Dangote Cement Plc

Nigeria | Equities | Industrial Goods | May 18, 2018 — PAC RESEARCH

Higher Volume, Improved Pricing and Exchange Rate Benefit Impact Earnings

INVESTMENT SUMMARY

Dangote Cement Plc reported another impressive performance in the first quarter result of 2018 as revenue increased by 16.31% to ₦242.12 billion (vs. ₦208.174 billion in Q1'17). The increase in the revenue was boosted by higher volume and improved pricing in Nigeria and increased per-tonne revenue in Pan-African operations (i.e. other African nations except Nigeria). From the company's cement capacity of 45.55 million tonnes per annum, a total of 6.20 million tonnes was produced in Q1'18 (vs. 6.03 million in Q1'17). Production cost of sales increased by 10.88% to ₦97.35 billion in Q1'18 (vs. ₦87.80 billion recorded in Q1'17). In general, the increase in the production cost of sales was driven by increased volumes in Nigeria and higher costs in Pan African operations, due to the exchange rate for Naira which was about ₦337/US$1 at the end of Q1'18 compared to ₦305/US$1 in Q1'17. However, we are enthralled with the company's ability to reduce the cost margins to 40.21% in Q1'18 from 42.18% recorded in Q1'17. As a result, gross profit grew by 20.27% to ₦144.76 billion in Q1'18 (vs. ₦120.36 billion in Q1'17).

With proper management of cost, an increased volume of cement with higher cement price in Nigeria and improved per-tonne revenue in Pan African operations, profit before tax increased by 10.21% to ₦108.40 billion in Q1'18 (vs. ₦77.32 billion recorded in Q1'17). However, provision for tax weigh on improved performance of the company as the provision for tax increased by 69.13% to ₦36.28 billion in Q1'18 (vs. ₦21.45 billion in Q1'17). Profit after tax increased to ₦72.12 billion in Q1'18 from ₦55.87 billion published in Q1'17, representing an increase of 29.10%. Impressively, 12-month trailing EPS increased by 51.09% to ₦12.94 from ₦8.56 recorded in the previous period.

Based on the recent figures released by the company, we upgrade our target price per share to ₦263.05 from ₦262.87 previously recommended and as a result, we maintain our **HOLD** rating on the stock

Fig. 1: Quarterly results highlights

	1Q2018	4Q2017	1Q2017	Q/q Δ	Y/y Δ
Revenue (₦'mn)	242,116	202,007	208,166	+5.82%	+19.86%
Op. Profit (₦'mn)	103,787	71,121	83,248	+2.13%	+45.93%
Net profit (₦'mn)	72,123	11,112	55,866	-77.36%	+549.06%

Source: NSE, Bloomberg, PAC Research

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Price:	
- Current	**₦248.00**
- Target	**₦263.05**
Recommendation:	**HOLD**

** As at Thursday May 17, 2018*

Fig. 2: Stock data

FYE	December
Price Mov't: YtD / 52wk	+7.83%/+52.15%
52-week range	₦162.01 - ₦290.00
30-day Average vol.	887,637
Shares Outstanding ('mn)	17,040.51
Market Cap. (₦bn)	4,226.064
EPS (₦) - 12months trailing	12.94
DPS (₦) - FY2017	10.50

Source: NSE, Bloomberg, PAC Research

Fig. 3: Key ratios

	Q1'18	Q1'17
Gross profit margin	59.79%	57.82%
Net profit margin	29.79%	26.84%
Equity multiplier	1.99x	2.13x
Asset turnover	0.14x	0.12x

Source: NSE, PAC Research

Fig. 4: Valuations

	FY2016	FY2017	FY2018F	FY2019F
P/E	29.56x	20.69x	15.53x	12.44x
P/B	5.82x	5.41x	4.70x	4.64x
Div Yield (%)	3.43	4.23	4.64	5.04
Pay-out Ratio	101.39%	87.60%	72.00%	62.71%
EV/EBITDA	18.35x	11.71x	9.22x	7.91x
Ev/Revenue	7.29	5.52	4.53	3.81
Sales Per Share	36.10	47.27	57.20	68.93
P/S Ratio	6.87	5.25	4.34	3.60

Source: NSE, PAC Research

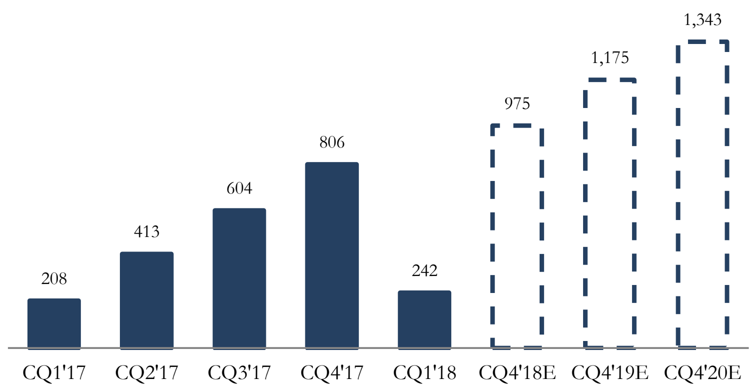
Fig. 5: DANGCEM vs NSE, 52-wk Movement (Rebased)

Source: Bloomberg, PAC Research

Increased volume and higher price in Nigeria and exchange rate benefit from Pan-African operation boost revenue: Dangote Cement delivered an impressive performance in Q1'18 as revenue increased by 16.31% to ₦242.12 billion from ₦208.17billion recorded in Q1'17. The improvement in revenue was driven by increased volume and higher price in Nigeria, and increased per-tonne revenue in Pan-African operations. The increased per-tonnes revenue in Pan-African operation was mainly as a result of depreciation in Naira which stood at ₦337/$1 at the end of Q1'18, compared with ₦305/$1 at the end of Q1'17. Total cement sold increased by 2.82% to 6.20 million tonnes in Q1'18 (vs.6.03 million tonnes sold in Q1'17). Nigeria remains the leading country in terms of total cement sold as it recorded 3.97 million tonnes in Q1'18 (vs. 3.77 million Tonnes reported in Q1'17), representing an increase of 5.28%. There was a slowdown in total cement sold in Pan African operations as total volume cement sold decreased by 4.40% to 2.24 million tonnes in Q1'18 from 2.34 million tonnes sold in Q1'17. The slowdown in Pan African operation was majorly driven by the fall in Ethiopia sales due to civil unrest in the region where the cement plant was located, as well as a fall in sales in Ghana and Tanzania.

The increased per-tonnes revenue in Pan African operation is mainly as a result of depreciation in Naira which stood at ₦337/$1 at the end of Q1'18, compared with ₦305/$1 at the end of Q1'17

Fig. 6: Revenue – Cummulative Quarters CQ1'17-CQ4'20E (Billion NGN)



Source: NSE, Bloomberg, PAC Research

Manufacturing costs rose by 10.88% YoY, due to increased volumes in Nigeria and exchange rate effects in Pan African operation:

In the first quarter of 2018, cost of sales grew by 10.88% to ₦97.35 billion from ₦87.80 billion recorded in corresponding quarter in 2017. The growth in manufacturing costs can be attributed to the increased production volume in Nigeria and increases in costs at Pan-African operations, mainly triggered by the exchange rate for Naira which was ₦337/$1 at the end of Q1'18 (vs. ₦305/$1 in Q1'17). Production cost of sales in Nigeria increased by 9.60% to ₦47.20 billion in Q1'18 (vs. ₦43.10 billion recorded in Q1'17) while exchange rate effects contributed about ₦4.50 billion to production cost of sales in Pan African operations as it increased by 12.10% to ₦50.10 billion in Q1'18 from ₦44.70 billion reported in Q1'17.

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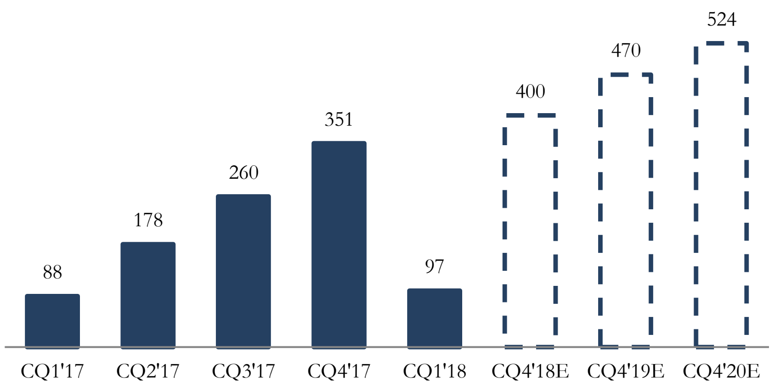
Overall, fuel and power consumption remains the largest contributor to manufacturing cost of sales as it contributed 32.99% in Q1'18 (Q1'17: 32.77%), closely followed by material consumed which contributed 29.55% to production cost of sales in Q1'18 (Q1'17: 31.24%).

Fig. 7: Production Cost of Sales Cum. Quarters CQ1'17-CQ4'20E (Billion NGN)



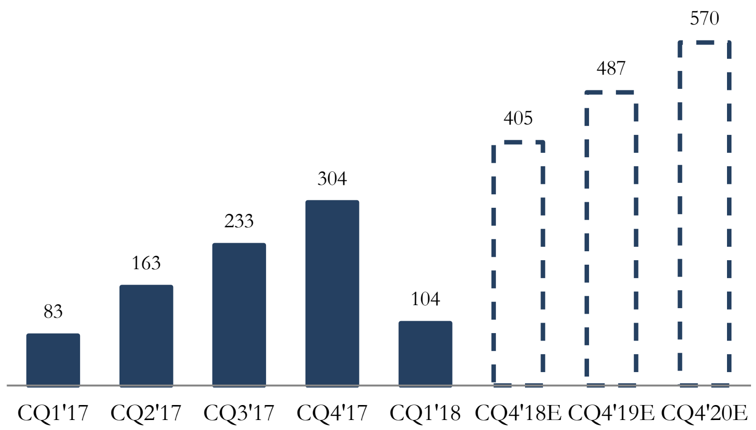
Source: NSE, Bloomberg, PAC Research

Operating profit bolstered as the company continue to monitor its operating expenses:

In the first quarter of 2018, the company's gross profit increased by 20.27% to ₦144.76 billion from ₦120.36 billion recorded in the first quarter of 2017. During the period, administrative expenses increased by 18.30% to ₦11.85 billion in Q1'18 (vs. ₦10.12 billion in Q1'17) while selling and distribution expenses increased to ₦29.57 billion in Q1'18 from ₦27.76 billion in Q1'17, representing an increase of 6.51%. In general, the increase in total selling and administrative expenses can be attributed to increased costs in Pan-African operations in Congo and Sierra Leone ramped up. The depreciation of Naira from ₦305/$1 at the end of Q1'17 to ₦337/$1 in Q1'18 also contributed about ₦1.50 billion to the general increase in operating costs of Pan-African operations when they were converted to Naira. However, the administration and selling expenses in Nigeria remained broadly stable at about ₦25.00 billion. As a result, profit from operating activities increased by 24.67% to ₦103.79 billion in Q1'18 (vs. ₦83.25 billion recorded in Q1'17). However, total operating expenses margin slightly reduced to 17.11% in Q1'18 from 18.15% recorded in Q1'17 while operating profit margin increased to 42.87% in Q1'18 from 39.99% reported in Q1'17.

In general, the increase in total selling and administrative expenses can be attributed to increased costs in Pan-African operations in Congo and Sierra Leone ramped up

Fig. 8: Operating Profit - Cumulative Quarters CQ1'17- CQ4'20E (Billion NGN)

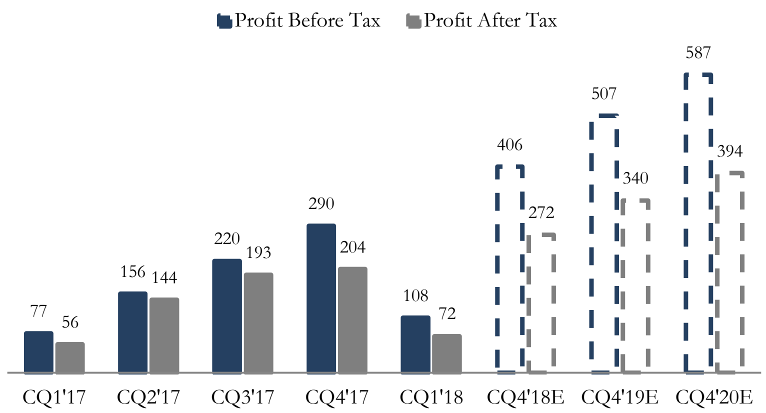


Source: NSE, Bloomberg, PAC Research

Even with higher tax provision, bottom line increased by 29.10% YoY: Outstanding performance from finance income, coupled with impressive performance from operating activities of the company boosted the profit before tax by 40.21% to ₦108.40 billion in Q1'18 from ₦77.32 billion published in Q1'17. Meanwhile, the company made adequate provision for tax in the first quarter of 2018 as tax holiday it used to enjoy in previous years has elapsed. However, the approval for tax relief, which the company is entitled to under Pioneer Status Incentive (PSI), is still pending. The company made a provision of ₦36.28 billion for tax in Q1'18 from ₦21.45 billion (revised from ₦6.75 billion) in Q1'17, representing an increase of 69.13%. Generally, the strong operating performance of the company and impressive performance from finance income offset the effect of higher tax provision on profit after tax as it increased by 29.10% to ₦72.12 billion in Q1'18 (vs. ₦55.87 billion published in Q1'17)

Generally, the strong operating performance of the company and impressive performance from finance income offset the effect of higher tax provision on profit after tax as it increased by 29.10% to ₦72.12 billion in Q1'18…

Fig. 9: Profit before Tax and Profit after Tax – CQ1'17- CQ4'20E (Billion NGN)



Source: NSE, Bloomberg, PAC Research

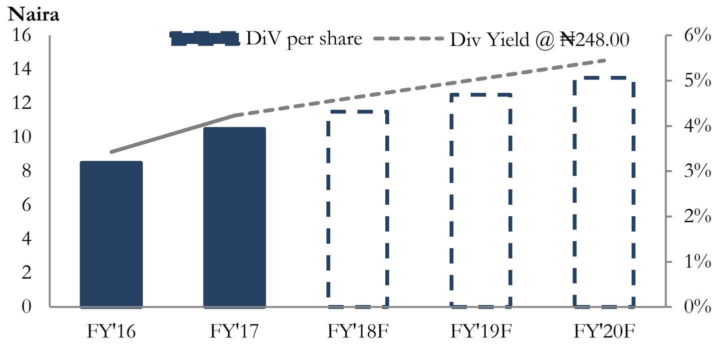
Dividend payment to shareholders in FY'18 is secured as the company's balance sheet remains strong:

During the period, the company increased its non-current asset by 3.11% to ₦1.26 trillion (vs. ₦1.22 trillion recorded in Q1'17) while total current assets increased by 50.77% to ₦457.07 billion in Q1'18 (vs. ₦303.16 billion reported in Q1'17). The increase in non-current assets is attributed to exchange gains on assets held outside Nigeria following the devaluation of the Naira which was partially offset by depreciation. With improvement in non-current assets and current asset, total assets rose by 8.88% to ₦1.72 billion in Q1'18 from ₦1.58 billion achieved in Q1'17. Total liabilities increased by 20.46% to ₦854.74 billion in Q1'18 (vs. ₦709.588 billion reported in Q1'17).

Consequently, the net assets of the company declined marginally by 0.57% to ₦864.23 billion in Q1'18 from ₦869.17 billion reported in Q1'17 while the NAPS of the company reduced marginally to ₦50.72 in Q1'18 from ₦51.01 in Q1'17.

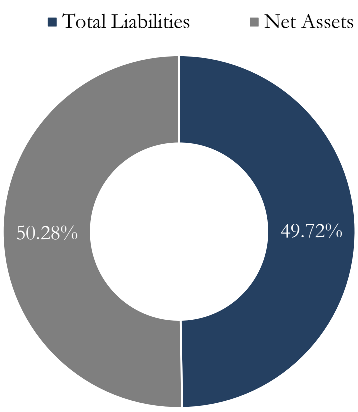
The increase in non-current asset is attributed to exchange gains on assets held outside Nigeria following the devaluation of the Naira which was partially offset by depreciation.

Fig. 10: Dividend Per Share and Dividend Yield (FY'16-FY'20F)



Source: NSE, PAC Research

Fig. 11: Total Liabilities Vs Net Asset in Q1'18



Source: NSE, PAC Research

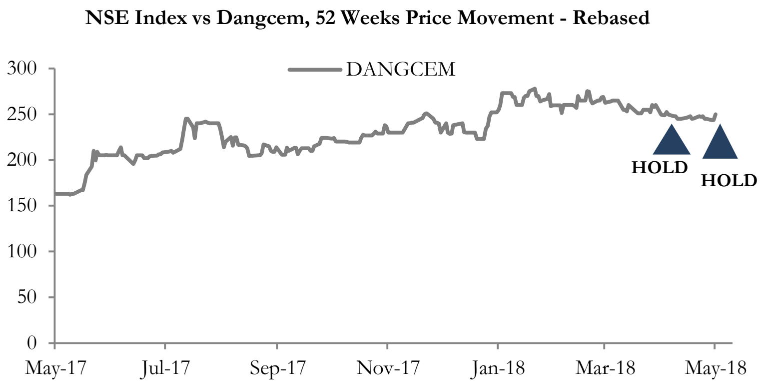
Valuation

Our valuation puts the target price of the stock at ₦263.05 representing an increase of 6.07% from the current price of ₦248.00. In arriving at the target price, we employed Discounted Cash flow Valuation methodology and Retained Earnings Model. Consequently, we maintained a **HOLD** 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 and the performance of the company in the cement industry

Our valuation puts the target price of the stock at N263.05 representing an increase of 6.07% from the current price of N248.00

Fig. 12: Share Price History



Source: NSE, PAC Research

Fig. 13: Statement of Profit or Loss, N'mn

	2016	2017	2018E	2019E
Revenue	615,103	805,582	974,754	1,174,579
Change		*30.97%*	*21.00%*	*20.50%*
Cost of Sales	(323,816)	(351,290)	(399,649)	(469,832)
Change		*8.48%*	*13.77%*	*17.56%*
Gross Profit	291,287	454,292	575,105	704,747
Change		*55.96%*	*26.59%*	*22.54%*
SG&A	(119,336)	(155,297)	(175,456)	(223,170)
Change		*30.13%*	*12.98%*	*27.19%*
Other Income	10,542	5,213	4,874	5,638
Change		*-50.55%*	*-6.51%*	*15.68%*
Operating profit	182,493	304,208	404,523	487,215
Change		*66.70%*	*32.98%*	*20.44%*
Finance Income	43,817	35,926	46,886	68,126
Change		*-18.01%*	*30.51%*	*45.30%*
Finance Cost	(45,381)	(52,711)	(45,193)	(48,360)
Change		*16.15%*	*-14.26%*	*7.01%*
Profit Before Taxation	180,929	289,590	406,216	506,981
Change		*60.06%*	*40.27%*	*24.81%*
Taxation	(38,071)	(85,342)	(134,051)	(167,304)
Change		*124.17%*	*57.08%*	*24.81%*
Profit After Taxation	142,858	204,248	272,165	339,677
Change		*42.97%*	*33.25%*	*24.81%*

Fig. 14: Statement of Financial Position, N'mn

	2016	2017	2018E	2019E
Fixed Assets	1,155,711	1,192,140	1,276,928	1,362,511
Intangible assets	4,145	6,355	6,569	7,915
Deferred tax assets	51,306	30,625	47,568	57,319
Inventories	82,903	94,594	105,468	127,089
Trade and other receivables	26,279	30,155	41,644	50,181
Bank and Cash Balances	115,693	168,387	175,456	193,806
Total current assets	303,164	410,299	454,428	529,967
Total Assets	1,529,104	1,665,883	1,816,430	1,993,637
Trade and other payables	268,966	270,721	282,679	317,136
Current tax payable	18,220	63,901	76,031	91,617
Financial debt	220,300	144,783	141,339	170,314
Other current liabilities	18,307	41,071	42,402	51,094
Total current liabilities	525,793	520,476	542,451	630,162
Deferred tax liabilities	103,162	116,898	144,264	173,838
Net Assets	725,528	781,360	898,524	911,052

Fig. 15: Profitability Ratio

	2016	2017	2018E	2019E
Return on Equity	19.69%	26.14%	30.29%	37.28%
Return on Assets	9.34%	12.26%	14.98%	17.04%
Gross margin	47.36%	56.39%	59.00%	60.00%
EBITDA margin	40.02%	47.47%	49.50%	48.50%
PBT margin	29.41%	35.95%	41.67%	43.16%
Net Profit Margin	23.23%	25.35%	27.92%	28.92%

Fig. 16: Asset Utilization

	2016	2017	2018E	2019E
cash/sales	0.19	0.21	0.18	0.17
Sales to inventory (x)	7.42	8.52	9.24	9.24
Sales to total assets (x)	0.40	0.48	0.54	0.59
Sales to total fixed assets	0.53	0.68	0.76	0.86
Equity multiplier	2.11	2.13	2.02	2.19
fixed asset turnover	1.88	1.48	1.31	1.16

Fig. 17: Liquidity Ratios

	2016	2017	2018E	2019E
Quick ratio	0.42	0.61	0.64	0.64
Current ratio	0.58	0.79	0.84	0.84
Cash ratio	0.22	0.32	0.32	0.31
Interest Coverage	3.99	5.49	8.99	10.48
Operating Cash Flow Ratio	1.22	1.44	1.58	1.63
Debt/net income	2.26	1.28	1.05	1.01
Debt/operating cash flow	0.50	0.35	0.33	0.34
Debt to asset	0.53	0.53	0.51	0.54
Total liabilities/equities	1.11	1.13	1.02	1.19
Inventory turnover	5.45	5.45	3.62	3.23
Inventory turnover days	67.00	67.00	67.00	67.00
Account payable days	211.00	211.00	211.00	211.00

Fig. 18: Shareholders' Investment Ratios

	2016	2017	2018E	2019E
EPS (₦)	8.38	11.99	15.97	19.93
DPS (₦)	8.50	10.50	11.50	12.50
NAVPS (₦)	42.58	45.85	52.73	53.46
Earnings yield (%)	3.38%	4.83%	6.44%	8.04%

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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