

24 March 2016

Ashaka Cement Plc. | Earnings Report

12 months ended 31st December, 2015

Rising competition eats into premium price advantage (₦19.63 - SELL)

- Ashaka Cement Plc. (Ashaka) released audited FY 15 results for 12 months ended 31st December 2015 wherein revenues declined 18% YoY (9M 15: -16% YoY) to ₦17 billion. PBT and PAT declined 39% (9M 15: -22% YoY) and 40% YoY (9M 15: 13% YoY) to ₦3.2billion and ₦2.8billion respectively.
- Ashaka proposed a dividend of ₦0.15 (FY 14: ₦0.45) which implies a dividend yield 0.6% using price as at last close.

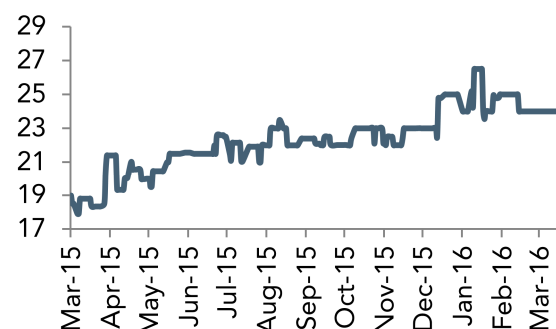
Revenue declines as price support gradually gives way

- Ashaka reported 26% YoY decline in Q4 15 revenues to ₦2.9 billion, mirroring over 20% YoY cut in cement prices to ₦24,688 per ton and ~6% YoY contraction in volumes to 115KT by our estimates. According to management, the company adjusted ex-factory gate prices in a bid to retain market competitiveness following Dangcem's 18% price slash and increased penetration into the 3.2MTPA North East cement market. In spite of this effort, we believe volume weakness still led to slight loss in Ashaka's market share over 2015 (i.e. -4pps YoY to 18%) in the North East.

Income Statement Data			
	2015 – 12M'm	2014 – 12M'm	%chg
Revenue	17,414	21,134	-18%
PBT	3,209	5,251	-39%
Tax	684	445	-35%
PAT	2,765	5,567	-40%

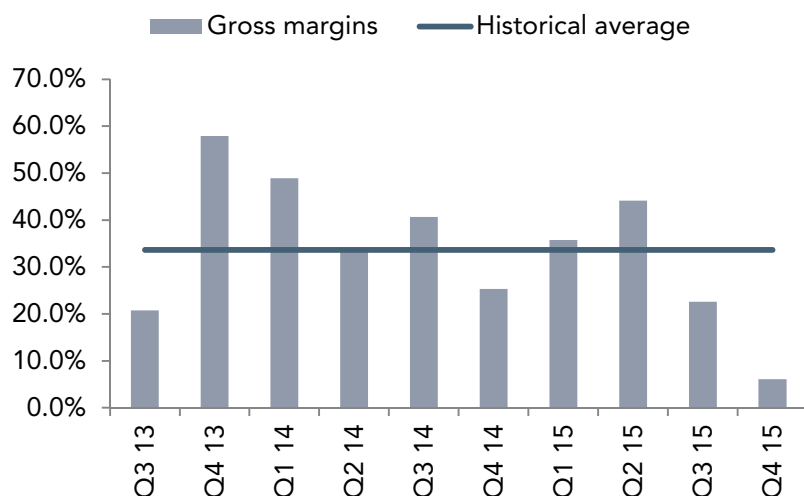
Balance Sheet Data			
	2015-Dec 'm	2014-Dec 'm	%chg
Inventory	4,508	3,464	30%
Receivables	8,558	7,176	19%
Cash	6,993	11,053	-37%
Payables	59,800	-	100%
Net Assets	53,015	51,262	3%

Stock Data	
Price	₦24.00
2 week range	₦17.82 – ₦26.50
Market Cap. (N'b)	53.747
1-month Avg. Vol	15,080
Curr. PE	22.1x
Bloomberg Ticker	ASHAKA:NL
Reuters Ticker	ASHAKA.LG

Ashaka Cement Plc- Share Price Trend

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- Q4 15 COGS declined a slower 6% YoY at ₦2.7 billion relative to revenues as pass-through from lower top-line drove an 82% YoY plunge in Q4 15 gross profits to ₦175 billion with related margins contracting 19.2pps YoY to 6.1% (lowest in the past 10 quarters).

Figure 1: Historical gross margin movement



Source: Company information, ARM Research

One-off redundancy cost drives Q4 15 loss

- On other fronts, Ashaka's Q4 15 operating expenses declined 15% YoY to ₦1.7 billion, reflecting savings from staff rightsizing over the period. Nevertheless, feed-through from weaker top-line as well as Q4 15 other operating cost of ₦171 million due to one-off redundancy cost following the company's staff cull cascaded to operating loss of ₦1.7 billion over the review period (vs. loss of ₦1 billion in Q4 14). Further exacerbating earnings pressures was the reported 63% YoY contraction in net finance income to ₦465 million, which bloated Q4 15 pre-tax loss by almost three fold YoY to ₦1.2 billion.

Earnings pressure to subsist over 2016 on lower prices

- Overall, Q4 15 result was affected by significant price and volume declines following the company's response to price changes in the industry. Although the

company retained a high coal to total energy ratio in its mix, its cost cutting strategy was too tame to offset the impact of top-line pressures on bottom-line.

- Given changes observed over Q4 15, we have reviewed our models to reflect ~21% price cut by the firm and also revised our volume growth expectation 6pps lower to 612KT (+8% YoY) in light of increasing competition in Ashaka's region of domicile. Beyond these, we have also pushed back our expectation for completion of capacity expansion project to YE 2018 (vs. 2017 previously) following our discussion with management at the start of 2016, wherein management hinged its decision to push back expansion plans on broadly weaker market conditions in the region. Given these adjustments, we now forecast 13% YoY contraction in FY 2016E revenue to ₦15 billion (vs. ₦25 billion in previous forecast).
 - On other fronts, we expect the company to continue to ramp up coal utilization in its energy mix (i.e. north of 90% in 2016E). Specifically, we are of the view that recent industry-wide margin compression makes the option of aggressive coal utilization a no-brainer for Ashaka. Consequently, we expect further gains on this front to ease cost to goods to sales ratio 2pps lower than in 2015 (i.e. 67%) in 2016E. In view of this, we expect input cost to decline 16% YoY to ₦10 billion and gross profits to come in 8% lower YoY at ₦5 billion with related margins at 33% (vs. 31% in 2015).
 - Although the company significantly reduced administrative costs in the final quarter of 2015, we expect the impact of higher distribution cost—following Ashaka's new strategy of transporting cement to the North West market due to insurgency concerns in the North East—to slightly offset most of these gains. This underpins our expectation of a mild 4% YoY contraction in operating expense to ₦3.2 billion. Consequently, we expect 2016 operating profits to decline 14% YoY to ₦1.7 billion (relative to ₦8 billion in previous forecast) with related margins unchanged at 11% relative to 2015.
 - Farther out, FGN's expressed desire to partner with Ashaka in the planned development of post-crisis North East should underpin a return to positive volume growth in the coming years, cascading to revenue growth CAGR of 26.34% over
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2016-2020 period (vs. CAGR of over 127% prior to adjustments). This revenue growth projection is firmly tied to our anticipation for an almost three-fold jump in plant capacity size to 3.5MTPA by 2019. Away from top-line, continued energy cost optimization should leave earnings in positive zones over our forecast horizon (i.e. more than double to ~~₦~~9.5 billion over our forecast horizon). Overall, we note that our price adjustments and push back in the completion time for capacity expansion have significantly narrowed earnings growth expectation relative of prior forecast (more than three folds over forecast horizon to ~~₦~~16 billion).

- Net adjustments to our model have driven 23% contraction in our **FVE** to **₦19.63**. Ashaka also trades at 2016E EV/EBITDA of **8.2x** relative to 6.1x for Bloomberg EMEA peers. Relative to the stock's last closing price, our FVE is at a discount of 18%, implying a downgrade in our recommendation to **SELL** (vs. NEUTRAL in previous communication).
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Summary of Results and Forecasts

ANNUAL					
Income Statement (N'millions)	FY 2015A	FY 2016F	FY 2017F	FY 2018F	FY 2019F
Revenue	17,415	15,109	18,022	19,749	34,560
COGS	12,020	9,519	11,354	12,442	21,773
Gross Profit	5,395	5,590	6,668	7,307	12,787
Operating Cost	3,376	3,248	3,316	3,812	6,670
Operating Profit	1,988	2,312	3,322	3,466	6,087
Interest income	1,221	1,118	1,265	1,484	1,721
Interest expense	-	-	-	-	-
PBT	3,209	3,430	4,587	4,950	7,809
Tax	445	480	642	693	1,093
PAT	2,765	2,950	3,945	4,257	6,716
Balance Sheet (N'millions)					
Assets	FY 2014A	FY 2015F	FY 2016F	FY 2017F	FY 2018F
Fixed Assets	48,605	47,988	47,751	47,734	49,494
Stocks	2,898	3,141	3,974	3,857	6,750
Trade debtors	540	499	613	602	1,037
Cash and other bank balances	17,008	20,095	22,942	27,379	31,542
Total Assets	69,129	71,802	75,358	79,651	88,901
Liabilities					
Trade Creditors	3,532	3,903	4,428	5,350	9,362
Long Term Liabilities	12,919	13,125	13,354	13,701	14,169
Total liabilities	16,808	17,386	18,142	19,412	23,894
Shareholders' fund	52,322	54,416	57,216	60,239	65,007
Key Ratios	FY 2015A	FY 2016F	FY 2017F	FY 2018F	FY 2019F
P/E	19.44	18.22	13.63	12.63	8.00
EV/EBITDA	9.32	7.10	5.38	4.51	2.62
ROA	4%	4%	5%	5%	8%
ROE	5%	6%	7%	7%	11%
Net Margins	16%	20%	22%	22%	19%
EPS	1.23	1.32	1.76	1.90	3.00
DPS	0.15	0.31	0.45	0.51	1.09
BVPS	23.36	24.13	25.24	26	29.14
Dividend yield	0.6%	1.3%	1.9%	2.1%	5%

Source: ARM Research

ARM ratings and recommendations

ARM now employs a two-tier rating system which is based on systemic importance of the security under review and the deviation of our target price for the stock from current market price. We characterize systemic importance as a function of a stock's ranking among the group of top 20 stocks by NSE market capitalization over a trailing 6 month period (minimum) to the review date. We adopt a 5 point rating system for this category of stocks and a 3 point rating system for stocks outside this group. The choice of top 20 stocks arises from the consideration that this group of stocks constitutes >75% of overall market capitalization and stocks outside this group are generally less liquid and individually account for <<1% of market capitalization. For stocks in both categories, the basis for ratings subject to target price deviation is outlined below:

TOP 20		NON-TOP 20	
Rating	Deviation	Rating	Deviation
STRONG BUY	>20%	BUY	>20%
OVERWEIGHT	10% — 20 %	NEUTRAL	5% — 20 %
NEUTRAL	0% — 10 %	SELL	<5%
UNDERWEIGHT	-5% — 0%		
SELL	<-5%		

RECOMMENDATION KEY	
Rating	Recommendation
BUY	Accumulate security to a substantial extent constrained only by portfolio diversification considerations
OVERWEIGHT	Accumulate security to an extent moderated by cognizance of its benchmark weight
NEUTRAL	Maintain status quo for security with respect to current holding—i.e. keep if already holding and don't buy otherwise—subject reasonable portfolio constraints
UNDERWEIGHT	Minimise exposure to security taking cognizance of its index weighting
SELL	Sell-off security completely from portfolio

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