

Lafarge Africa Plc.

Making Hay While Prices Shine

After four successive quarters of losses, Lafarge Africa Plc (LAFARGE) reported N17.56 billion pre-tax profit in Q4-2016 on (1) price-driven 1004bps y/y and 3290bps q/q gross margin expansion, (2) other gains/operating income of N9.97 billion (vs. losses in previous quarters), and (3) investment/finance income of N2.88 billion (highest since Q2-2015). Of the above mentioned items that impacted the fourth quarter result, the restoration of gross margin to the pre-2015 price-crash levels (given the uncertainty of other items) will be most defining of LAFARGE's return to profitable performance in 2017. Consequently, we have revised 2017 PAT forecast higher to N25.8 billion, from N11.2 billion previously. The PAT is also reflective of the elimination of forex-related losses as well as relatively higher sales volume.

Cement prices in Nigeria are currently above the end-2016 levels, following the additional increases (twice) effected this quarter. We estimate LAFARGE's realized average Nigerian price to be 42% above 2016 average. In addition, we look for relatively lower per tonne production cost, given the earlier-than-expected progress made with energy substitution, and considering that about 50% of 2017 capex outlay will be committed to delivering energy optimization.

Notwithstanding the generally modest Nigerian cement consumption outlook, we forecast LAFARGE's Nigerian cement sales volume to increase by c.7%, as markets lost in 2016 on production challenges (which limited supply capability) are reclaimed. For reference, Q4-2016 realized volume was 39% and 3% above Q3 and Q2 levels (during which energy challenges adversely impacted production) respectively, despite the relatively higher price. In addition to pricing and efficiency gains, we estimate 2017 EBITDA of N64.34 billion, higher than both the previous estimate of N50.2 billion, and the N29.65 billion reported in 2016.

Following the revision to our forecasts, we have increased 2017 TP to N80.56 (from N60.10) and retain BUY recommendation on 107.37% upside. At current price, the stock is trading on a forward PE of 7.8x, at 37% and 5% discount respectively to Bloomberg's SSA and Nigerian comparables. While acknowledging the risks to earnings recovery in the short term, we think LAFARGE's shares have faced intense pressure and expect the market price to rise to our 2017 TP on relatively (compared to 2016) better performance.

Key risk is that notwithstanding the expected lower production cost, the strength of LAFARGE's profitability in 2017 has greater dependence on pricing development where we think the market leader (Dangote Cement) might a pull negative surprise. While updating on DANGCEM, we noted that the Group targets sizeable absolute Nigerian EBITDA in 2017 which is realizable under a lower price (from current level, but above 2016 average) scenario. From our sensitivity test, LAFARGE risks losing up to N9 billion of the above forecast 2017 EBITDA on N32,000-N34,000 realized average price scenario (from the N42,000 estimated). Target price under this scenario is N62.88, representing 57.60% upside from market value.

Income Statement (N'bn)	Q1-17	Q2-17	Q3-17	Q4-17
Revenue	66.19	73.44	74.05	62.27
Cost of sales	-46.33	-51.41	-51.84	-43.59
Gross profit	19.86	22.03	22.22	18.68
Operating expenses	-8.60	-9.55	-9.63	-8.09
Other expenses	-0.28	-0.28	-0.28	-0.28
EBIT	10.98	12.21	12.31	10.31
Other gains/(losses)	-0.11	-0.11	-0.11	-0.11
Investment income	0.42	0.42	0.42	0.42
Finance cost	-4.18	-4.18	-4.18	-4.18
Profit before tax	7.11	8.34	8.45	6.44
Taxation	-1.07	-1.25	-1.27	-0.97
Profit after tax	6.04	7.09	7.18	5.48

Source: Company Account, Cordros Research

BUY

Target Price (N)	80.56
Current Price (N)	38.85
Implied Return (%)	107.37

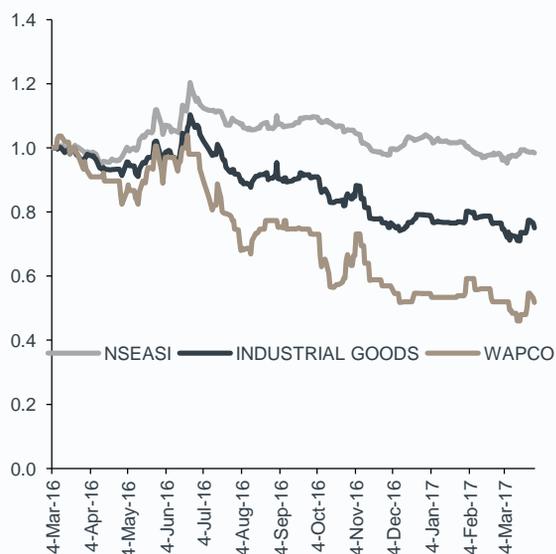
Company Data

NSE Code	WAPCO
Bloomberg Code	WAPCO:NL
Reuters Code	WAPCO.LG
Sector	INDUSTRIAL GOODS
Market Cap. (N'bn)	212.93
Free Float (%)	34.97

Ratios	Q4-16	Q4-15	2016FY
Gross margin	38.44%	28.39%	18.51%
Opex margin	17.94%	12.49%	13.99%
EBIT margin	37.49%	4.24%	-5.00%
PBT margin	29.91%	-4.43%	-10.39%
RoAE	39.43%*	15.98%*	7.95%
EPS (N)	9.58	-0.05	3.15

*Trailing 12m

Price movement (WAPCO vs. Benchmark Indices)



Source: NSE, Bloomberg, Cordros Research

Financial Statement (N'billion).

Statement of Comprehensive Income						Profitability Ratios					
	2014a	2015a	2016a	2017f	2018f		2014a	2015a	2016a	2017f	2018f
Turnover	260,810	267,234	219,714	275,954	287,307	Gross profit margin	31.8%	30.9%	18.5%	30.0%	30.1%
Cost of sales	(177,783)	(184,589)	(179,052)	(193,168)	(200,827)	EBITDA margin	25.0%	25.8%	13.5%	23.3%	23.4%
Gross profit	83,028	82,645	40,662	82,786	86,479	Operating profit margin	19.1%	19.8%	6.3%	16.6%	16.6%
Gross opex	(29,061)	(31,509)	(30,735)	(35,874)	(37,637)	PBT margin	15.5%	11.0%	-10.4%	11.0%	12.3%
Other operating income/(expenses)	(5,676)	(13,096)	(20,905)	(1,104)	(1,034)	Net prof it margin	13.0%	10.2%	7.7%	9.3%	10.5%
Operating profit	49,875	52,838	13,769	45,808	47,808	RoAE	19.5%	15.4%	8.0%	9.9%	10.9%
Interest income	3,334	1,953	3,676	1,695	1,770	RoAA	9.5%	6.3%	3.5%	4.9%	5.3%
Interest expenses	(11,266)	(10,702)	(15,504)	(16,701)	(14,000)	RoACE	13.6%	8.7%	4.8%	6.5%	7.4%
Share of net loss from associate	-	(5)	(13)	-	-						
Profit before tax	40,358	29,287	(22,819)	30,343	35,472	Liquidity Ratios					
Taxation	(6,538)	(2,124)	39,717	(4,551)	(5,321)	Working capital (N'm)	-3,506	-20,478	-77,644	-84,665	-81,091
Profit for the year - continued	33,820	27,163	16,899	25,792	30,151	Current ratio	1.0x	0.8x	0.6x	0.6x	0.6x
						Quick ratio	0.5x	0.4x	0.3x	0.3x	0.3x
						Cash ratio	0.3x	0.2x	0.1x	0.1x	0.1x
Financial Position						Efficiency Ratios					
	2014a	2015a	2016a	2017f	2018f		2014a	2015a	2016a	2017f	2018f
Property, plant and equipment	331,257	364,397	390,489	428,891	448,425	Fixed assets turnover	0.8x	0.7x	0.6x	0.6x	0.6x
Intangible assets	2,197	1,549	1,563	1,717	1,801	Current assets turnover	3.6x	3.6x	2.2x	2.6x	2.5x
Investment in Associate	43	27	90	98	109	Total assets turnover	0.6x	0.6x	0.4x	0.5x	0.5x
Other long term investment	8	6	6	7	13	Inventory turnover	6.7x	5.7x	4.6x	4.1x	4.0x
Deferred tax asset	295	-	7,641	8,392	8,780	Receivables turnover	16.0x	12.9x	9.3x	10.2x	9.9x
Long term receivables	6,248	9,975	-	-	-	Payables turnover	3.2x	2.6x	2.0x	1.8x	1.8x
Total non current assets	343,732	378,434	404,147	443,893	464,144	Days inventory outstanding	55	64	79	88	91
Inventories	31,545	33,027	44,531	48,910	51,143	Days collection outstanding	23	28	39	36	37
Trade and other receivables	19,830	21,590	25,801	28,339	29,635	Days payable outstanding	139	148	205	210	214
Current tax receivable	509	2,138	8,746	9,606	10,050	Cash conversion cycle	-61	-56	-87	-86	-87
Cash and cash equivalents	20,330	16,493	19,265	21,160	22,065						
Current assets	72,214	73,249	98,344	108,015	112,893	Solvency Ratios					
TOTAL ASSETS	415,947	451,683	502,491	551,908	577,037	Debt-to-capital ratio	0.4x	0.5x	0.3x	0.3x	0.3x
Trade and other payables	67,463	75,012	100,808	111,361	117,901	Net debt-to-equity ratio	45.8x	57.9x	39.5x	43.5x	36.6x
Provisions	1,334	1,864	1,177	1,300	1,379	Interest coverage	4.4x	4.9x	0.9x	2.7x	3.4x
Financial liabilities	5,134	12,823	59,483	63,980	57,714						
Deferred revenue	235	235	235	259	277	Investment Ratios					
Current tax payable	1,554	387	825	911	967	Earnings per share (N)	7.7	6.0	3.1	4.7	5.5
Total current liabilities	75,720	93,726	175,987	192,680	193,983	Dividend per share (N)	3.6	3.0	1.1	2.4	2.8
Financial liabilities	116,002	135,465	68,047	76,434	64,747	Dividend payout	47%	50%	34%	50%	50%
Retirement benefits obligation	8,979	7,542	3,780	4,176	4,424	Dividend yield	4.5%	3.1%	2.4%	5.9%	6.9%
Deferred tax	34,173	32,937	-	-	-						
Provisions	3,125	2,577	2,448	2,705	2,866						
Deferred revenue	2,368	2,134	1,555	1,717	1,821						
Liabilities associated with assets held for sale	-	1,150	1,721	2,366	28,678						
Total non-current liabilities	164,647	181,805	77,551	87,398	102,537						
TOTAL LIABILITIES	240,367	275,531	253,538	280,078	296,520						
Share capital	2,202	2,277	2,740	2,740	2,740						
Share premium	173,998	186,420	217,528	217,609	217,609						
Retained earnings	87,206	100,993	102,843	114,479	123,165						
Foreign currency translation reserve	(1,341)	(10,157)	(8,660)	2,501	2,501						
Other reserves arising on business combination	(161,690)	(162,185)	(256,900)	(256,900)	(256,900)						
Non-controlling interest	75,204	58,803	191,401	191,401	191,401						
TOTAL EQUITY	175,580	176,152	248,953	271,830	280,517						

Source: Company Accounts, Cordros Research

Disclosures

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