Dangote Cement Plc

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Nigeria | Equities | Industrial Goods | July 29, 2020 — PAC RESEARCH

Resilient Performance amidst COVID-19 Challenges

Oluwole Adeyeye
oluwole.adeyeye@panafricancapitalholdings.com

Price:	
- Current	**₦141.80**
- Target	**₦173.13**
Recommendation:	**BUY**

** As at Tuesday July 28, 2020*

INVESTMENT SUMMARY

Coronavirus outbreak has affected global economy as most businesses continue to struggle during the lockdown in most countries. One of the sectors expected to underperform during this period is cement sector due to reduced activities in constructions. However, Dangote Cement Plc defied the odds by reporting a modest improvement in performance amidst COVID-19 challenges as revenue increased by 1.95% to ₦476.85 billion in H1'20 (vs. ₦467.73 billion in H1'19). The higher revenue was driven by higher average net prices realised in Nigeria and Pan-Africa (i.e. other African nations except Nigeria) as well as higher cement volumes in Pan-Africa. However, due to the partial lockdown and border closures (which translated to a lower export sales), total cement volume sold in Nigeria fell by 2.40%. Of the company's cement capacity of 45.55 million tonnes per annum across Africa, a total of 12.11 million tonnes was produced in H1'20 (vs. 12.29 million tonnes in H1'19). Overall, production cost of sales increased by 4.79% to ₦202.42 billion in H1'20 (vs. ₦193.17 billion in H1'19), due to a rise in the manufacturing costs in Nigeria. Consequently, the group's EBITDA increased marginally by 0.06% to ₦218.07 billion in H1'20 (vs. ₦217.94 billion in H1'19).

Mainly as a result of a higher exchange gain in Nigeria and a higher interest earning cash balances in Ethiopia, net finance loss fell by 29.18% to ₦10.63 billion in H1'20 (vs. ₦15.01 billion net financial loss in H1'19). With impressive operating and non-operating performance, profit before tax rose by 4.74% to ₦162.85 billion in H1'20 (vs. ₦155.49 billion in H1'19). The company made a provision of ₦36.71 billion for tax in H1'20 (vs. ₦36.25 billion in H1'19). Consequently, profit after tax increased marginally by 5.79% to ₦126.14 billion in H1'20 (vs. ₦119.24 billion in H1'19). With the impressive performance in the first half of 2020, we upgrade the target price per share to ₦173.18 (Previous Target Price: ₦171.38) and maintain a **BUY** recommendation.

Fig. 1: Quarterly results highlights

	2Q2020	1Q2020	2Q2019	Q/q Δ	Y/y Δ
Revenue (₦'mn)	227,670	249,182	227,573	-8.63%	+0.04%
Op. Profit (₦'mn)	81,700	91,779	82,114	-10.98%	-0.50%
Net profit (₦'mn)	65,551	60,592	58,986	+8.18%	+11.13%

Source: NSE, Bloomberg, PAC Research

Fig. 2: Stock data

FYE	December
Price Mov't: YtD / 52wk	-0.14%/-16.59%
52-week range	₦116.00- ₦180.40
30-day Average vol.	3,181,717
Shares Outstanding ('mn)	1,547,422
Market Cap. (₦bn)	2,416.34
EPS (₦) - 12months trailing	12.17
DPS (₦) - FY2019	16.00

Source: NSE, Bloomberg, PAC Research

Fig. 3: Key ratios

	H1'20	H1'19
Gross profit margin	57.55%	58.70%
Net profit margin	26.45%	25.49%
Equity multiplier	2.44x	1.99x
Asset turnover	0.26x	0.28x

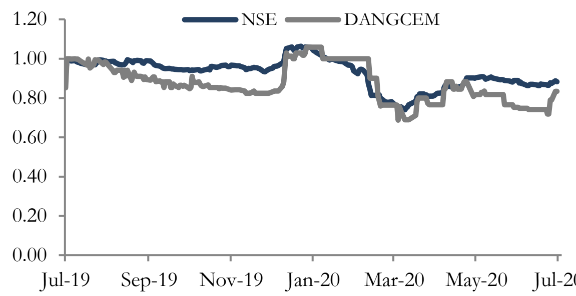
Source: NSE, PAC Research

Fig. 4: Valuations

	FY2018	FY2019	FY2020E	FY2021F
P/E	6.19x	12.05x	12.29x	11.44x
P/B	2.45x	2.69x	2.81x	2.65x
Div Yield (%)	11.28	11.28	7.40	8.11
Pay-out Ratio	69.85%	135.97%	91.01%	92.82%
EV/EBITDA	5.96x	6.73x	6.69x	6.24x
Ev/Revenue	2.88	2.98	3.01	2.86
Sales Per Share	52.89	52.33	52.59	55.74
P/S Ratio	2.68	2.71	2.70	2.54

Source: NSE, PAC Research

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



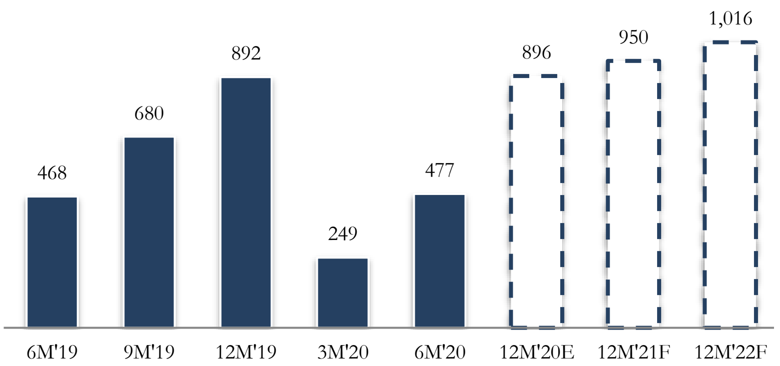
Source: Bloomberg, PAC Research

Group revenue improves by 1.95% YoY due to increased cement volumes in Pan-Africa and higher prices across board: Dangote cement reported impressive figure for the top-line amidst COVID-19 challenges in the first half of 2020 as revenue increased by 1.95% to ₦476.85 billion (vs. ₦467.73 billion in the first half of 2019). The increase in revenue was mainly driven by improved average net prices realised in Nigeria and Pan Africa as well as higher cement volumes in Pan-Africa. Although, total cement volume sold in Nigeria declined by 2.40% to 7.41 million tonnes in H1'20 (vs. 7.60 million tonnes in H1'19), total revenue of Nigerian operation increased by 1.20% to ₦332.38 billion in H1'20 (vs ₦328.29 billion in H1'19). The decline in cement volumes sold by the Nigerian operation was mainly attributed to the lockdown of economic activities in various states as well as border closures, which also affected the export sales during the period. However, net revenue per tonne in Nigeria increased by 3.77% to ₦44,855 in H1'20 (vs. ₦43,224 in H1'19).

The decline in cement volumes sold by the Nigerian operation was mainly attributed to the lockdown of economic activities in various states as well as border closures, which also affected the export sales during the period.

Surprisingly, Pan-Africa recorded the higher cement volumes and improved price during the period under review. Pan-African volume improved marginally by 0.70% to 4.73 million tonnes in H1'20 (vs. 4.70 million tonnes in H1'19) due to improved volumes in Congo, Cameroon, Ethiopia, Senegal and Sierra Leone. However, Zambia, Ghana and South Africa recorded lower cement sales volumes as a result of COVID-19 restrictions during the period

Fig. 6: Revenue – 6M'19-12M'22F (Billion NGN)



Source: NSE, Bloomberg, PAC Research

Group manufacturing costs rise by 4.79% year-on-year due to higher energy costs: In the first half of 2020, Dangote cement recorded higher manufacturing costs as it increased by 4.79% to ₦202.42 billion (vs. ₦193.17 billion incurred in the first half of 2019), due to higher manufacturing costs in both Nigeria and Pan-Africa. Nigerian manufacturing costs increased by 8.01% to ₦101.10 billion in H1'20 (vs. ₦93.60 billion in H1'19). The increase in the manufacturing costs of Nigerian operation was mainly attributed to unfavourable fuel mix which led to the use of more expensive gas during the period.

In addition, manufacturing cost in other African countries rose by 1.76% to ₦101.32 billion in H1'20 (vs. ₦99.57 billion in H1'19) due to the rise in Pan-Africa sales as well as the depreciation of the Naira which resulted in higher values in Naira when other Pan-African currencies were converted to Naira.

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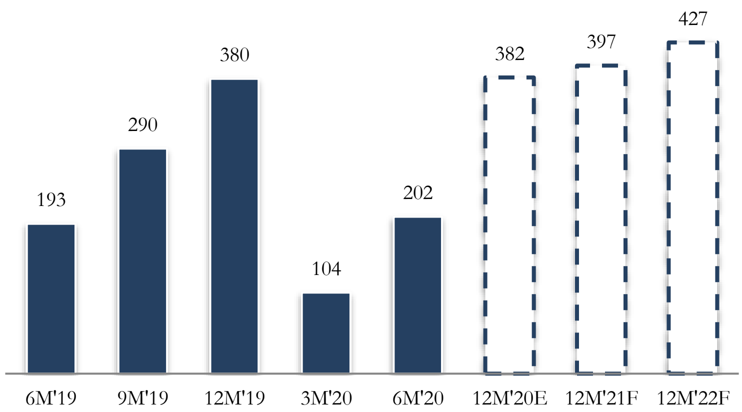
Mainly as a result of salary increments and general inflation during the period under review, Dangote Cement recorded higher figure for administration expenses as it increased by 4.30% to ₦26.05 billion in H1'20 (vs. ₦24.98 billion in H1'19). However, the increase in administrative expenses was offset by the reduction in selling and distribution expenses as it fell by 3.32% to ₦77.64 billion in H1'20 (vs. ₦80.31 billion in H1'19). The reduction in selling and distribution costs during the period could be attributed to reduced haulage costs in Tanzania and Zambia due to the reduced cement volumes when compared with the corresponding period of the previous year. In addition, Ethiopia recorded lower figure for depreciation charges as some trucks are getting close to the end of their useful lives.

Fig. 7: Manufacturing Costs – 6M'19-12M'22F (Billion NGN)



Source: NSE, Bloomberg, PAC Research

With impressive operating and non-operating performance, profit before tax rises by 4.74% year-on-year: In addition to the impressive operating performance during the period, the company also reported an interesting figure for non-operating activities as net finance costs fell significantly by 29.18% to ₦10.63 billion in the first half of 2020 (vs. ₦15.01 billon in the first half of 2019), due to higher exchange gain during the period. The Nigerian Naira was adjusted to ₦387/1$ in H1'20 (H1'19: ₦365/1$) and this resulted in net exchange gains from inter-group assets and liabilities that do not eliminate in full on consolidation in the Nigerian operations. According to Dangote Cement, the part of the exchange gains was reclassified to Other Comprehensive income on Consolidation which resulted in a net exchange gain of ₦5.00 billion in H1'20 (vs. exchange loss ₦4.03 billion in H1'19) after taking into accounts exchange losses from Pan Africa operations that use different currencies.

The impressive overall performance reflected on profitability of the company as profit before tax increased by 4.74% to ₦162.85 billion in the first half of 2020 (vs. ₦155.49 billion reported in the first half of 2019). The company made a provision of ₦36.71 billion for tax in H1’20 (vs. ₦36.25 billion in H1’19). The moderate tax rate for the group could be attributed to Nigerian effective tax rate of 16.40% as the portion of the H1’20 performance was impacted by the tax exemption arising from the Pioneer Status Incentive scheme for Ibese Lines 3 &4 and Obajana Line 4 which ended in February 2020. Consequently, profit after tax for the period increased by 5.79% to ₦126.14 billion in H1’20 (vs. ₦119.24 billion reported in H1’19).

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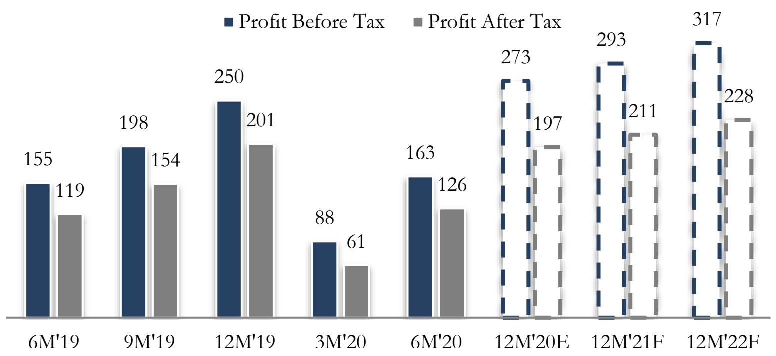
Fig. 8: Profit before Tax and Profit after Tax – 6M’19-12M’22F (Billion NGN)

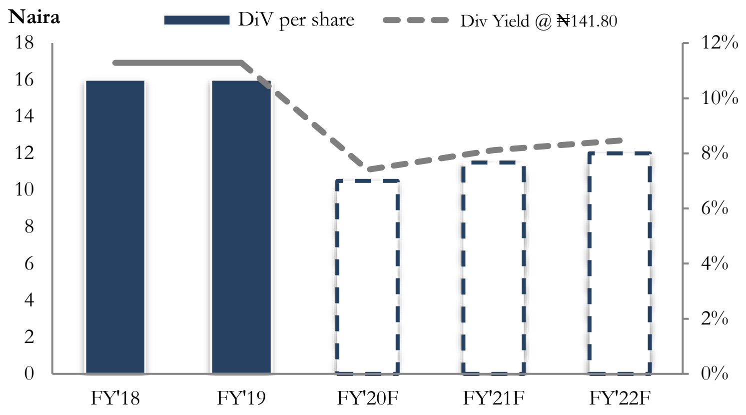


Source: NSE, Bloomberg, PAC Research

Balance sheet position remains strong; historical dividend payment to continue in FY’20: The balance sheet position of the company remains solid and strong, which reflected in improved total assets during the period. Total assets increased by 8.98% to ₦1.81 trillion in H1’20 (vs. ₦1.66 trillion in H1’19), mainly as a result of improvement in property, plant and equipment. Property, plant and equipment rose by 5.61% to ₦1.25 trillion in the half yar of 2020 (vs ₦1.19 trillion in the corresponding period of previous year). Addition to property, plant and equipment was ₦83.20 billion, of which ₦72.50 billion was spent in Nigeria and ₦10.70 billion in Pan-African operations. However, total liabilities increased significantly by 29.16% to ₦1.07 trillion in H1’20, from ₦825.19 billion reported in H1’19. The increase in total liabilities of the company was attributed to a 59.75% increase in current liabilities mainly as a result of current tax payable, amount owed to related parties for trucks and the exchange impact (depreciation of Naira from ₦365/1$ to ₦387/1$ in H1’20). Consequently, the net assets of the company fell by 11.05% to ₦739.37 billion in the first half of 2020 (vs. ₦831.24 billion in the first half of 2019), and this translated to a net asset per share of ₦43.39 (vs. ₦48.78 in H1’19). With the impressive H1’20 performance and solid balance sheet position, we expect the company to pay at least a dividend of ₦10.50 per share in FY’20.

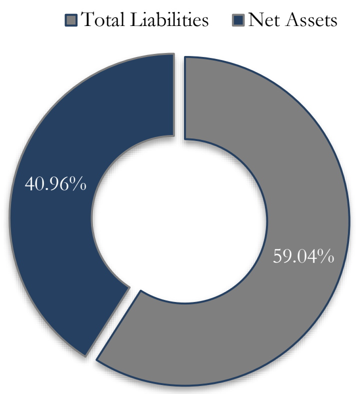
Addition to property, plant and equipment was ₦83.20 billion, of which ₦72.50 billion was spent in Nigeria and ₦10.70 billion in Pan-Africa operations.

Fig. 9: Dividend Per Share and Dividend Yield (FY'18-FY'22F)



Source: NSE, PAC Research

Fig. 10: Total Liabilities Vs Net Asset in H1'20



Source: NSE, Bloomberg, PAC Research

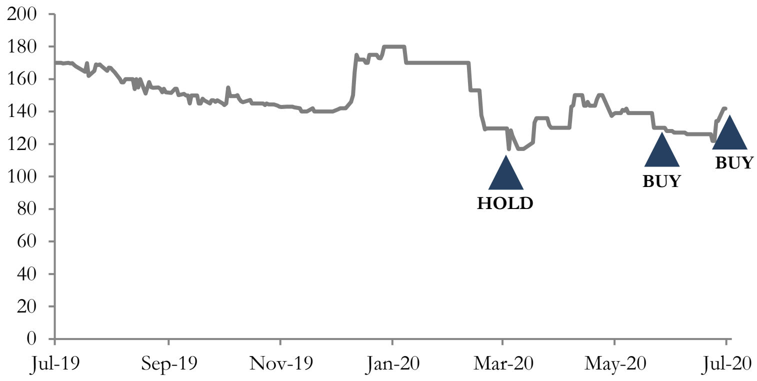
Valuation

Our valuation puts the target price of the stock at ₦173.18, representing an increase of 22.13%, from the current price of ₦141.80. In arriving at the target price, we employed Discounted Cash flow Valuation methodology. Consequently, we maintain 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, the impact of COVID-19 on the cement industry and the outlook of the management.

Our valuation puts the target price of the stock at N173.18, representing an increase of 22.13%, from the current price of N141.80.

Fig. 11: Share Price History (Naira)



Source: NSE, PAC Research

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

	2018	2019	2020E	2021F
Revenue	901,213	891,671	896,129	949,897
Change		*-1.06%*	*0.50%*	*6.00%*
Cost of Sales	(383,311)	(379,989)	(381,751)	(397,057)
Change		*-0.87%*	*0.46%*	*4.01%*
Gross Profit	517,902	511,682	514,378	552,840
Change		*-1.20%*	*0.53%*	*7.48%*
SG&A	(189,426)	(214,769)	(211,487)	(224,176)
Change		*13.38%*	*-1.53%*	*6.00%*
Other Income	10,222	2,980	5,377	5,699
Change		*-70.85%*	*80.43%*	*6.00%*
Operating profit	338,698	299,893	308,268	334,364
Change		*-11.46%*	*2.79%*	*8.47%*
Finance Income	11,323	7,610	17,923	15,198
Change		*-32.79%*	*135.51%*	*-15.20%*
Finance Cost	(49,778)	(57,673)	(53,768)	(56,994)
Change		*15.86%*	*-6.77%*	*6.00%*
Profit Before Taxation	300,806	250,479	273,051	293,233
Change		*-16.73%*	*9.01%*	*7.39%*
Taxation	89,519	(49,958)	(76,454)	(82,105)
Change		*-155.81%*	*53.04%*	*7.39%*
Profit After Taxation	390,325	200,521	196,596	211,128
Change		*-48.63%*	*-1.96%*	*7.39%*

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

	2018	2019	2020E	2021F
Fixed Assets	1,171,864	1,206,749	1,254,581	1,320,357
Intangible assets	5,969	3,663	5,556	5,889
Deffered tax assets	40,622	44,768	43,910	46,545
Inventories	106,998	114,806	120,977	128,236
Trade and other recievables	44,468	30,001	35,845	37,996
Bank and Cash Balances	166,896	123,903	116,497	118,737
Total current assets	428,838	406,736	431,486	453,101
Total Assets	1,694,463	1,741,351	1,816,006	1,911,193
Trade and other payables	230,970	284,739	304,684	322,965
Current tax payable	9,223	49,932	71,690	75,992
Financial debt	220,128	260,631	286,761	303,967
Other current liabilities	35,185	34,083	76,171	66,493
Total current liabilities	495,506	630,794	740,741	770,936
Deferred tax liabilities	83,350	93,841	96,782	102,589
Net Assets	986,613	897,937	858,940	912,851

Fig. 14: Profitability Ratio

	2018	2019	2020E	2021F
Return on Equity	39.56%	22.33%	22.89%	23.13%
Return on Assets	23.04%	11.52%	10.83%	11.05%
Gross margin	57.47%	57.38%	57.40%	58.20%
EBITDA margin	48.30%	44.34%	44.97%	45.77%
PBT margin	33.38%	28.09%	30.47%	30.87%
Net Profit Margin	43.31%	22.49%	21.94%	22.23%

Fig. 15: Asset Utilization

	2018	2019	2020E	2021F
cash/sales	0.19	0.14	0.13	0.13
Sales to inventory (x)	8.42	7.77	7.41	7.41
Sales to total assets (x)	0.53	0.51	0.49	0.50
Sales to total fixed assets	0.77	0.74	0.71	0.72
Equity multiplier	1.72	1.94	2.11	2.09
fixed asset turnover	1.30	1.35	1.40	1.39

Fig. 16: Liquidity Ratios

	2018	2019	2020E	2021E
Quick ratio	0.65	0.46	0.42	0.42
Current ratio	0.87	0.64	0.58	0.59
Cash ratio	0.34	0.20	0.16	0.15
Interest Coverage	6.04	4.34	5.08	5.15
Operating Cash Flow Ratio	1.81	1.45	1.24	1.13
Debt/net income	0.78	1.77	1.95	1.93
Debt/operating cashflow	0.34	0.39	0.42	0.47
Debt to asset	0.42	0.48	0.53	0.52
Total liabilities/equities	0.72	0.94	1.11	1.09
Inventory turnover	8.58	7.94	7.78	7.62
Inventory turnover days	41.97	45.33	46.26	47.22
Account payable days	216.92	269.76	287.32	292.82

Fig. 17: Shareholders' Investment Ratios

	2018	2019	2020E	2021F
EPS (₦)	22.91	11.77	11.54	12.39
DPS (₦)	16.00	16.00	10.50	11.50
NAVPS (₦)	57.90	52.69	50.41	53.57
Earnings yield (%)	16.15	8.30	8.14	8.74

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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PanAfrican Capital Holdings Ltd
8A, Elsie Femi Pearse Street
Victoria Island
Lagos, Nigeria
Tel: +234 (1) 2716899, 2718630
www.panafricancapitalholdings.com