₦247.36 billion in recoded in 9M'18).

However, the tax exemption benefits on Ibese Production Line 3 & 4 and Obajana Production Line 4 of Nigerian operations lessened the effects of overall unimpressive performance of the company on the bottom-line.

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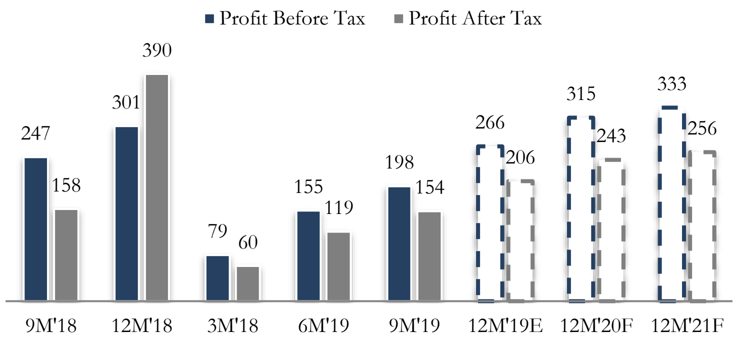
This translated to lower tax effective rate (ETR) of 22.00% in 9M'19 (vs. 28.00% ETR in 9M'18) as the company made a lower provision of ₦43.33 billion for tax (vs. ₦89.09 billion in 9M'18). Consequently, profit after tax fell modestly by 2.48% to ₦154.35 billion in 9M'19 (vs. ₦158.28 billion in 9M'18).

Fig. 8: Profit before Tax and Profit after Tax – 9M'18-12M'21F (Billion NGN)



Source: NSE, Bloomberg, PAC Research

Balance sheet remains strong and solid; Expectation of impressive dividend payment in FY'19: In the third quarter of 2019, the balance sheet position of Dangote Cement remained strong and solid, which reflected in lower total liabilities during the period. The total liabilities of the company fell significantly by 13.77% to ₦0.79 trillion in Q3'19 (vs. ₦0.91 trillion recorded in Q3'18), due to significant reduction in deferred tax liabilities, lower financial liabilities, reduced current tax payables and trades & other payables. However, total assets of the company fell by 3.03% to ₦1.64 trillion in Q3'19 (vs. ₦1.70 trillion in Q3'18), due to lower bank & cash balances, reduced trade & other receivables and lower prepayments & other current assets. Consequently, the net assets of the company rose by 9.50% to ₦0.86 trillion in Q3'19 (vs. ₦0.78 trillion achieved in Q3'18). This translated to a net asset per share of ₦50.27 (vs. ₦45.91 in Q3'18). With solid balance sheet position and expectation of improved revenue in the last quarter of the year, we presume the company to pay at least a dividend of ₦11.00 per share in the full year of 2019.

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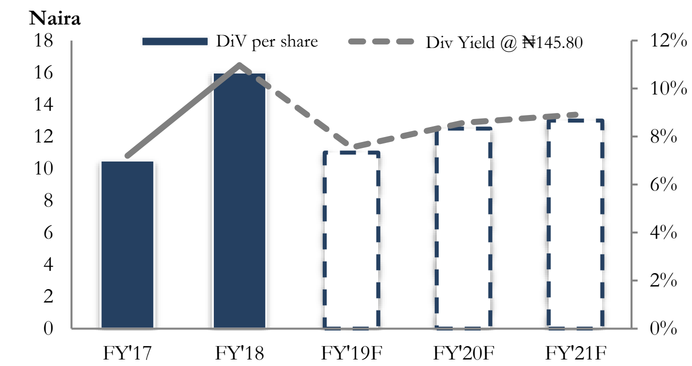
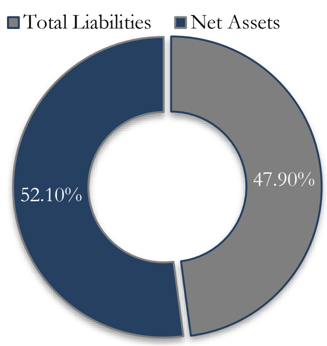
Fig. 9: Dividend Per Share and Dividend Yield (FY'17-FY'21F)



Source: NSE, PAC Research

Fig. 10: Total Liabilities Vs Net Asset in Q3'19



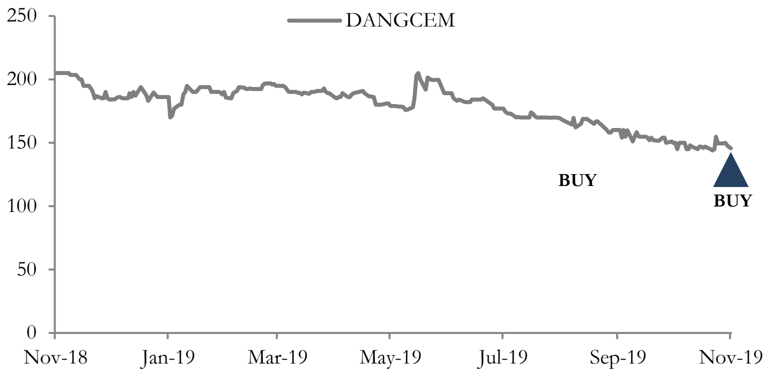
Source: NSE, Bloomberg, PAC Research

Valuation

Our valuation puts the target price of the stock at ₦202.84, representing an increase of 28.12% from the current price of ₦145.80. In arriving at the target price, we employed Discounted Cash Flow valuation methodology. Consequently, we maintained a **BUY** recommendation on the stock of the company. Our valuation and forecasts considered several factors (both quantitative and qualitative) among which are; the previous financial reports of the company, the current figures released by the company, higher cement prices and the performance of the company in the cement industry.

Our valuation puts the target price of the stock at N202.84, representing an increase of 28.12% from the current price of N145.80.

Fig. 11: Share Price History (Naira)



Source: NSE, PAC Research

Fig. 12: Statement of Profit or Loss, N'mn

	2017	2018	2019E	2020F
Revenue	805,582	901,213	905,719	941,948
Change		*11.87%*	*0.50%*	*4.00%*
Cost of Sales	(351,290)	(383,311)	(384,931)	(395,618)
Change		*9.12%*	*0.42%*	*2.78%*
Gross Profit	291,287	454,292	517,902	520,788
Change		*55.96%*	*14.00%*	*0.56%*
SG&A	(155,297)	(189,426)	(212,844)	(205,345)
Change		*21.98%*	*12.36%*	*-3.52%*
Other Income	5,213	10,222	5,434	10,361
Change		*96.09%*	*-46.84%*	*90.67%*
Operating profit	304,208	338,698	313,379	351,347
Change		*11.34%*	*-7.48%*	*12.12%*
Finance Income	35,926	11,323	7,246	11,303
Change		*-68.48%*	*-36.01%*	*56.00%*
Finance Cost	(52,711)	(49,778)	(54,521)	(47,266)
Change		*-5.56%*	*9.53%*	*-13.31%*
Profit Before Taxation	289,590	300,806	266,104	315,384
Change		*3.87%*	*-11.54%*	*18.52%*
Taxation	(85,342)	89,519	(59,873)	(72,538)
Change		*-204.89%*	*-166.88%*	*21.15%*
Profit After Taxation	204,248	390,325	206,230	242,845
Change		*91.10%*	*-47.16%*	*17.75%*

Fig. 13: Statement of Financial Position, N'mn

	2017	2018	2019E	2020F
Fixed Assets	1,192,140	1,171,864	1,188,303	1,191,564
Intangible assets	6,355	5,969	6,103	6,348
Deffered tax assets	30,625	40,622	38,946	40,504
Inventories	94,594	106,998	104,158	108,324
Trade and other recievables	30,155	44,468	36,229	37,678
Bank and Cash Balances	168,387	166,896	108,686	113,034
Total current assets	303,164	428,838	378,242	393,371
Total Assets	1,665,883	1,694,463	1,666,483	1,687,382
Trade and other payables	270,721	230,970	226,430	230,777
Current tax payable	63,901	9,223	22,643	23,549
Financial debt	144,783	220,128	198,896	206,852
Other current liabilities	41,071	35,185	39,399	40,975
Total current liabilities	520,476	495,506	488,273	503,000
Deferred tax liabilities	116,898	83,350	81,515	83,833
Net Assets	781,360	986,613	947,704	955,959

Fig. 14: Profitability Ratio

	2017	2018	2019E	2020F
Return on Equity	26.14%	39.56%	21.76%	25.40%
Return on Assets	12.26%	23.04%	12.38%	14.39%
Gross margin	56.39%	57.47%	57.50%	58.00%
EBITDA margin	48.18%	48.30%	45.17%	47.87%
PBT margin	35.95%	33.38%	29.38%	33.48%
Net Profit Margin	25.35%	43.31%	22.77%	25.78%

Fig. 15: Asset Utilization

	2017	2018	2019E	2020F
cash/sales	0.21	0.19	0.12	0.12
Sales to inventory (x)	8.52	8.42	8.70	8.70
Sales to total assets (x)	0.48	0.53	0.54	0.56
Sales to total fixed assets	0.68	0.77	0.76	0.79
Equity multiplier	2.13	1.72	1.76	1.77
fixed asset turnover	1.48	1.30	1.31	1.27

Fig. 16: Liquidity Ratios

	2016	2017	2018E	2019E
Quick ratio	0.61	0.65	0.56	0.57
Current ratio	0.79	0.87	0.77	0.78
Cash ratio	0.32	0.34	0.22	0.22
Interest Coverage	5.49	6.04	4.88	6.67
Operating Cash Flow Ratio	1.44	1.81	2.06	1.94
Debt/net income	1.28	0.78	1.36	1.20
Debt/operating cashflow	0.35	0.34	0.28	0.30
Debt to asset	0.53	0.42	0.43	0.43
Total liabilities/equities	1.13	0.72	0.76	0.77
Inventory turnover	5.45	3.57	2.96	2.89
Inventory turnover days	67.00	67.00	67.00	67.00
Account payable days	211.00	211.00	211.00	211.00

Fig. 17: Shareholders' Investment Ratios

	2017	2018	2019E	2020F
EPS (₦)	11.99	22.91	12.10	14.25
DPS (₦)	10.50	16.00	11.00	12.50
NAVPS (₦)	45.85	57.90	55.61	56.10
Earnings yield (%)	8.22%	15.71%	8.30%	9.77%

Source: Company's Annual Reports, PAC Research

Equity research methodology employed in this report

Views documented in this equity research report stem from conclusions reached through the use of multiple valuation methodologies, industry-wide knowledge, company specific information and our near to medium term expectations of industry and company performance, as well as market outlook. Our forecasts are based on a combination of top-down and bottom-up analysis, alongside historical trends in industry and company financials. Where appropriate, we factored in available forecasts and business direction provided by company management.

Our recommendation tends towards value investing. Therefore, our investment rank gauge—a customized scale we use to judge how well a firm under coverage has performed—is determined using major value parameters as well as relevant ratios and multiples computed with figures from the company's most recent financials.

The variables used to arrive at the company's investment rank cover a wide range of measures which characterize liquidity, operational efficiency, profitability, profit margins, growth, economic viability, gearing, relative valuation ratios, capital structure and management performance. Our investment recommendation is underpinned by the upside or downside potential of a stock under coverage. This potential is estimated by comparing the stock's current market price to its price target and fair value, on a percentage increase or decrease basis as summarized below:

Deviation from current price	Recommendation
>30%	STRONG BUY
10% to < 30%	BUY
-10% to < 10%	HOLD
<-10%	SELL

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