

Dangote Cement Plc

Higher Cement Volumes and Improved Prices in Nigeria Impact Earnings

INVESTMENT SUMMARY

Year 2020 has been described as a year of survival due to the outbreak of coronavirus which has not only claimed the lives of many people, but also affected businesses in many countries. However, the impacts of this virus were not fully felt in Nigeria until the end of first quarter when the Federal Government of Nigeria locked down the activities in Lagos, Ogun and Abuja. With the little impacts of COVID-19 on the Nigerian economy in Q1'20, Dangote Cement Plc reported impressive performance as revenue increased by 3.76% to ₦249.18 billion (vs. ₦240.16 billion in Q1'19). The increase in the group's revenue can be attributed to higher volumes and realised prices in Nigeria. However, Pan-African sales fell marginally by 0.60% due to the early COVID-19 lockdown in South Africa and lower sales in Tanzania and Zambia. Of the company's cement capacity of 45.55 million tonnes per annum across Africa, a total of 6.30 million tonnes was produced in Q1'20 (vs. 6.34 million tonnes in Q1'19). Overall, the group production cost of sales rose by 4.87% to ₦104.33 billion in Q1'20 (vs. ₦99.48 billion in Q1'19). Consequently, the company's EBITDA rose by 2.20% to ₦114.22 billion in Q1'20, from ₦111.76 billion in Q1'19.

Mainly as a result higher exchange gain, net finance loss fell significantly by 60.50% to ₦3.72 billion in Q1'20 (vs. ₦9.42 billion in Q1'19). With impressive performance across the board, profit before tax rose by 11.52% to ₦88.06 billion (vs. ₦78.96 billion in Q1'19). The pioneer tax exemption for major production lines in Nigeria ended in Q1'20 and this resulted in higher tax of ₦27.46 billion in Q1'20 (vs. ₦18.71 billion in Q1'19). Consequently, profit after tax rose marginally by 0.56% to ₦60.59 billion in Q1'20 (vs. ₦60.25 billion in Q1'19). Due to the expectation of slowdown in cement demand in Africa as a result of impacts of COVID-19, we downgrade the target price per share to ₦171.38 (Previous Target Price: ₦178.06) but upgrade to a **BUY** recommendation.

Fig. 1: Quarterly results highlights

	1Q2020	4Q2019	1Q2019	Q/q Δ	Y/y Δ
Revenue (₦mn)	249,182	211,880	240,157	+17.61%	+3.79%
Op. Profit (₦mn)	90,657	67,479	87,845	+34.35%	+3.20%
Net profit (₦mn)	60,592	46,171	60,254	+31.23%	+0.56%

Source: NSE, Bloomberg, PAC Research

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Price:

- Current	₦139.00
- Target	₦171.38
Recommendation:	BUY

* As at Friday June 5, 2020

Fig. 2: Stock data

FYE	December
Price Mov't: YtD / 52wk	-2.11%/-26.46%
52-week range	₦116.00- ₦189.00
30-day Average vol.	3,181,717
Shares Outstanding ('mn)	17,040.51
Market Cap. (₦bn)	2,368.63
EPS (₦) - 12months trailing	11.79
DPS (₦) - FY2019	16.00

Source: NSE, Bloomberg, PAC Research

Fig. 3: Key ratios

	Q1'20	Q1'19
Gross profit margin	58.13%	58.58%
Net profit margin	24.32%	25.09%
Equity multiplier	1.90x	1.66x
Asset turnover	0.14x	0.14x

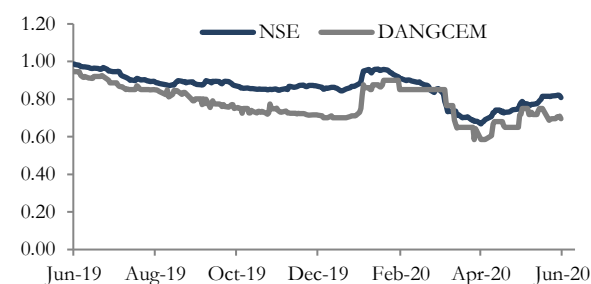
Source: NSE, PAC Research

Fig. 4: Valuations

	FY2018	FY2019	FY2020E	FY2021F
P/E	6.07x	11.81x	12.69x	12.09x
P/B	2.40x	2.64x	2.59x	2.55x
Div Yield (%)	11.51	11.51	7.91	8.27
Pay-out Ratio	69.85%	135.97%	100.42%	99.99%
EV/EBITDA	5.85x	6.61x	6.64x	6.36x
Ev/Revenue	2.83	2.93	3.00	2.87
Sales Per Share	52.89	52.33	50.76	53.29
P/S Ratio	2.63	2.66	2.74	2.61

Source: NSE, PAC Research

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



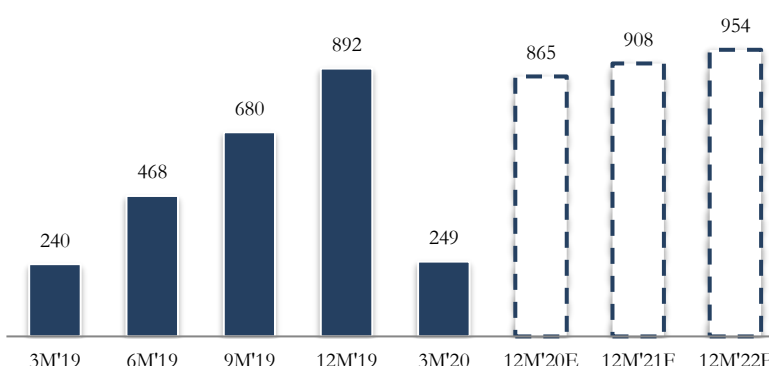
Source: Bloomberg, PAC Research

With higher cement volumes and improved average prices in Nigeria, group revenue rises by 3.76% YoY: Dangote cement reported impressive figure for the top-line in the first quarter of 2020 as revenue increased by 3.76% to ₦249.18 billion in Q1'20 (vs. ₦240.16 billion in Q1'19). The increase in revenue was attributed to higher cement volumes and improved average net prices in Nigeria during the period. Total volume of cement sold in Nigeria in the first quarter of 2020 was 4.02 million tonnes (vs. 3.99 million tonnes in the first quarter of 2019), with increased local sales being partially offset by the decline in exports due to the border closure. The net revenue per tonne in Nigeria was ₦44,633 in the first quarter of 2020 (vs. ₦42,567 in the first quarter of 2019). The increase in both the cement volume and average net prices in Nigeria translated to a total revenue of ₦179.34 billion for Nigerian operation in Q1'20 (vs. ₦169.88 billion in Q1'19).

However, volume of cement sold in Pan-African operations (i.e. other African nations except Nigeria) fell by 2.90% to 2.28 million tonnes in the first quarter of 2020 (2.35 million tonnes in the first quarter of 2019). During the period, Ethiopia, Senegal, Cameroon, Ghana, Sierra Leone and Congo recorded improved cement volumes, but this were partially offset by the reduction in the cement volumes of South Africa, Zambia and Tanzania. Consequently, the revenue of Pan-African operations fell marginally by 0.61% to ₦69.85 billion in Q1'20 (vs. ₦70.27 billion in Q1'19).

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Fig. 6: Revenue – 3M'19-12M'22F (Billion NGN)



Source: NSE, Bloomberg, PAC Research

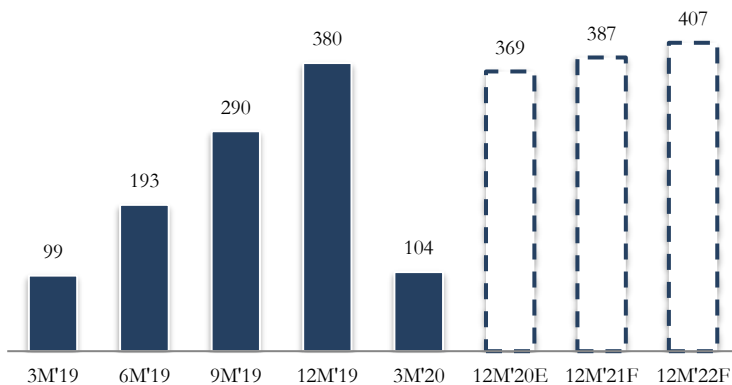
As a result of unfavourable fuel mix in Nigeria, group manufacturing costs increases by 4.87% year-on-year: In the first quarter of 2020, the manufacturing costs of the group increased by 4.87% to ₦104.33 billion (vs. ₦99.48 billion incurred in the corresponding period of the previous year), mainly as a result of an increase in the Nigerian manufacturing costs. The Nigerian manufacturing costs increased by 11.06% to ₦55.2 billion in Q1'20 (Q1'19: ₦49.70 billion).

The increase in the Nigeria's manufacturing costs was mainly driven by the energy costs due to unfavourable fuel mix which resulted in the use of more gas whose price increased when compared to the corresponding quarter of the previous year. However, Pan-African manufacturing cost fell by 1.40% in Q1'20 and this is in line with the decrease in the Pan-African sales volume during the period.

During the period, Dangote Cement also reported higher figure for total selling and administration expenses as it increased by 2.60% to ₦54.20 billion in Q1'20 (vs. ₦52.83 billion in Q1'19), due to higher sales distribution costs in Nigeria. Although, the total cement volume sold in Nigeria was marginally up to 4.02 million tonnes in Q1'20 (vs. 3.99 million tonnes in Q1'19), cements were delivered to different locations in Nigeria with trucks and this resulted in higher haulage costs. In addition, the company engaged in various promotion schemes which drove the increase in advertising and promotion costs.

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Fig. 7: Manufacturing Costs – 3M'19-12M'22F (Billion NGN)



Source: NSE, Bloomberg, PAC Research

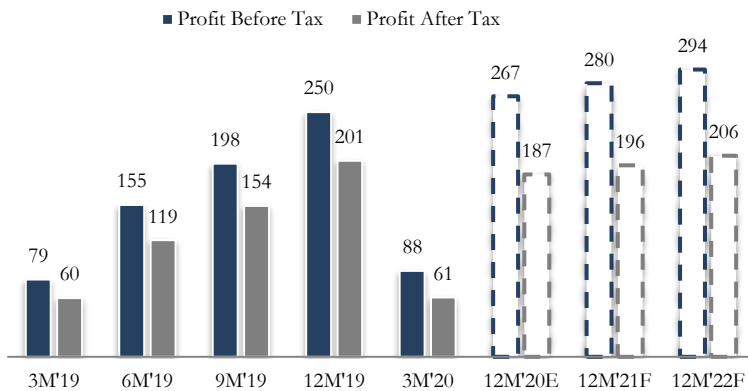
With impressive non-operating performance, profit before tax rises by 11.52% year-on-year: In addition to the impressive operating performance during the period, the company also reported a progressive figure for non-operating activities as net finance costs fell significantly by 60.50% to ₦3.72 billion in the first quarter of 2020 (vs. ₦9.42 billion in the first quarter of 2019), due to higher net exchange gain. The Nigerian Naira was devalued to ₦386/1\$ in Q1'20, from ₦364/1\$ and this resulted in net exchange gains from inter-group assets.

The impressive figure from the core operating activities and non-operating activities reflected on profitability of the company as profit before tax increased by 11.52% to ₦88.06 billion in the first quarter of 2020, relative to ₦78.96 billion reported in the first quarter of 2019.

However, tax holiday is over as pioneer tax exemption for some production lines, especially in Nigeria, ended in the first quarter of 2020 and this resulted in higher effective tax rate of 31.2% for the group. The effective tax rate of 31.2% translated to higher tax provision of ₦27.47 billion (₦18.71 billion in Q1'19) and as a result, profit after tax for the period rose marginally by 0.56% to ₦62.59 billion in Q1'20 (vs. ₦60.25 billion reported in Q1'19).

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Fig. 8: Profit before Tax and Profit after Tax – 3M'19-12M'22F (Billion NGN)



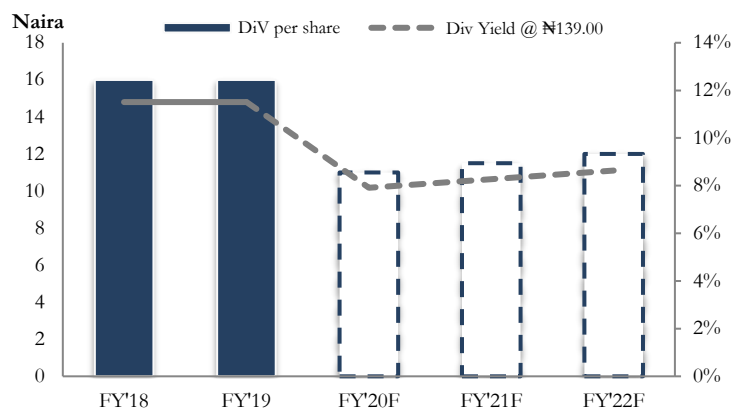
Source: NSE, Bloomberg, PAC Research

Balance sheet position remains solid; historical dividend payment to continue in FY'20: The balance sheet position of the company remains strong, reflected in improved total assets during the period. Total assets increased by 3.23% to ₦1.80 trillion in Q1'20 (vs. ₦1.74 trillion in the previous quarter), mainly as a result of improvement in property, plant and equipment. Property, plant and equipment increased by 2.70% to ₦1.24 trillion in Q1'20 (vs ₦1.21 trillion in the previous quarter). However, total liabilities increased marginally by 0.68% to ₦849.12 billion in Q1'20, from ₦843.41 billion reported in the corresponding previous period. The increase in total liabilities of the company was attributed to a 12.87% increase in deferred tax liabilities, 30.71% rise in current income tax payable and 134.15% increase in other current liabilities.

Consequently, the net assets of the company increased by 21.11% to ₦948.50 billion in the first quarter of 2020 (vs. ₦879.94 billion achieved in the previous quarter) and this translated to a net asset per share of ₦55.66 (vs. ₦52.69 in the previous quarter). Going forward, we do not expect Dangote Cement to have an improved performance in FY'20 as we expect to see the adverse impacts of COVID-19 on the financial statements of second and third quarter of 2020. However, with the solid balance sheet position, we expect the company to pay at least a dividend of ₦11.00 per share in FY'20.

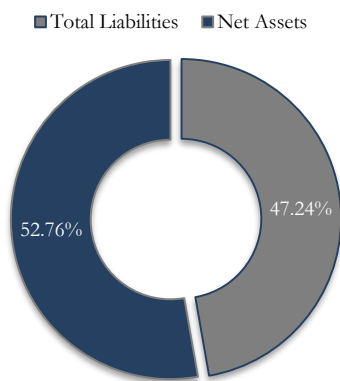
... with the solid balance sheet position, we expect the company to pay at least a dividend of ₦11.00 per share in FY'20.

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



Source: NSE, PAC Research

Fig. 10: Total Liabilities Vs Net Asset in Q1'20



Source: NSE, Bloomberg, PAC Research

Valuation

Our valuation puts the target price of the stock at ₦171.38, representing an increase of 23.30%, from the current price of ₦139.00. In arriving at the target price, we employed Discounted Cash flow Valuation methodology. Consequently, we upgrade to 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 in 2020 and the outlook of the management.

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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	864,921	908,167
Change		-1.06%	-3.00%	5.00%
Cost of Sales	(383,311)	(379,989)	(368,889)	(387,333)
Change		-0.87%	-2.92%	5.00%
Gross Profit	517,902	511,682	496,032	520,834
Change		-1.20%	-3.06%	5.00%
SG&A	(189,426)	(214,769)	(203,256)	(213,419)
Change		13.38%	-5.36%	5.00%
Other Income	10,222	2,980	6,141	6,448
Change		-70.85%	106.07%	5.00%
Operating profit	338,698	299,893	298,917	313,862
Change		-11.46%	-0.33%	5.00%
Finance Income	11,323	7,610	10,379	8,174
Change		-32.79%	36.39%	-21.25%
Finance Cost	(49,778)	(57,673)	(43,246)	(42,684)
Change		15.86%	-25.02%	-1.30%
Profit Before Taxation	300,806	250,479	266,655	279,988
Change		-16.73%	6.46%	5.00%
Taxation	89,519	(49,958)	(79,997)	(83,996)
Change		-155.81%	60.13%	5.00%
Profit After Taxation	390,325	200,521	186,659	195,992
Change		-48.63%	-6.91%	5.00%

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

	2018	2019	2020E	2021F
Fixed Assets	1,171,864	1,206,749	1,243,756	1,262,352
Intangible assets	5,969	3,663	5,363	5,631
Deferred tax assets	40,622	44,768	42,381	44,500
Inventories	106,998	114,806	116,764	122,603
Trade and other receivables	44,468	30,001	34,597	36,327
Bank and Cash Balances	166,896	123,903	112,440	113,521
Total current assets	428,838	406,736	416,459	433,196
Total Assets	1,694,463	1,741,351	1,785,629	1,827,232
Trade and other payables	230,970	284,739	285,424	299,695
Current tax payable	9,223	49,932	69,194	72,653
Financial debt	220,128	260,631	233,529	245,205
Other current liabilities	35,185	34,083	73,518	63,572
Total current liabilities	495,506	630,794	663,048	682,578
Deferred tax liabilities	83,350	93,841	93,411	98,082
Net Assets	986,613	897,937	913,789	927,238

Fig. 14: Profitability Ratio

	2018	2019	2020E	2021F
Return on Equity	39.56%	22.33%	20.43%	21.14%
Return on Assets	23.04%	11.52%	10.45%	10.73%
Gross margin	57.47%	57.38%	57.35%	57.35%
EBITDA margin	48.30%	44.34%	45.13%	45.13%
PBT margin	33.38%	28.09%	30.83%	30.83%
Net Profit Margin	43.31%	22.49%	21.58%	21.58%

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	0.48	0.50
Sales to total fixed assets	0.77	0.74	0.70	0.72
Equity multiplier	1.72	1.94	1.95	1.97
fixed asset turnover	1.30	1.35	1.44	1.39

Fig. 16: Liquidity Ratios

	2018	2019	2020E	2021E
Quick ratio	0.65	0.46	0.45	0.46
Current ratio	0.87	0.64	0.63	0.63
Cash ratio	0.34	0.20	0.17	0.17
Interest Coverage	6.04	4.34	6.17	6.56
Operating Cash Flow Ratio	1.81	1.45	1.35	1.34
Debt/net income	0.78	1.77	1.75	1.75
Debt/operating cashflow	0.34	0.39	0.36	0.38
Debt to asset	0.42	0.48	0.49	0.49
Total liabilities/equities	0.72	0.94	0.95	0.97
Inventory turnover	8.58	7.94	7.54	7.59
Inventory turnover days	41.97	45.33	47.73	47.44
Account payable days	216.92	269.76	278.55	278.55

Fig. 17: Shareholders' Investment Ratios

	2018	2019	2020E	2021F
EPS (₦)	22.91	11.77	10.95	11.50
DPS (₦)	16.00	16.00	11.00	11.50
NAVPS (₦)	57.90	52.69	53.62	54.41
Earnings yield (%)	16.48	8.47	7.88	8.27

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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