

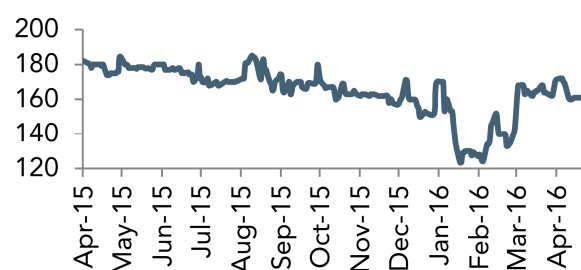
Dangote Cement Plc | Earnings Report

3 months ended 31st March, 2015

Energy challenges drive margin compression (₦166.52 - NEUTRAL)
Top-line growth subsists on higher volumes

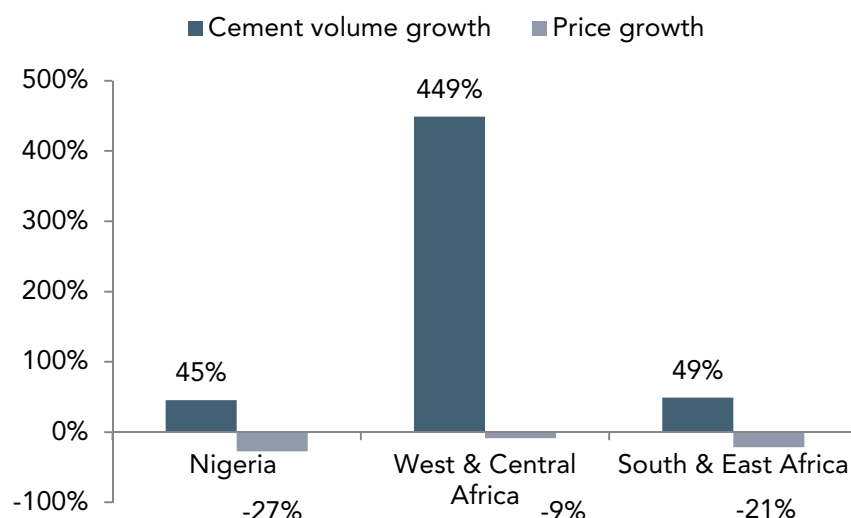
- Dangote Cement Plc. (Dangcem) reported 23% YoY increase in revenues to ₦141 billion over Q1 16 in line with our forecast. Advance in top-line was underpinned by another jump in volumes to 6.5MT (+70% YoY), which offset lower average cement prices of ₦21,790 per ton (-28% YoY) over the period.
- Cascading to regions, revenue in Nigeria rose 6% YoY to ₦107 billion as record volume sales of 4.5MT (+12.5%YoY) offset lower average prices of ₦23,743 per ton. The surge in volume, which follows a similar climb in the preceding quarter, suggests that Dangcem's low pricing strategy—implemented in Q4 2015—continued to stimulate demand over Q1 16. Nevertheless, in contrast to Q4 15, Dangcem's market share contracted 2pps QoQ to 66%, suggesting that competitors managed to claw back some market share after they adopted similar pricing late in Q4 15.
- Away from Nigeria, the company posted strong topline growth in West & Central Africa (over five-fold YoY to ₦24 billion) and South & East Africa (+17% YoY to ₦10 billion). Importantly, growth on the West & Central Africa front mainly reflects maiden first-quarter sales from the factory in Ethiopia and doubling of sales in Ghana, while growth in South & East Africa reflects

Income Statement Data			
	2016 – 3M'm	2015 – 3M'm	%chg
Revenue	140,521	114,738	23%
PBT	54,539	70,168	-22%
Tax	1,760	1,548	14%
PAT	52,779	68,620	-23%
Balance Sheet Data			
	2016-Mar 'm	2015-Dec 'm	%chg
Inventory	50,997	53,118	24%
Receivables	15,168	11,544	31%
Cash	65,742	40,792	61%
Payables	162,695	127,597	28%
Net Assets	707,343	644,720	10%
Stock Data			
Price	₦161.00		
2 week range	₦122.90– ₦188.68		
Market Cap. (N'b)	2,752		
1-month Avg. Vol	466,473		
Curr. PE	16.3x		
Bloomberg Ticker	DANGCEM:NI		
Reuters Ticker	DANGCEM.LG		
Dangote Cement Plc- Share Price Trend			


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production ramp up in Zambia and Tanzania¹.

Figure 1: Cement and price volume growths over Q1 16



Source: Company financials, ARM Research

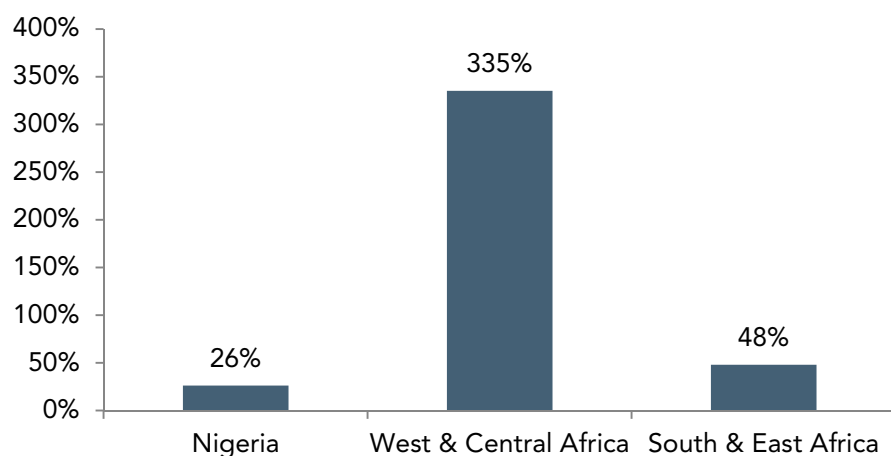
...though significantly higher energy cost stokes margin compression

- Q1 16 COGS rose significantly faster than revenues (+56% YoY to ₦62 billion), leaving gross profits only up 5% YoY to ₦78 billion with related margins contracting 9.4pps YoY to 55.7%. Input cost pressures in the quarter were mainly driven by significant increases in fuel & power consumed (over two-fold YoY to ₦22 billion) and material costs (+74% YoY to ₦17 billion) in the review period. On the former, management reported significant gas disruption over the quarter, with energy utilization at Ibese averaging 34% gas, 52% coal and 14% LPFO (Q1 2015: 85%, 15%, 0%) while utilisation at Obajana averaged 72% gas, 15% coal and 13% LPFO (Q1 2015: 92%, 1%, 7%). Management highlighted that energy cost pressures were underpinned by the ramp up LPFO, which, despite the decline in its price (-16% YoY to ₦54.17) in tandem with oil prices, remained 3x more expensive than coal and gas. In addition to energy pressures, margin compression also reflects impact of significantly depressed prices over the period.
- Furthermore, OPEX pressures subsisted over Q1 16 (+27% YoY to ₦22 billion)

¹ Dangcem grouped Ethiopia in West & Central Africa region for reporting purpose.

mainly due to continued ramp-up of selling and distribution expenses outside Nigeria as well as promotional activities across regions. Consequently, Q1 16 operating profit declined 4%YoY to ₦56 billion with related margins contracting sharply to 39.9% (Q1 15: 50.9%).

Figure 2: Growth in operating cost by region



Source: Dangote Cement Plc, ARM Research

- Compounding the pressure was a reported net finance cost of ~₦2 billion in Q1 16 (vs. net finance income of ₦12 billion in corresponding period of 2015) which drove PBT and PAT lower to ₦55 billion (-22% YoY) and ₦53 billion (-23% YoY) respectively. Thus, PBT and PAT margins both compressed 22pps YoY to 38.8% and 37.6% respectively.

Higher energy cost to pressure 2016 earnings

- Despite strong top-line growth, Dangcem's Q1 16 earnings performance was scarred by high cost (input and opex) as well as net finance charges. Responding to the cost pressures, the company raised prices by ₦100 to ₦1540 per 50kg bag of cement. However, it appears there were multiple price adjustments over Q1 16, as current price is ~30% higher than the average Q1 16. Notwithstanding management's rationale for this price increase, we think the decision is more reflective of the company's strength as market leader in the domestic market as prices in other regions were left unchanged despite operating margins being nearly 33pps lower.

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- That said, we believe this upward price adjustment is broadly positive for the company. In particular, following delays in the passage of 2016 budget, we think—when the budget is eventually signed into law—implementation of the record capex of ₦1.8 trillion will be accelerated over the second half of the year, helping to sustain demand for cement. In view of this, we have left our volumes expectations unchanged at 29% YoY to 24.2MT for the group. However, given the hike in prices, we have raised our 2016 average cement price estimate by 22% to ₦29,000 per ton for Nigeria (vs. current realizable prize of ₦30,800), mindful of the significantly low price over the first quarter of the year. Thus, we now expect group revenues to rise 19% YoY to ₦585 billion over 2016 (vs. +6% YoY to ₦519 billion in previous estimate).
 - For costs, we now expect COGS to rise 33% YoY to ₦269 billion (vs. +13% YoY to ₦228 billion in previous estimates) as delays in completing repair works at the damaged Trans Forcados pipeline suggest current gas challenges are likely to linger for most of the year. Similarly, we have revised our OPEX estimate 9% higher from previous based on management's plans to add an additional 14,000 retail outlets over 2016. Consequently, our operating profit estimate is now 5% higher than previous at ₦224 billion (+8% YoY). Leaving our estimate for net finance charges unchanged, our FY 2016E PAT is now 5% higher YoY at ₦200 billion (+ 6% YoY).
 - Over our forecast horizon (2016 – 2020), we now expect revenue and earnings CAGR of 17.37% and 25% respectively (vs. 15% and 21% prior to current adjustment). Net impact of these adjustments result in 8% rise in our FVE to **₦166.52**, which currently stands at a 3% upside from the stock's last market price. Dangcem trades at current EV/EBITDA of 10.5x relative to 9.0x for Bloomberg EMEA peers. Recent adjustments have however led to an upgrade in our recommendation to **NEUTRAL** (vs. SELL in previous communication).
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Summary of Results and Forecasts

QUARTERLY					
Income Statement (N'000,000)*	Q1 2016A	Q2 2016F	Q3 2016F	Q4 2016F	
Turnover	140,521	122,663	146,213	175,456	
COGS	62,204	66,932	69,948	69,948	
Gross Profit	78,317	55,731	76,265	105,507	
Operating Costs	22,409	23,911	25,090	25,090	
Operating Profit	56,130	33,844	52,391	81,634	
Net Finance costs	-1,591	-10,327	-5,959	-5,959	
Profit Before Taxation	54,539	23,517	46,432	75,675	
Taxation	1760	4245	3002	3002	
Profit After Taxation	52,779	19,272	43,430	72,672	
ANNUAL					
Income Statement (N'000,000)*	FY 2015A	FY 2016A	FY 2017F	FY 2018F	FY 2019F
Revenue	491,725	584,853	651,195	801,247	946,780
COGS	201,808	269,032	280,014	320,499	369,244
Gross Profit	289,917	315,821	371,181	480,748	577,536
Operating Cost	86,046	96,501	81,399	76,118	75,742
Operating Profit	207,822	223,999	294,992	411,040	509,368
Interest income	34,819	31,883	30,693	30,679	22,806
Interest expense	54,347	55,720	39,265	29,523	21,627
PBT	188,294	200,162	286,419	412,196	510,547
Tax	6,971	12,010	34,370	65,951	102,109
PAT	181,323	188,152	252,049	346,244	408,437
Balance Sheet (N'000,000)*					
Assets					
Cash & Short term funds	917,212	979,929	1,023,551	1,073,221	1,122,367
Net Loans	53,118	72,639	60,154	59,790	82,521
Fixed Assets	11,544	11,697	13,381	17,937	22,041
LT investment	40,792	23,061	(8,493)	(19,486)	(24,822)
Other Assets	1,110,943	1,191,108	1,183,249	1,245,162	1,331,244
Total Assets					
Liabilities	127,597	185,632	156,922	179,370	206,302
Deposits	265,525	251,047	224,056	189,258	152,646
Borrowings	466,223	495,598	426,660	404,382	388,745
Total liabilities	644,720	695,510	756,589	840,780	942,500
Shareholders' fund	917,212	979,929	1,023,551	1,073,221	1,122,367
Key Ratios					
P/E	15.13	14.58	10.88	7.92	6.72
EV/EBITDA	11.27	10.53	8.29	6.14	5.00
ROA	17%	16%	21%	28%	31%
ROE	29%	28%	35%	43%	45%
Net Margins	37%	32%	39%	43%	43%
EPS	10.64	11.04	14.79	20.32	23.97
EV/EBITDA	11.27	10.53	8.29	6.14	5.00
P/B	4.26	3.96	3.61	3.00	3.00
Dividend yield	4.9%	5.1%	6.8%	9.3%	11.0%

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 to 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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