

Price	₦16.40
52-week range	₦10.80-27.50
Market Cap. (₦bn)	215.553
1-month Avg. Vol	164,464
Curr. PE	10.9x

CCNN.NL - Share Price Trend



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Cement Co Northern Nigeria PLC. (CCNN.NL)

Equity Commentary

OBU-CCNN Merger... Some value accretion with few blurry lines

- We recently received the scheme of merger document showing details of the proposed merger between CCNN and sister company, OBU Cement (“OBU”), as announced in late October. The merger entails absorption of all CCNN’s assets, liabilities and undertakings by OBU Cement and consequently a delisting of CCNN’s shares from the Nigerian Stock Exchange (NSE) on January 8th, 2020 and listing of the enlarged entity on same day. Upon conclusion of the merger, existing OBU and CCNN shareholders will hold 61.2% and 38.8% of the enlarged OBU which will have total of 33.8 billion shares. For context, pre-merger, OBU held 40 million units of shares (100% held by BUA Group) which is being reconstructed in a 1-for-518 exchange ratio and increased to 20.7 billion units, while CCNN’s 13.1 billion shares, was included in the enlarged entity on a 1-for-1 exchange ratio.

Table 1: Shareholding Structure pre and post-merger

Description	CCNN	OBU	Enlarged-OBU
BUA Cement Company Limited	87.42%		33.93%
Abdulsamad Rabi, CON		90.00%	55.07%
Isiaku Rabi		10%	
Others	12.58%		11.00%
Total	100%	100%	100%
Number of shares	13,143,500,966	20,720,853,094	33,864,354,060

Source: Company Financial, ARM Research

- Going by the valuation provided in the scheme document (See here: ***CCNN_Obu Scheme Document***), the additional shares to be created by OBU to integrate all shareholders of CCNN, is valued at ₦460,022,533,810. This translates to a per share valuation of ₦35, which is at a premium to CCNN’s current 9M 19 BVPS of ₦25.6 and market price of ₦16.4. The merger consideration is at a 74% premium to our FVE of ₦20.14 for CCNN. At the end of the merger the equity value of the enlarged entity will settle at ₦1.2 trillion.
- Unlike the previous merger of CCNN and Kalambaina, we see some value accretion for existing CCNN shareholders from the merger.*** Combining the published FY 18 numbers of both CCNN and OBU (which is yet to reflect the additional 3 MT launched in November 2018) and also adjusting for the increase in the enlarged entity shares to 33.9 billion, we note that the combined entity’s earnings per share and ROE would

have settled at ₦1.90 and 15% respectively (excluding the impact of prior years' cumulative tax benefit of OBU in 2018, EPS and ROE would have been ₦0.80 and 6.5% respectively), compared to reported ₦0.44 and 2% respectively by CCNN. However, the higher EPS and ROE are still below the respective level reported by CCNN as a standalone business in 2017 of ₦2.57 and 22%.

- Upon conclusion of the merger, total production capacity of the enlarged entity will increase to 8MT, comprising CCNN's 2MT plant in Sokoto and OBU's 6MT in Okpella, both of which include new 1.5 MT and 3MT which came on board late 2018, respectively. Based on CCNN's price per ton, we estimate that both entities produced 2.8MT in 2018 which translates to a utilization rate of 80% – CCNN on an adjusted basis: 59% and OBU: 68% on 3MT. Interestingly, reflecting the improved energy source at CCNN (now largely coal) starting Q2 2018 and a largely gas powered plant in OBU, by our estimate, the enlarged entity's gross margin of 51% inches closer to DANGCEM's leading margin of 57.5% and above Lafarge Africa's of 31% (Ex-South Africa).

Table 2: Key Financials Pre and Post-merger

FY 18 Financials	GCNN	OBU	Enlarged OBU
Energy source	Coal & LPFO	Gas	Gas, Coal & LPFO
Number of shares ('Mn units)	13,143,502	40,000	33,864,354
Revenue (₦'000)	31,721,962	87,290,610	119,012,572
EBIT (₦'000)	7,874,575	35,149,843	43,024,418
PAT (₦'000)	5,731,320	58,585,867	64,317,187
COGS per ton (₦)	(23,592)	(19,727)	(20,757)
Gross margin	45%	54%	51%
EPS (₦)	0.44	1,465	1.90
ROE	2%	68%	15%
Debt to Capital	0.16%	4% ¹	0.93%
BVPS (₦)	25.37	2,150.37	12.39
P/B (x)	0.65	0.01	1.32
P/E (x)	37.61	0.01	8.63
Interest coverage	18.7x	10.6x	11.5x

Source: Company Financial, ARM Research

- Similar to CCNN, OBU also has minimal leverage on its balance sheet and high interest coverage. As at FY 18, OBU had only ₦3.4 billion as outstanding to external parties, but ₦124 billion was classified as due to related companies which we suspect will be indebtedness to the parent company BUA for financing the OBU plant. Further discussions with management show that the completed 3MT plant in 2018, is yet to reflect in the 2018 balance sheet available in the scheme of merger. Thus, we envisage OBU could tow a similar path to bring in the 3MT OBU plant II into the books upon consolidation as a due to related party obligation. Combining the related party obligation and borrowings which summed to ₦127.5 billion, total interest payment of ₦3.3 billion over 2018 translates to an unweighted average cost of 3% (4-year average: 3.84%). Except we see a change to the cost of financing the new plant, we believe the impact of the addition of the plant will more than outweigh additional finance cost on a related party basis.

¹ Excluding the N128 billion due to related companies. Including the

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- The enlarged OBU stands to benefit from pioneer tax status on both of the new plants in Kalambaina and Okpella. To mention, OBU enjoyed tax credits of ₦27 billion which pushed PAT to ₦59 billion in 2018. Going through NIPC's quarterly reports, the only application made so far, has been on the Kalambaina Cement plant in March 2019 and pioneer tax credit on the OBU plant I was granted in 2015 and will expire in May 2019.
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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 reas portfolio constraints
UNDERWEIGHT	Minimize exposure to security taking cognizance of its index weighting
SELL	Sell-off security completely from portfolio

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