

Stronger outing expected despite concerns

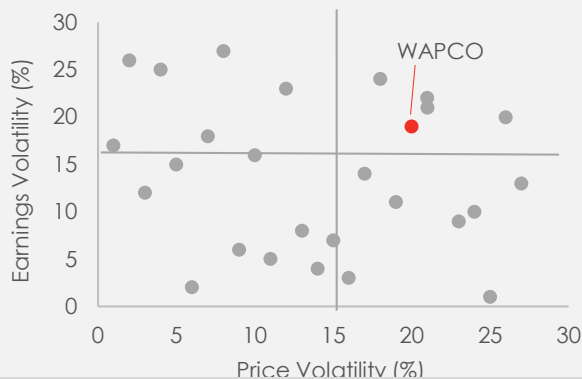
30th March, 2021

Research Analyst:

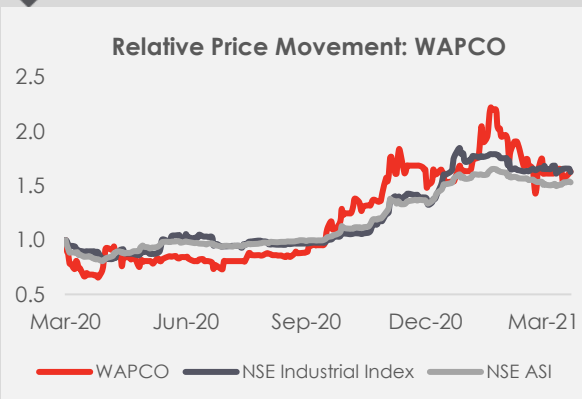
Ayooluwa Aseweje

+234-(0)813-767-0892

Ayooluwa.aseweje@unitedcapitalplcgroup.com

Risk Rating: High**Key Data**

Last Price (₦)	22.25
Last Price (\$)	0.05
52 week High/Low (₦)	30.3/ 8.95
1M Price Change (%)	6.0
3M Price Change (%)	5.7
6M Price Change (%)	48.3
YTD Change (%)	5.7
Beta	1.02
Market Capitalization (₦'bn)	358.4
Market Capitalization (\$'mn)	879.0
Shares Outstanding. (Units'bn)	16.1
Float (%)	99.9
Dividend Yield (%)	4.5

Price Performance Chart
Stock Rating
BUY
Target Price
N27.7
Expected Return
24.3%

Lafarge Africa Plc (WAPCO) released its FY-2020 results last week, showing a 98.8% y/y rise in PAT to N30.8bn. Lafarge's revenue (up 8.3% y/y to N230.6bn) grew faster than its cost of sales (up 4.0% to N163.3bn) during the period. This, coupled with improved operating cost management (9.4% of revenue vs 9.9% in FY-2019) and a marked decline in finance costs (-51.9% y/y), resulted in a whopping 110.0% y/y increase in PBT to N34.3bn. Notably, the drop in finance costs, due to balance sheet restructuring, was again at the heart of the improvement in profitability. We review WAPCO's latest financials, and our valuation estimates below.

Topline performance bolstered by sector-wide demand recovery

Following a 5.1% y/y slump in revenue in Q2-2020, which threatened the sales outlook, the easing of lockdown measures, which largely took effect in Q3 2020, supported a turnaround in WAPCO's full-year revenue (up 8.3 % y/y to N230.6bn vs N239.8bn est.), as Cement sales (98.1% of total revenue) rose by 9.1% y/y while revenue from Aggregates and Concrete Products (1.2% of total revenue) declined by -25.5%.

WAPCO managed to keep its input costs in check, as Cost of Sales climbed moderately, in comparison to Revenue (Cost of Sales up 4.0% y/y to N163.3bn). As such Cost margin dropped 289bps y/y to 70.8% in FY-2020. Fuel and power costs (up 21.7% to N38.6bn) were mainly responsible for the increase in Cost of Sales, according to the cost breakdown. However, the cost of materials and consumables remained stable, and lower production (down 2.6% to N23.8bn) and fixed distribution costs (down 59.3% to N1.8bn) helped alleviate cost pressures, as shown by the increase in Gross Margin (29.2% in FY-2020 vs 26.3% in FY-2019).

EBITDA was up 16.0% on the back of turnaround initiatives vis-à-vis WAPCO's "Health, Cost and Cash" strategy to cut down on excessive operating expenses, which climbed by 2.5% y/y to N21.5bn. Specifically, the company curtailed Selling and Marketing expenses

Stronger outing expected despite concerns

(down -17.2% to 4.2bn), as advertising, campaign and innovation expenses fell dramatically. This offset increases in Directors costs (up 391.4% to N174.3m) and staff-related expenses (up 15% to N6.2bn). This made for a decent operating performance as the company posted a 217bps increase in EBITDA margin to 32.7%.

Balance sheet improvements drive finance costs lower, prop up Net Income

WAPCO sustained its efforts in deleveraging its balance sheet as Total Debt declined by 22.5% y/y to N49.7bn. Notably, the company's Debt to Total Capital ratio improved to 0.41x (from 0.44x in FY-19 and a 1.76x 5-year average). Consequently, Net finance cost tumbled 49.9% y/y, driven by a 51.9% drop in interest expense to N9.7bn, further aided by the low-interest rate environment. As a result, Pre-tax profit surged 110.0% y/y to N37.6bn while Post-tax profit grew 98.8% y/y to N30.8bn.

Additionally, effective working capital management, particularly in terms of inventories (inventory turnover of 5.1x vs 4.0x in FY-2019) and trade receivables (receivables turnover of 7.3x vs 5.4x in FY-2019), aided cash generation (Cash and cash equivalents grew 96.7% to N53.3bn).

Outlook: Stronger outing expected despite concerns

Looking ahead, we are cautiously optimistic about WAPCO. Although we expect continued revenue growth driven by broader demand trends and economic momentum, which should drive higher volumes. The company's operational difficulties (particularly in its Ewekoro and Mfamosing plants), which were mostly illustrated in its Q4-2020 performance (revenue rose by just 1.5% y/y), weigh slightly on our outlook. Specifically, we have forecasted a 9.0% y/y growth in Revenue as we expect a stronger outing in FY-2021 hinged on management guidance on the resolution of the operating challenges experienced in Q4-2020 which capped revenue growth. On the cost level, we expect the company's cost optimization strategies to bear more fruit, and input costs to normalize later in the year, allowing for margin improvement. However, we express our concerns over the depressed marketing spend, considering competitors' marketing strategies and the intensifying competition for market share. In all, we estimate a 16.9%y/y improvement in EPS to N2.2/share.

Adjusting our model estimates for the new assumptions, higher risk-free rate and country risk premium, we review our year-end target price downward to N27.7/share, from N32.5/share. The stock's current market price of N22.25/share reflects a 24.3% discount to our year-end Target Price. Also, the counter currently trades at a P/E of 11.6x, compared with domestic peers, DANGCEM (13.9x) and BUACEMENT (35.3x). Thus, we maintain our BUY rating on the ticker.

**...we estimate a 16.9%
y/y improvement in EPS
to N2.2/share**

Stronger outing expected despite concerns

Financial Highlights (N'Mn)

Headlines	FY- 2020	FY- 2019	Change
Revenue	230,573	212,999	8.3%
Cost of sales	-163,333	-157,047	4.0%
Gross Income	67,240	55,952	20.2%
Net Finance (cost)/Income	-8,534	-17,018	-49.9%
Profit/Loss Before Tax	37,572	17,892	110.0%
Taxation	-6,730	-2,374	183%
Profit/Loss After Tax	30,842	15,518	98.8%
	FY- 2020	FY- 2019	
Cash and cash equivalents	53,323	27,104	96.7%
Trade & Other Receivables	5,029	8,193	-38.6%
Trade & Other Payables	76,858	69,718	10.2%
Net Assets	359,639	344,914	4.3%
Gross Margin	29.2%	26.3%	2.9%
Net Margin	13.4%	7.3%	6.1%
Cost to Sales	70.8%	73.7%	-2.9%
Leverage (Total Liabilities/ Total Assets)	29.1%	30.6%	-1.5%
Price(N)	22.3		
EPS(N)	1.9		
BVPS(N)	22.3		
P/E(X)	11.6		
P/BV	1.0		
ROAE	8.8%		
Proposed Dividend	1.00		
Dividend Yield	4.5%		
Qualification Date	30th-Apr-2021		
Closure Date	7th-May-2021		
Payment Date	25th-May-2021		

Sources: Company Financials, United Capital Research

Disclosure Appendix

Investment Rating Criteria and Disclosure

United Capital Research adopts a 3-tier recommendation system for assets under our coverage: Buy, Hold and Sell. These generic ratings are defined below:

Buy: Based on our valuation and subjective view (if any), the expected upside on the stock's close price as at 31st December is greater than the Asymmetric Corridor around the MPR of the Central Bank of Nigeria (which is currently MPR – 500bps; i.e 9%). We consider this as the minimum return that may deserve our holding of a risk asset, like equity.

Hold: Based on our valuation and subjective view (if any), the expected upside on the stock's close price as at 31st December is greater zero but less than the Asymmetric Corridor around the MPR of the Central Bank of Nigeria (which is currently MPR – 500bps; i.e 9%).

Sell: Based on our valuation and subjective view (if any), the expected upside on the stock's close price as at December 31st is less than zero.

NR*: Please note that in addition to our three rating heads, we indicate stocks that we do not rate with NR; meaning Not-Rated. We may not rate a stock due to investment banking relationships, other sources of conflict of interests and other reasons which may from time to time prevent us from issuing a rating on the shares (or other instruments) of a company.

Please note that we sometimes give concessional rating on stocks, which may be informed by technical factors and market sentiments.

Conflict of interest: It is the policy of United Capital Plc and all its subsidiaries/affiliates (hereafter collectively referred to as "UCAP") that research analysts may not be involved in activities that suggest that they are representing the interests of UCAP in a way likely to appear to be inconsistent with providing independent investment research. In addition, research analysts' reporting lines are structured so as to avoid any conflict of interests. Precisely, research analysts are not subject to the supervision or control of anyone in UCAP's Investment Banking or Sales and Trading departments. However, such sales and trading departments may trade, as principal, on the basis of the research analyst's published research. Therefore, the proprietary interests of those Sales and Trading departments may conflict with your interests as clients. Overall, the Group protects clients from probable conflicts of interest that may arise in the course of its business relationships.

Risk Rating

Our Risk rating assesses the likelihood of market price deviating significantly from valuation fair prices. Risk factors limit gravitation of market prices towards target prices or result in significant decline in current price and thus swing buy/sell rating from positive to negative or vice versa. Risk factors are broadly grouped into systematic and unsystematic risk. Systematic risk (also called market risk or un-diversifiable risk) captures uncertainties or volatilities inherent to the entire market. This also includes macroeconomic shocks emanating from government actions or inactions, unanticipated policy pronouncements, external shocks and socio-political tensions which may swing market prices significantly away from targets. Unsystematic risk (specific risk, diversifiable risk or residual risk) on the other hand captures company or sector specific uncertainties which can mostly be reduced by diversification. These include labour union/industrial actions, corporate governance/management inefficiency, litigation, possible liquidation/winding-down of operation, internal labour unrest, government action, policy missteps as well as disruptions resulting from innovation, technology and technical progress etc.

United Capital Research adopts a 3-tier risk rating for assets under our coverage: High, Medium and Low. The rating scale is ordinal and captures the diverse risks that we deem applicable the company of focus. The ratings are defined below:

High: High probability of an imminent systematic risk or/and unsystematic risk

Medium: Slightly high (but lower compared to 'High') probability of an imminent systematic risk or/and unsystematic risk

Low: Low probability of an imminent systematic risk or/and unsystematic risk

Analyst Certification

The research analysts who prepared this report certify as follows:

1. That all of the views expressed in this report articulate the research analyst(s) independent views/opinions regarding the companies, securities, industries or markets discussed in this report.
2. That the research analyst(s) compensation or remuneration is in no way connected (either directly or indirectly) to the specific recommendations, estimates or opinions expressed in this report.

Other Disclosures

United Capital Plc or any of its affiliates (hereafter collectively referred to as "UCAP") may have financial or beneficial interest in securities or related investments discussed in this report, potentially giving rise to a conflict of interest which could affect the objectivity of this report. Material interests which UCAP may have in companies or securities discussed in this report are disclosed:

- UCAP may own shares of the company/subject covered in this research report.
- UCAP does or may seek to do business with the company/subject of this research report
- UCAP may be or may seek to be a market maker for the company which is the subject of this research report
- UCAP or any of its officers may be or may seek to be a director in the company(ies) covered in this research report
- UCAP may be likely recipient of financial or other material benefits from the company/subject of this research report

Company	Disclosure
Dangote Cement Plc	a,h
Fidelity Bank Plc	h
Flour Mills of Nigeria Plc	h
Forte Oil Plc	g
International Breweries Plc	a,h
Nigerian Breweries Plc	h
PZ Nigeria Plc	h
Stanbic IBTC Plc	g
Total Nigeria Plc	h
UAC of Nigeria Plc	h
Zenith Nigeria Plc	a

Disclosure keys

- a. The analyst holds personal positions (directly or indirectly) in one or more of the stocks covered in this report
- b. The analyst(s) responsible for this report (whose name(s) appear(s) on the front page of this report is a Board member, Officer or Director of the Company or has influence on the company's operating decision directly or through proxy arrangements
- c. UCAP is a market maker in the publicly traded equities of the Company
- d. UCAP has been lead arranger or co-lead arranger over the past 12 months of any offer of securities of the Company
- e. UCAP beneficially own 1% or more of the equity securities of the Company
- f. UCAP holds a major interest in the debt of the Company
- g. UCAP has received compensation for investment banking activities from the Company within the last 12 months
- h. UCAP intends to seek, or anticipates compensation for investment banking services from the Company in the next 6 months
- i. The content of this research report has been communicated with the Company, following which this research report has been materially amended before its distribution
- j. The Company is a client of UCAP
- k. The Company owns more than 5% of the issued share capital of UCAP

Disclaimer

United Capital Plc Research (UCR) notes are prepared with due care and diligence based on publicly available information as well as analysts' knowledge and opinion on the markets and companies covered; albeit UCR neither guarantees its accuracy nor completeness as the sole investment guidance for the readership. Therefore, neither United Capital (UCAP) nor any of its associates or subsidiary companies and employees thereof can be held responsible for any loss suffered from the reliance on this report as it is not an offer to buy or sell securities herein discussed. Please note this report is a proprietary work of UCR and should not be reproduced (in any form) without the prior written consent of Management. UCAP is registered with the Securities and Exchange Commission and its subsidiary, United Capital Securities Limited is a dealing member of the Nigerian Stock Exchange. For enquiries, contact United Capital Plc, Afriland Towers (3rd Floor), 97/105, Broad Street, Lagos. ©United Capital Plc 2021.