

## Performance below Expectation as Higher Distribution Costs and FX Loss Impact Profits

### INVESTMENT SUMMARY

Dangote Cement Plc reported higher sales volume across the group in three-month to March 2019, however the group revenue declined marginally by 0.81% to ₦240.16 billion (vs. ₦242.12 billion in three-month to March 2018). The lower group revenue was as a result of reduced net average prices in Nigeria during the period. Of the company's cement capacity of 45.55 million tonnes per annum across Africa, a total of 6.34 million tonnes was produced in Q1'19 (vs. 6.20 million tonnes produced in Q1'18). Overall, the group manufacturing costs rose by 2.18% to ₦99.48 billion in Q1'19 (vs. ₦97.35 billion in Q1'18), as a result of general increase in prices of raw materials and labour in Nigeria. Manufacturing costs in Pan-African operations remained flat at approximately ₦50.00 billion while manufacturing costs in Nigeria rose by 5.20% to ₦49.70 billion. Mainly as a result of 32.81% rise in haulage expenses, total selling and distribution expenses rose by 33.97% to ₦39.61 billion in Q1'19 (vs. ₦29.57 billion in Q1'18). Consequently, EBITDA fell by 11.24% to ₦111.76 billion in Q1'19, from ₦125.92 billion in Q1'18.

For non-operating activities of the company, FX loss of ₦3.08 billion was recorded in Q1'19 (vs. FX gain of ₦12.48 billion in Q1'18). With unimpressive performance across board, profit before tax declined by 27.16% to ₦78.96 billion (vs. ₦108.40 billion in Q1'18). On the back of tax exemptions on three production lines in Nigeria, the company made a lower provision of ₦18.71 billion for tax in Q1'19 (vs. ₦36.28 billion in Q1'18). Consequently, profit after tax fell by 16.46% to ₦60.25 billion (vs. ₦72.12 billion in Q1'18). However, the company's 12-month trailing EPS increased to ₦22.21, from ₦12.94 recorded in the previous period. With this unimpressive result, we downgrade our target price per share to ₦215.73 (Previous Target Price: ₦247.29) and also maintain a **BUY** recommendation on the company shares.

Fig. 1: Quarterly results highlights

	1Q2019	4Q2018	1Q2018	Q/q Δ	Y/y Δ
Revenue (₦mn)	240,157	215,923	242,116	+11.22%	-0.81%
Op. Profit (₦mn)	87,845	71,838	103,345	+22.28%	-15.00%
Net profit (₦mn)	60,254	232,048	72,123	+74.03%	-16.46%

Source: NSE, Bloomberg, PAC Research

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Price:

- Current	₦176.00
- Target	₦215.73

Recommendation: **BUY**

\* As at Friday May 17, 2019

Fig. 2: Stock data

FYE	December
Price Mov't: YtD / 52wk	-7.22%/-29609%
52-week range	₦170.00- ₦250.00
30-day Average vol.	552,905
Shares Outstanding ('mn)	17,040.51
Market Cap. (₦bn)	2,999.13
EPS (₦) - 12months trailing	22.21
DPS (₦) - FY2018	16.00

Source: NSE, Bloomberg, PAC Research

Fig. 3: Key ratios

	Q1'19	Q1'18
Gross profit margin	58.58%	59.79%
Net profit margin	25.09%	29.79%
Equity multiplier	1.66x	1.99x
Asset turnover	0.14x	0.14x

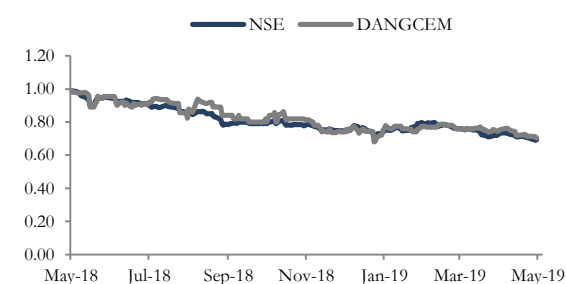
Source: NSE, PAC Research

Fig. 4: Valuations

	FY2017	FY2018	FY2019F	FY2020F
P/E	14.68x	7.68x	11.67x	10.80x
P/B	3.84x	3.04x	2.83x	2.78x
Div Yield (%)	5.97	9.09	7.39	7.95
Pay-out Ratio	87.60%	69.85%	85.88%	86.37%
EV/EBITDA	8.29x	7.30x	6.72x	6.41x
Ev/Revenue	4.00	3.53	3.30	3.15
Sales Per Share	47.27	52.89	55.53	58.31
P/S Ratio	3.72	3.33	3.17	3.02

Source: NSE, PAC Research

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

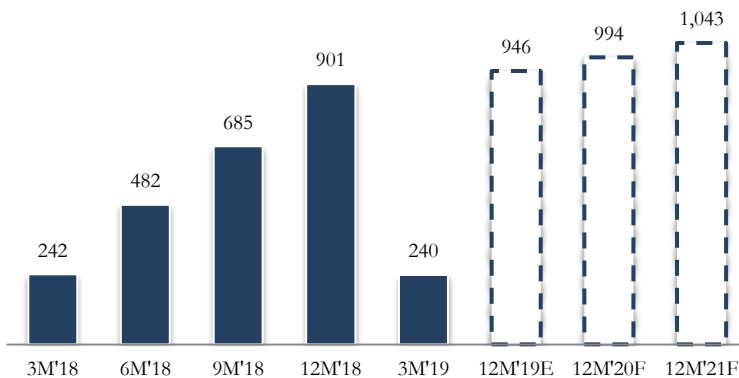


Source: Bloomberg, PAC Research

**Lower average prices in Nigeria drag group revenue down by 0.81% YoY.** Despite strong increase in volumes sold in Nigeria in January, sales in first quarter of 2019 were affected by the delayed national/local elections and growth slowed across the market in February and March. As a result, total volumes sold in Nigeria increased marginally by 0.55% to 3.99 million tonnes in the first quarter of 2019, relative to 3.97 million tonnes achieved in the corresponding quarter of the previous year. However, volume sold in Pan-African operations increased by 4.82% to 2.35 million tonnes in Q1'19 (vs. 2.24 million tonnes in Q1'18). Across board, total volume sold increased by 2.31% to 6.34 million tonnes in Q1'19 (vs. 6.20 million tonnes recorded in Q1'18), as Nigerian operations contributed 62.97% (Q1'18: 63.93%) to the group volumes sold while Pan-African operations contributed 37.03% (Q1'18: 36.07%) during the period. Meanwhile, the higher volume did not translate to higher revenue as group revenue decreased marginally by 0.81% to ₦240.16 billion in Q1'19 (vs. ₦242.12 billion reported in Q1'18). The decline in revenue can be mainly attributed to lower average price per tonne on Nigeria sales as it declined by 2.82% to ₦42,467 in the first quarter of 2019, from ₦43,800 recorded in the first quarter of 2018. In the beginning of second quarter of 2019, Dangote Cement raised prices by ₦150 per bag (or ₦3,000 per tonne) and as a result, we expect improvement in group revenue going forward.

*The decline in revenue can be mainly attributed to lower average price per tonne on Nigeria sales as it declined by 2.82% to ₦42,467 in the first quarter of 2019...*

**Fig. 6: Revenue – 3M'18-12M'21F (Billion NGN)**



Source: NSE, Bloomberg, PAC Research

**Due to general increase in prices of raw materials and labour in Nigeria, group manufacturing costs increase by 2.18% year-on-year.**

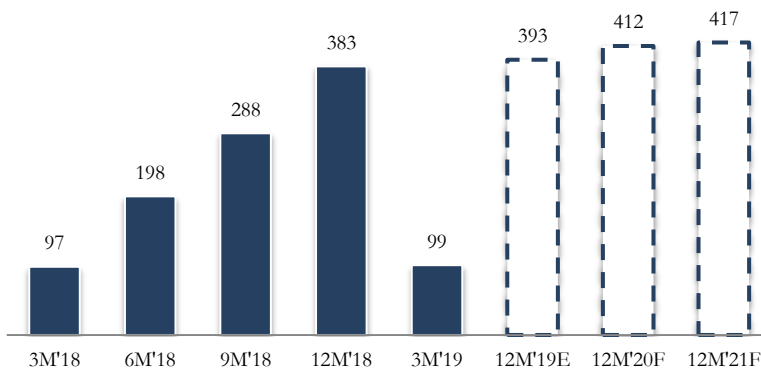
In the first quarter of 2019, manufacturing costs of the group increased by 2.18% to ₦99.48 billion, from ₦97.35 billion incurred in the corresponding period of the previous year. In general, the increase in manufacturing costs can be ascribed to the general increase in prices of raw materials and labour in Nigeria. Manufacturing costs in Nigeria increased by 5.20% to ₦49.70 billion in Q1'19 (vs. ₦47.20 billion in Q1'18) while manufacturing costs in Pan-African operations remained flat at ₦50.00 billion, despite higher volumes sold.

*In terms of contribution, fuel and power consumed remained the highest contributor to total manufacturing costs as it contributed 32.47% in Q1'19*

In general, material consumed and salaries & related staff costs (at production level) are the key drivers of higher manufacturing cost as they increased by 3.07% and 5.58% to ₦29.65 billion (Q1'18: ₦28.76 billion) and ₦7.89 billion in Q1'19 (Q1'18: ₦7.47 billion) respectively. In terms of contribution, fuel and power consumed remained the highest contributor to total manufacturing costs as it contributed 32.47% in Q1'19 (Q1'18: 32.99%), closely followed by material consumed as it contributed 29.80% to total manufacturing cost in Q1'19 (Q1'18: 29.55%).

The company also incurred higher administrative expenses and distribution expenses during the period. Due to higher provision for depreciation & amortisation and salaries & related staff costs (administrative level), total administrative expenses increased by 11.58% to ₦13.22 billion in Q1'19 (vs. ₦11.55 billion incurred in Q1'18). Mostly as a result of 32.81% increase in haulage expenses, total selling and distribution cost increased by 33.97% to ₦39.61 billion in first quarter of 2019, from ₦29.57 billion incurred in the corresponding period of the previous year.

Fig. 7: Manufacturing Costs – 3M'18-12M'21F (Billion NGN)



Source: NSE, Bloomberg, PAC Research

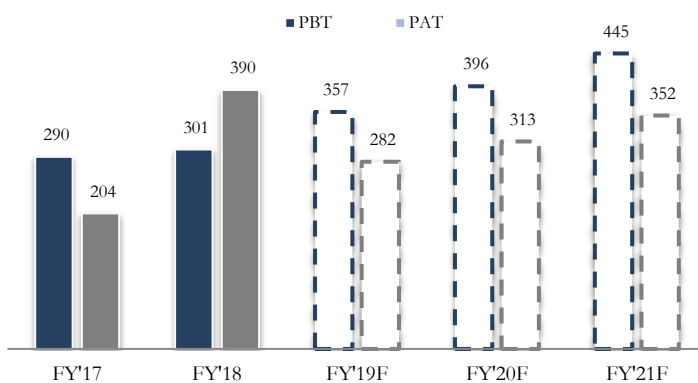
**With FX loss of ₦3.08 billion and poor operating performance, profit before tax declines by 27.16% year-on-year.** In addition to the poor operating performance during the period, the company reported an unimpressive figure for non-operating performance as net finance costs of ₦9.42 billion was reported, relative to net finance income of ₦4.61 billion in the corresponding quarter of the previous year. The reported net finance cost can be mainly attributed to foreign exchange loss of ₦3.08 billion in Q1'19, compared to exchange gain of ₦12.48 billion in Q1'18. During the first quarter of 2019, the Nigerian Naira was devalued slightly from about ₦359/US\$1 to ₦360/US\$1, compared to first quarter of 2018 when it was devalued from about ₦331/US\$1 to ₦337/US\$1. The ₦12.48 billion foreign exchange gain in Q1'18 was mainly driven by the depreciation of the Naira and appreciation of the CFA, resulting in gains on intergroup assets.

*The reported net finance cost can be mainly attributed to foreign exchange loss of ₦3.08 billion in Q1'19, compared to exchange gain of ₦12.48 billion in Q1'18*

The devaluation of the Naira in Q1'19 was much lower, resulting in lower exchange gains which were outweighed by exchange losses in Pan-African operations and this led to a net exchange loss for the first quarter of 2019.

The unimpressive figure from core operating activities and non-operating activities reflected on profitability of the company as profit before tax declined significantly by 27.16% to ₦78.96 billion in the first quarter of 2019, relative to ₦108.40 billion reported in the first quarter of 2018. However, the company continues to benefit from tax exemptions on some lines of productions, resulting in a reduced effective tax rate of 19% for Q1'19 (vs. ETR of 30% in Q1'18) which represents a mix of production lines that are out of tax exemptions and lines that are still entitled to the tax exemptions. This ETR of 19% translated to a lower tax provision of ₦18.71 billion in Q1'19 (vs. ₦36.28 billion in Q1'18) and as result, profit after tax for the period declined by 16.46% to ₦60.25 billion (vs. ₦72.12 billion reported in Q1'18).

**Fig. 8: Profit before Tax and Profit after Tax – 3M'18-12M'21F (Billion NGN)**



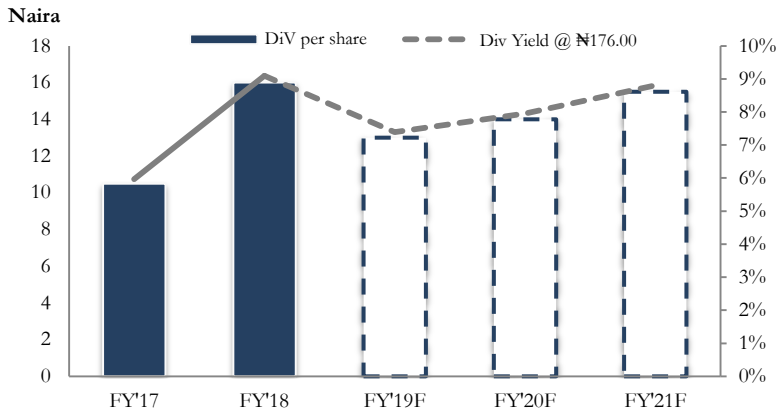
Source: NSE, Bloomberg, PAC Research

**Balance sheet remains in a solid position; historical dividend payment to continue in FY'19.** The balance sheet position of the company remains strong, reflected in improved total assets and lower liabilities during the period. Total assets increased by 1.34% to ₦1.74 trillion in Q1'19 (vs. ₦1.72 trillion in Q1'18), due to higher deferred tax assets and higher prepayments on current and non-current assets. Deferred tax assets increased by 30.30% to ₦40.62 billion (Q1'18: ₦31.05 billion) while total prepayments on assets increased by 37.19% to ₦170.07 billion in Q1'19 (vs. ₦123.97 billion prepayments in Q1'18). However, total liabilities declined by 18.65% to ₦695.35 billion in March 2019, from ₦854.74 billion in the corresponding period of the previous year. The decline in total liabilities of the company can be attributed to a 65.38% reduction in current tax payable, 39.71% decline in deferred tax liabilities and 56.47% reduction in long-term financial liabilities.

*With a solid balance sheet position and expectation of improved revenue in the coming quarters, we expect the company*

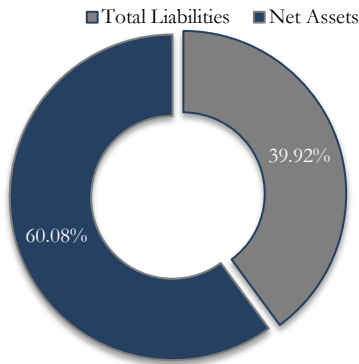
Consequently, the net assets of the company increased by 21.11% to ₦1.05 trillion in the first quarter of 2019 (vs. ₦0.86 trillion achieved in the first quarter of 2018) and this translated to a net asset per share of ₦61.42 (vs. ₦50.72 in Q1'18). With a solid balance sheet position and expectation of improved revenue in the coming quarters, we expect the company to pay at least a dividend of ₦13.00 per share in full year of 2019.

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



Source: NSE, PAC Research

**Fig. 10: Total Liabilities Vs Net Asset in Q1'19**



Source: NSE, Bloomberg, PAC Research

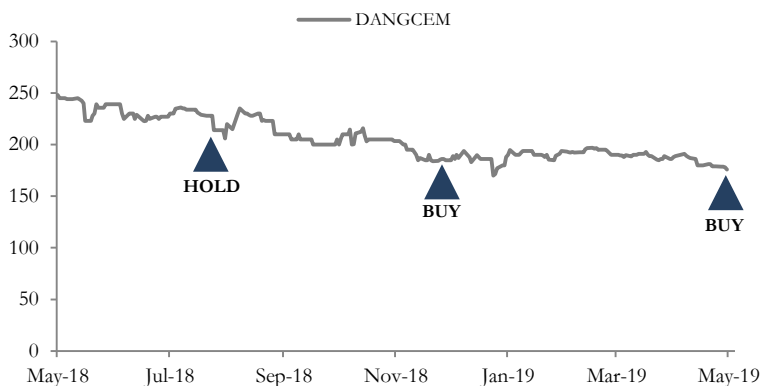
## Valuation

Our valuation puts the target price of the stock at ₦215.73, representing an increase of 22.58%, from the current price of ₦176.00. 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 N215.73, representing an increase of 22.58%, from the current price of N176.00.*

**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	946,274	993,587
Change		11.87%	5.00%	5.00%
Cost of Sales	(351,290)	(383,311)	(392,704)	(412,339)
Change		9.12%	2.45%	5.00%
Gross Profit	291,287	454,292	517,902	553,570
Change		55.96%	14.00%	6.89%
SG&A	(155,297)	(189,426)	(198,717)	(208,653)
Change		21.98%	4.91%	5.00%
Other Income	5,213	10,222	10,409	10,929
Change		96.09%	1.83%	5.00%
Operating profit	304,208	338,698	365,262	383,525
Change		11.34%	7.84%	5.00%
Finance Income	35,926	11,323	9,463	11,923
Change		-68.48%	-16.43%	26.00%
Finance Cost	(52,711)	(49,778)	(40,970)	(34,683)
Change		-5.56%	-17.70%	-15.34%
Profit Before Taxation	289,590	300,806	333,755	360,764
Change		3.87%	10.95%	8.09%
Taxation	(85,342)	89,519	(76,764)	(82,976)
Change		-204.89%	-185.75%	8.09%
Profit After Taxation	204,248	390,325	256,991	277,789
Change		91.10%	-34.16%	8.09%

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

	2017	2018	2019E	2020F
Fixed Assets	1,192,140	1,171,864	1,192,305	1,212,177
Intangible assets	6,355	5,969	6,377	6,695
Deferred tax assets	30,625	40,622	40,690	42,724
Inventories	94,594	106,998	108,821	114,263
Trade and other receivables	30,155	44,468	37,851	39,743
Bank and Cash Balances	168,387	166,896	156,135	158,974
Total current assets	303,164	428,838	447,223	464,616
Total Assets	1,665,883	1,694,463	1,743,644	1,784,493
Trade and other payables	270,721	230,970	236,568	243,429
Current tax payable	63,901	9,223	23,657	24,840
Financial debt	144,783	220,128	207,802	218,192
Other current liabilities	41,071	35,185	41,163	43,221
Total current liabilities	520,476	495,506	510,136	530,576
Deferred tax liabilities	116,898	83,350	85,165	88,429
Net Assets	781,360	986,613	1,058,921	1,077,555

Fig. 14: Profitability Ratio

	2017	2018	2019E	2020F
Return on Equity	26.14%	39.56%	24.27%	25.78%
Return on Assets	12.26%	23.04%	14.74%	15.57%
Gross margin	56.39%	57.47%	58.50%	58.50%
EBITDA margin	48.18%	48.30%	49.17%	49.17%
PBT margin	35.95%	33.38%	35.27%	36.31%
Net Profit Margin	25.35%	43.31%	27.16%	27.96%

Fig. 15: Asset Utilization

	2017	2018	2019E	2020F
cash/sales	0.21	0.19	0.17	0.16
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	0.79	0.82
Equity multiplier	2.13	1.72	1.65	1.66
fixed asset turnover	1.48	1.30	1.26	1.22

Fig. 16: Liquidity Ratios

	2016	2017	2018E	2019E
Quick ratio	0.61	0.65	0.66	0.66
Current ratio	0.79	0.87	0.88	0.88
Cash ratio	0.32	0.34	0.31	0.30
Interest Coverage	5.49	6.04	8.15	10.40
Operating Cash Flow Ratio	1.44	1.81	2.00	2.07
Debt/net income	1.28	0.78	1.14	1.10
Debt/operating cashflow	0.35	0.34	0.29	0.28
Debt to asset	0.53	0.42	0.39	0.40
Total liabilities/equities	1.13	0.72	0.65	0.66
Inventory turnover	5.45	3.57	2.99	2.94
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	15.08	16.30
DPS (₦)	10.50	16.00	13.00	14.00
NAVPS (₦)	45.85	57.90	62.14	63.23
Earnings yield (%)	6.81%	13.01%	8.57%	9.26%

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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