

BUA CEMENT PLC

Unearthing returns from aggressive expansions

BLOOMBERG: BUACEMENT NL

HOLD

Target Price: N93.13

Ref Price: N105.80

We initiate equity coverage on BUA Cement Plc (BUACEMENT) with a 12-month Target Price (TP) of N93.13 and a HOLD recommendation. The medium-to-long-term case for the company is supported by Nigeria's significant infrastructure gap, export opportunities enabled by location advantage, and cost efficiency of relatively new plants.

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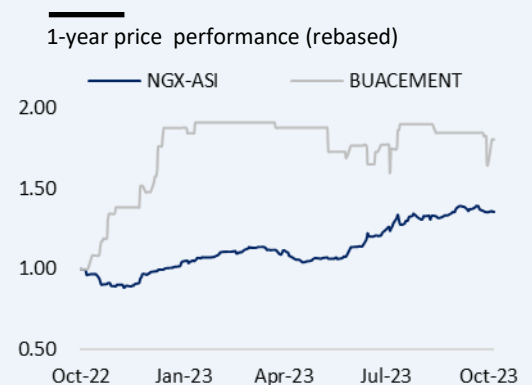
Executive summary

BUACEMENT embarked on an aggressive capacity rollout between 2018 and 2022, growing from 5 million metric tonnes (MT) at the start of the period to 11.0MT in January 2022, aided by the 6.0MT capacity expansion across its Kalambaina plant in Sokoto and Obu plant in Edo. Its management took the capacity expansion drive further in 2023 by commencing an additional 6.0MT plant capacity project, following a \$500 million capital raise from the International Finance Corporation (IFC). This project should raise the total installed capacity to 17.0MT by 2024, boost economies of scale potential, and drive down cash costs per ton.

However, in light of slowing demand owing to the tough macroeconomic environment, the company has decided to reduce its ex-factory price to capture additional market share. Aided by these potential market share gains, the company's revenue is expected to grow at a CAGR of 34.6% between FY23E and FY27E vs 32.0% over the last five years. In addition, we forecast EBITDA to grow by a CAGR of 34.8% over the forecast period, translating into an EPS CAGR of 38.7%.

Valuation and Rating: BUACEMENT is currently trading at a forward EV/EBITDA of 19.6x, which looks expensive relative to our select EMEA average of 14.1x and ahead of its four-year mean of 18.7x. However, the company also boast a LTM ROE of 22.1%, which is at a premium to its historical mean of 21.5% and the average of EMEA peers (13.4x), suggesting some little justification for its EV/EBITDA.

Market Data	BUACEMENT
Market Cap (N'bn)	3,582.85
Last close price (N)	105.80
52-week high-low price (N)	105.80/51.95
Avg 3M daily volume (mn)	0.99



Source: NGX, CardinalStone Research

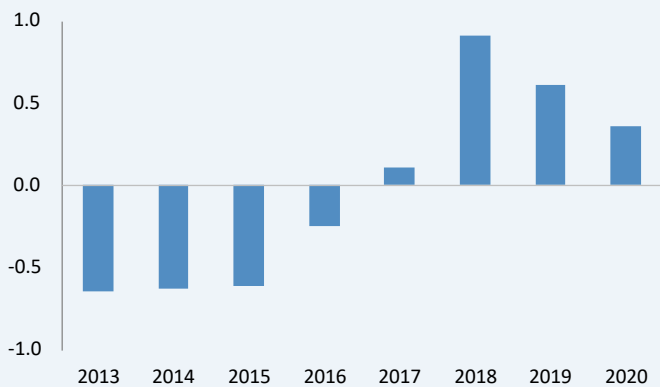
NB: All prices in this report are as of 25 October 2023



The Nigerian Cement sector

Over the last two decades, the Nigerian cement sector has evolved from import-dependent into a growing hub for cement export. Federal government policies, including tax relief programs and cement importation ban, have encouraged local players' emergence and subsequent expansion. The latter has driven installed capacity beyond domestic demand (57.7MT vs 29.5MT).

Figure 1: Nigeria's cement market has evolved from net importation to net exportation (MT)

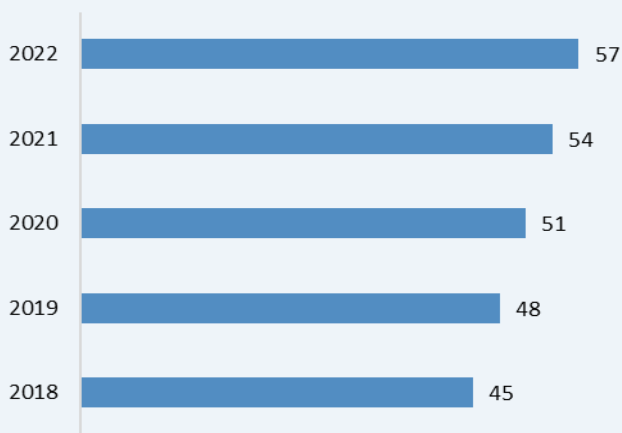


Source: Company Financials, CardinalStone Research

Over the years, with favourable policy, indigenous cement companies have risen to the challenge of helping, in their way, to meet Nigeria's huge infrastructure deficit. The Nigerian cement market consists of three key players, Dangote Cement (DANGCEM), BUA Cement (BUACEMENT) and Lafarge Africa (WAPCO), responsible for 99.0% of production. There is also a fringe player, PureChem Industries Limited, based in Ogun State, with 0.9MT. Mangal Industries Limited and Mandugu Cement also plan to build 3.0MT and 5.0MT cement plants. In addition, IBETO Group (in partnership with Sinomas) is building two greenfield projects in Effium (1.0MT) and Enugu (2.2MT), plus a 3.0MT expansion project at its Nkalagu plant in Ebonyi. These projects could increase the nation's aggregate installed capacity to over 70.0MT by 2025.

In light of recent capacity expansions, there have been major shifts in the market share of industry players. DANGCEM, as the industry leader by installed capacity, has seen market share fall from 63.5% to 61.2%. WAPCO's position as the second largest cement company by installed capacity (10.5MT) was usurped by BUACEMENT, with the former's market share declining from 21.8% to 18.2%. BUACEMENT's aggressive capacity rollout over the past year saw its market share rise from 17.6% to 19.1%. BUACEMENT is the largest cement producer in North West, South-South and South-East Nigeria and has captured an additional 9.4 ppts of market share post consolidation with CCNN.

Figure 2: Nigerian Capacity (MT) dynamics over the last five years



Source: Company Financials, CardinalStone Research

Increasing capacity begets competition

Considering the time involved in new plant construction (typically 3-4 years), current expansion plans may be targeted at meeting future demand amid the potential for improved adoption of AfCFTA. DANGCEM, intent on maintaining its capacity advantage, added two 3.0MT plants to its ranks between Q1'20 and Q3'21 (at Obajana and Okpella, respectively) and is on course to churn out another 6.0MT plant in Ogun state, Nigeria.

Similarly, BUACEMENT expanded its Kalambaina Plant in Sokoto by adding a 3.0MT line 4 commissioned in January 2022. With BUACEMENT being the only cement company with a physical production facility in the North West, its continued expansion is unsurprising as it aims to consolidate market share. Notably, DANGCEM also serves the Northern market from its Kogi plant via its truck fleets. WAPCO, on the other hand, having divested its loss-making South African business and deleveraged its balance sheet, is focusing on debottlenecking its Ashaka and Ewekoro plants to unlock additional plant utilisation benefits instead of new capacity rollout.

Figure 3: Oligopolistic market with a clear leader

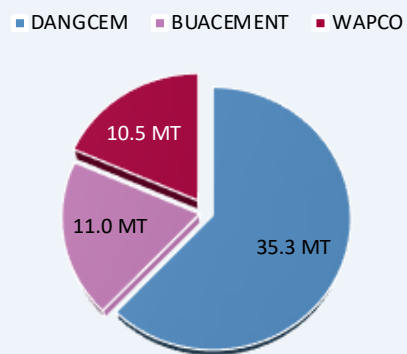
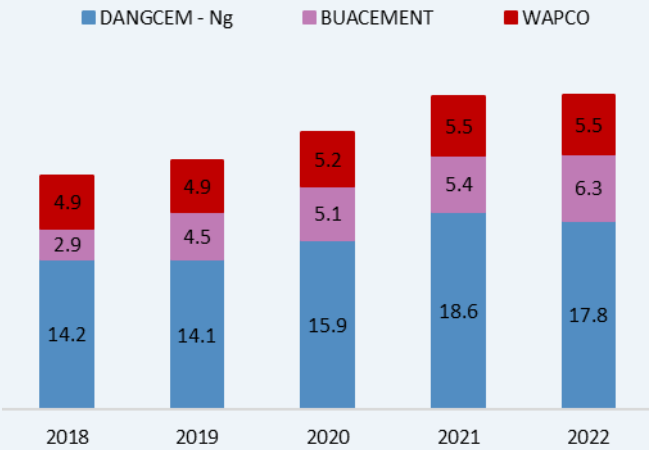


Figure 4: Volume (MT) between 2018 –2022



Source: Company Financials, CardinalStone Research

BUACEMENT has been playing catch-up to win market share from market leader Dangote Cement, overtaking Lafarge Africa. From 2018 to 2022, its installed capacity increased from 5 million tonnes (MT) to 11.0MT, a compound annual growth rate (CAGR) of 21.8%. This strategy has begun to yield results as newly commissioned plants are starting to drive increased cement output. Coupled with rising cement prices as reflected in the revenue/tonne growth, extension. WAPCO’s volumes have been relatively flat, leveraging price increases to drive revenues.

Figure 5: Revenue/tonne (N’000) between 2018 –2022

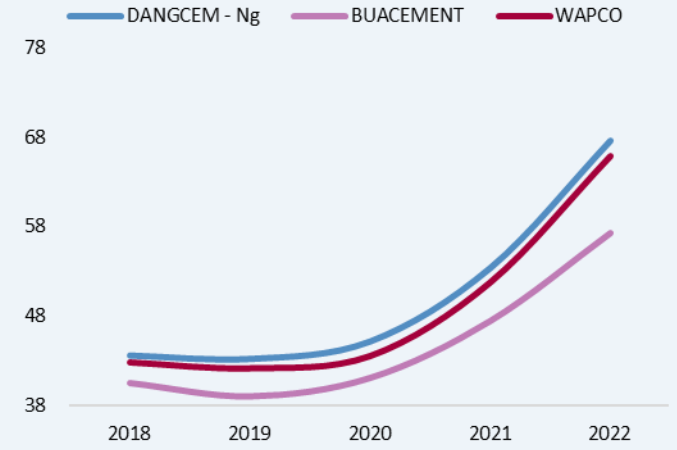
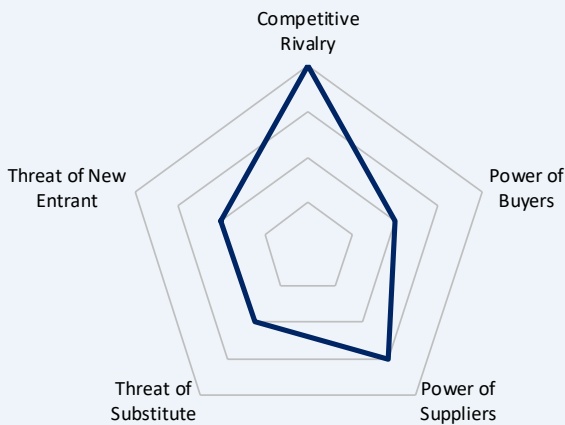


Figure 6: Cement sector porter 5 forces



Source: CardinalStone Research

Figure 7: Utilization still below 5-year average

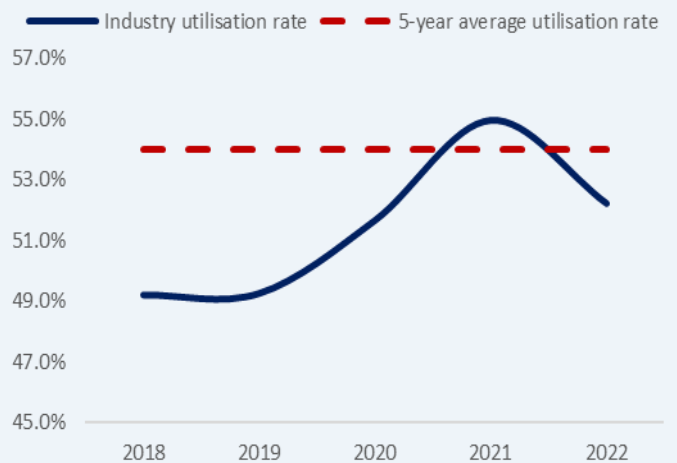
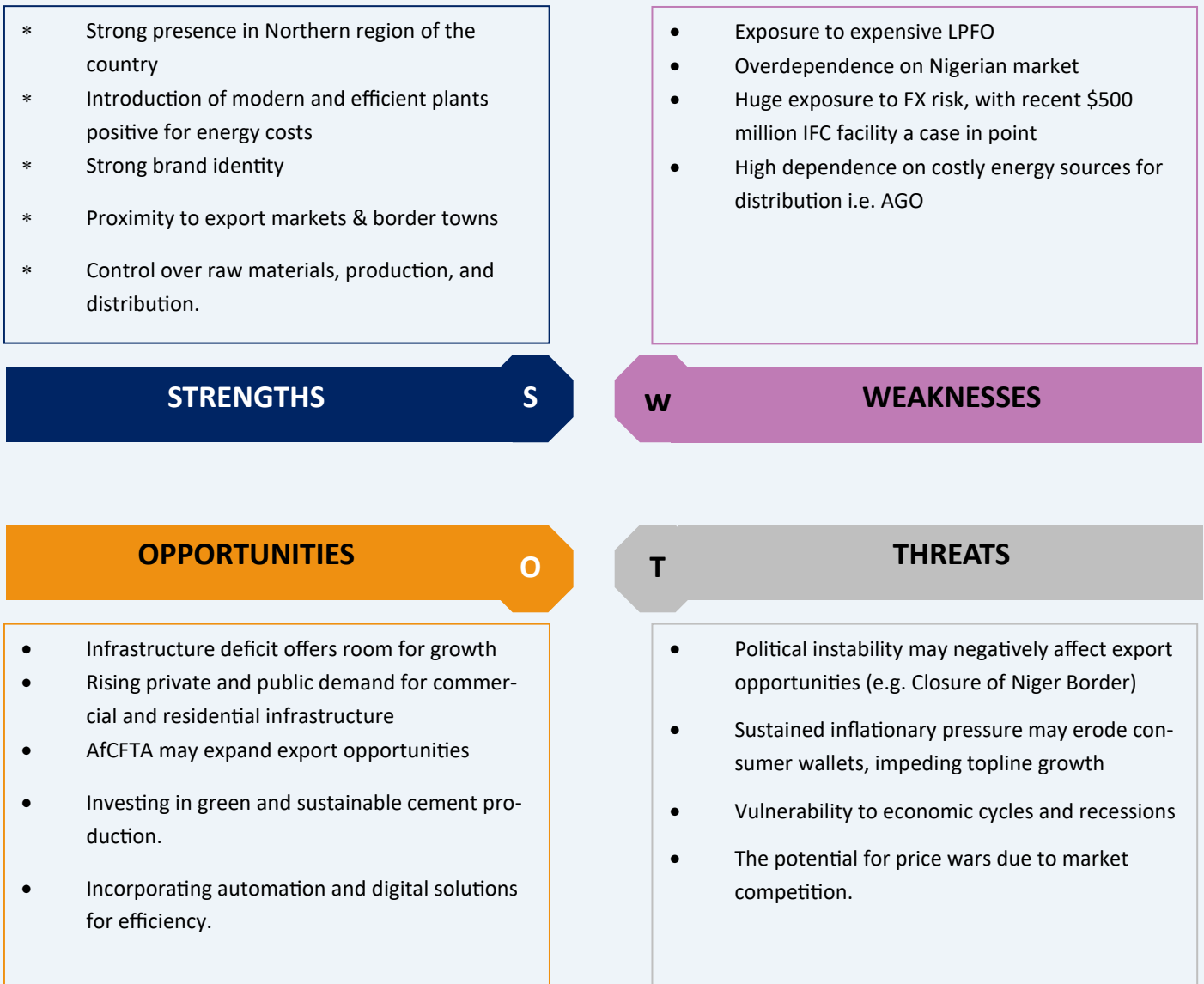


Figure 8: SWOT Analysis



Source: CardinalStone Research

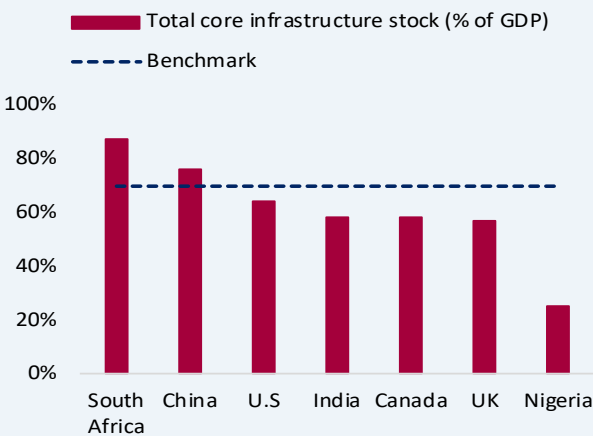


Sector Investment Thesis

The Nigerian infrastructure challenge

Cement remains at the core of infrastructure development globally, and the Nigerian cement market offers a runway for sustained growth, considering the country’s huge infrastructural deficit. Our current infrastructure stock is about 35% of GDP, which pales compared to the global average of 70%. According to the Bureau of Public Enterprises, Nigeria may have to invest about \$3 trillion in the next 30 years to bridge its vast infrastructure gap. In the short term, the nation needs an average of \$100 billion annually in the next six years to bridge the deficit. Considering the plethora of panaceas proffered by the government to bridge this gap, we recognize this deficit as a sustainable demand point for cement in the near to long term.

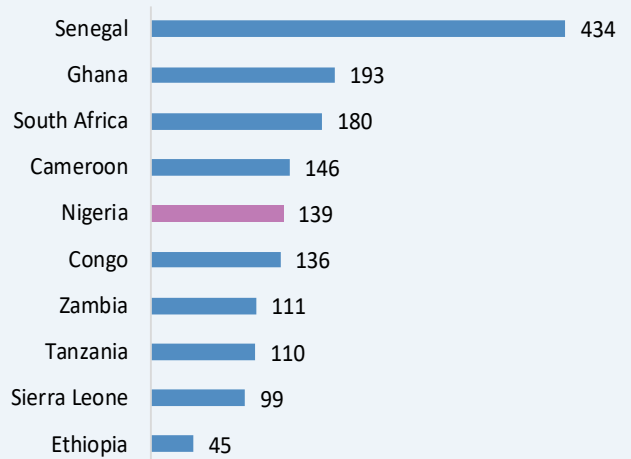
Figure 9: Infrastructure stock as % of GDP



Source: Nigeria Budget Office, Cemnet, CardinalStone Research

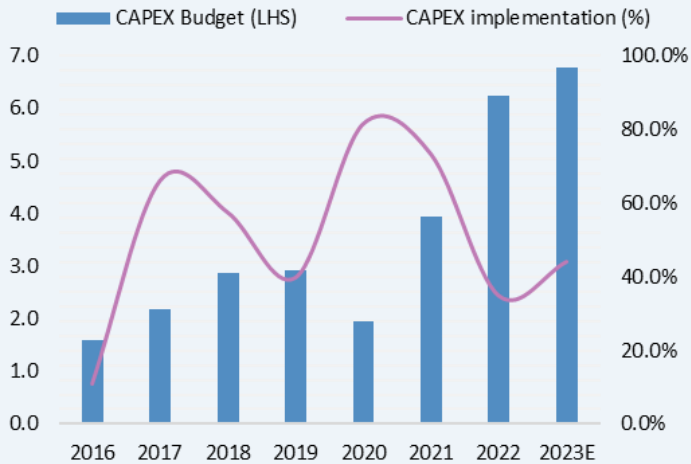
On a direct basis, the federal government has stepped up its budget allocation towards capital expenditures post the 2016 recession and ex-2020. To this point, actual capital expenditure increased by a CAGR of 23.7% between 2015-2020, with the government disclosing plans to invest over \$1 billion into the Presidential Infrastructure Development Fund in 2021. These investments target three flagship projects: the Lagos-Ibadan Expressway, Second Niger Bridge, and Abuja-Kaduna-Zaria-Kano Expressway.

Figure 10: Cement consumption per capita (kg)



Despite the government's apparent commitment to addressing these infrastructural gaps, historical precedence suggests that more public funds are needed to address the need. To buttress this point, Nigeria has spent only \$100 billion on infrastructure (the equivalent of the annual spend required to plug the infra gap) over the last 20 years.

Figure 11: CAPEX budget (N' billion) is rising, but more implementation is needed



Source: Budget Office , CardinalStone Research

The Buhari administration stepped up efforts to steer private investment in infrastructure through several public and private partnerships (PPP). Some of these initiatives came in the form of the following:

- Infrastructural Corporation of Nigeria Limited (INFRACO)
 - Road Infrastructure Development and Refurbishment Investment Tax Credit Scheme (RITC).
- ⇒ **INFRACO:** The previous administration launched the Infrastructural Corporation of Nigeria Limited (INFRACO) in Q3'2021 with an initial seed capital of N1 trillion (\$2.4 billion) to fund public projects like roads, rails and power infrastructure across the country. However, it is yet to fully take off due to a delay by the Central Bank of Nigeria (CBN) in disbursing the initial seed money of N1 trillion to the four fund managers that will manage the company's assets. Despite the delays, INFRACO carries a potentially positive passthrough to the cement sector and the overall construction industry in the medium to long term.
- ⇒ **RITC:** The RITC enables the government to leverage private sector capital and efficiency for constructing, repairing, and maintaining critical road infrastructure in Nigeria by granting an income tax credit to companies and individuals that provide funding for the refurbishment and rehabilitation of roads. Some of the projects that have been approved under the scheme include:

- ◇ Onitsha-Enugu Expressway (110km, at ₦202.8 billion)
- ◇ Bonny – Bodo Road (34 km; ₦37.28 billion)
- ◇ Lokoja-Obajana-Kabba Road (43km)
- ◇ Apapa-Oworonshoki-Ojota Road (35km; at ₦73 billion)
- ◇ Bali-Sheti-Gashaka-Gembu in Taraba state (234 km, for ₦95.2 billion)
- ◇ Nnamdi Azikiwe Expressway/Bypass, Kaduna State. (21,477km for ₦37.560 billion)
- ◇ Bama-Banki Road, Borno State (49,153km for ₦51.016 billion)
- ◇ Dikwa-Gamboru-Ngala Road, Borno State (49,577km at a cost of ₦55.504 billion)
- ◇ Obele-Illaro-Papalanto Shagamu Road, Ogun State (100km for ₦79.9 billion)
- ◇ Oyigbo-Izuoma-Mirinwayi-Oklama-Afam Road
- ◇ Oniru axis of VI-Lekki circulation Road in Lagos State (5km)
- ◇ Umueme Village Road, Abia State
- ◇ Malando-Garin Baka-Ngwaski Road
- ◇ Bode-Saadu-Lafiagi Road; Eyinkorin Road and Bridge
- ◇ Obajana-Kabba Road
- ◇ Construction/rehabilitation of about 21 different federal roads by the NNPC across the six geopolitical zones (1,804.6km for ₦621 billion)

The roads approved under the scheme are at various stages of construction/rehabilitation, and it is expected that the participating companies will get the twin benefit of improved motorable roads leading to their businesses and the accompanying tax credits. The fact that the tax credits are tradable instruments and transferrable between companies with common ownership is also an added advantage.

Infrastructure Support Fund (ISF): The new administration led by President Bola Ahmed Tinubu also announced the creation of an Infrastructure Support Fund (ISF) as part of a series of measures to boost the economy and ease the inflationary impact of the petrol subsidy removal. The ISF is expected to help Nigeria revamp transportation and upgrade farm-to-market roads across states. It is also expected to fund health, education, power and water projects.

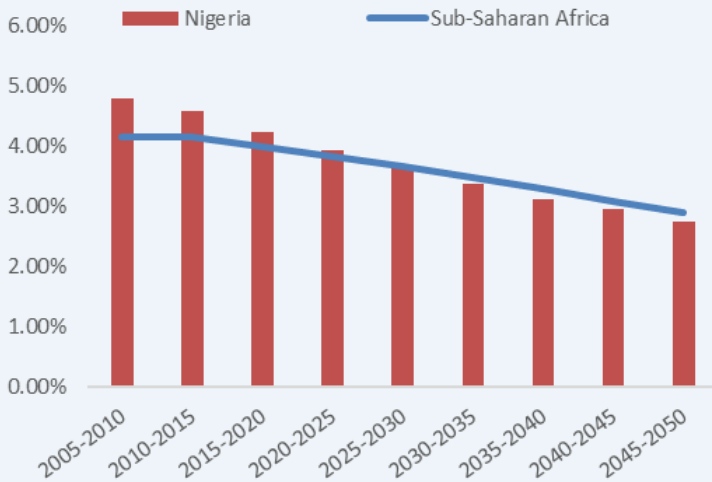
Elsewhere, the new Minister of Housing and Urban Development, Mr Ahmed Dangiwa, in August 2023, pledged to work towards increasing the capital base of the Federal

Mortgage Bank of Nigeria (FMBN) to N500 billion, as well as reform the Federal Housing Authority (FHA) and other agencies under his ministry.

While specific details are yet to be provided, we anticipate some positive passthrough to cement consumption over the medium-to-long term.

The FMBN recapitalization exercise is also expected to improve access to capital for home builders and sustain the growing cement consumption pattern.

Figure 12: Urbanization is projected to remain strong over the next 27 years

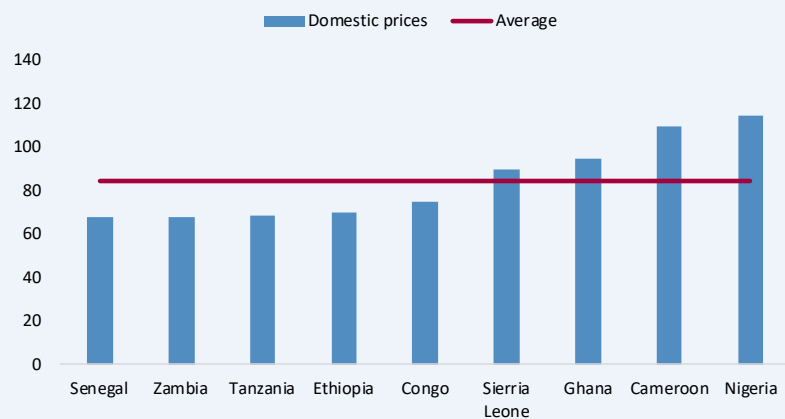


Source: United Nations, CardinalStone Research

Nigeria's premium pricing advantage

Nigerian cement has historically traded at a significant premium compared to prices in other African countries. As of 2023, local cement traded at over 40.0% premium compared to select African nations, partly due to favourable government policies such as the ban of imports alongside the absence of price caps.

Figure 13: Nigerian cement prices (\$/MT) vs prices in peer countries (2022)



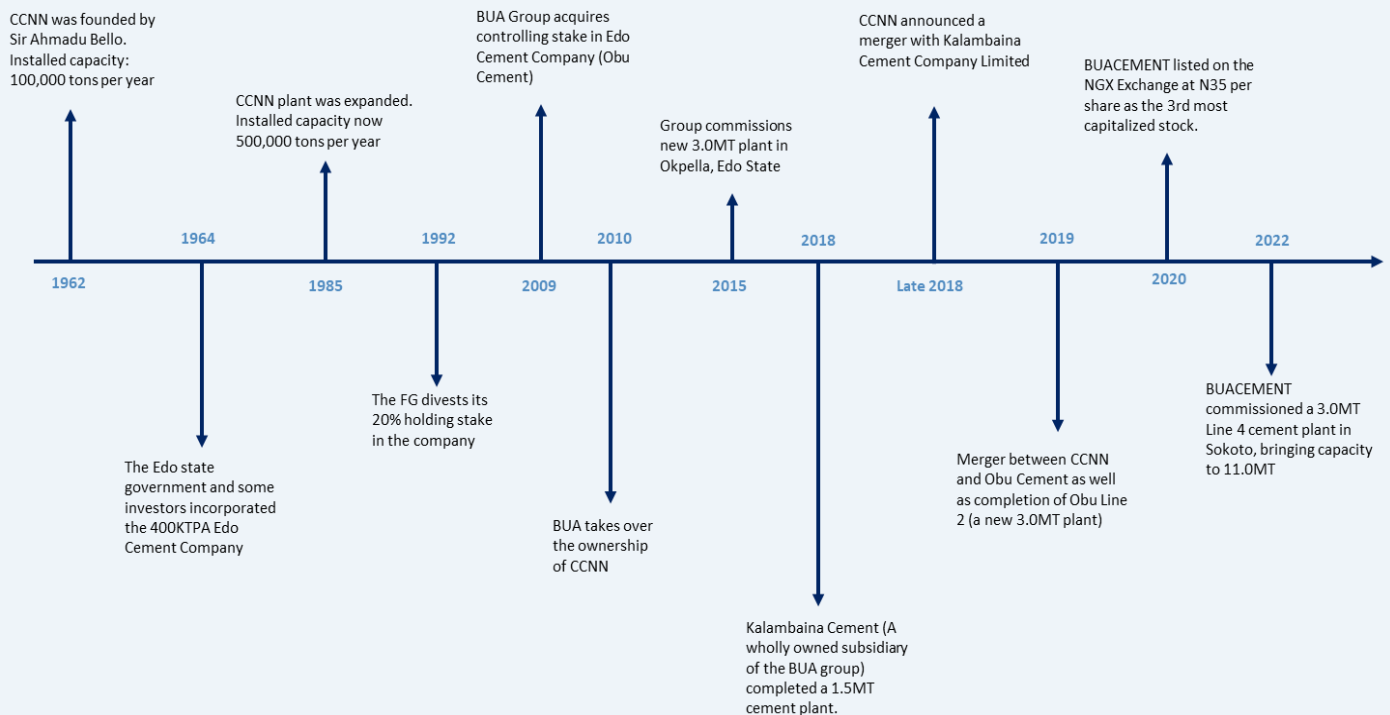
Source: Dangote Cement, CardinalStone Research



A brief history of BUACEMENT

BUACEMENT was incorporated in 2008 and commenced operations in the same year through its 2.0MT floating cement terminals, 'BUA Cement 1', designed specifically for bulk and bag cement unloading. Its production capacity was increased to 2.0MT in 2009 following the acquisition of Cement Company of Northern Nigeria (CCNN) and Edo Cement Company. The former came via the company's holdings in Damnaz Cement Company Ltd, the majority shareholder in CCNN at the time. By 2019, BUA had expanded capacity by an extra 6MT (bringing total installed capacity to 8.0MT), aided by the commissioning of two 3.0MT lines in Obu,

Figure 14: Time chart of BUACEMENT's evolution



Source: Company documents, CardinalStone Research

Edo State. Thus, the consolidation of the group's cement concerns across the country in 2020 confirmed the emergent entity as the third-largest cement producer in the country after Lafarge (10.5MT) and Dangote Cement (35.3MT). The company also became the dominant cement force in the Northwest region.

Obu Cement

Obu Cement was incorporated as a private limited liability company in 2014 and commenced operations in 2015. It was later re-registered as a public limited company in 2019 after its merger with CCNN. However, the company's foundation dates back to the old 400KTPA Edo Cement (later upgraded to 3.0MT) in Okpella, owned by the Edo state government at the time. Edo Cement's location in Okpella is known for its natural sedimentary rock-based mineral resources (i.e., limestone, feldspar, calcium and granite, clay, and marble) and marble-making industries. These attractions led BUA Group to acquire a controlling stake in Edo Cement Company in 2009. The group eventually commissioned a new plant at Obu, a few kilometres from Okpella, in 2015 when it maxed out on capacity at the older plant.

The proximity of Obu plants to Edo Cement (about 5km distance) enables an efficient production process on a combined installed capacity of 6.0MT. The plants primarily operate on multiple fuel sources - a gas turbine that powers the plant, which utilizes a gas supply for power stability, and liquid fuels as a backup for potential supply disruptions. It is also furnished with a 50MW captive gas power plant to supply the plant's non-kiln operations. Its primary gas source is a 30km gas pipeline built by Obu Cement from the Ajaokuta gas line to Okpella.

Figure 15: Obu Cement Complex (Lines 1,2 & proposed line 3)

Location: Okpella, Edo State (South-South Nigeria)	Production Capacity (MT)	Completion date
Obu Cement Plant (Line 1)	3.0	2015
Obu Cement Plant (Line 2)	3.0	2018
Obu Cement Plant (Line 3)	3.0	2024*

Source: Company Financials, CardinalStone Research

*expected completion date

CCNN

Cement Company of Northern Nigeria Plc (CCNN) was founded by the then Northern Region's Premier, Alhaji Sir Ahmadu Bello. It was incorporated in 1962 and commenced production in 1967 with an initial installed capacity of 100KTPA in Kalambaina, Sokoto state. CCNN was expanded to 600 KTPA capacity in 1985 by introducing a 500 KTPA second line. Due to its relative inefficiency, the first line was shut down in 1986, leaving the plant with a rated capacity of 500 KTPA.

The Federal Government divested a considerable stake in the company as part of the complete privatization of certain government-owned businesses. As a result, Scancem International of Norway, a member of the Heidelberg Cement Group, joined CCNN as a key investor and technical partner in 2000. Damnaz Cement Company Ltd (owned by Abdul Samad Rabiou and BUA International Limited) acquired a 50.7% stake in CCNN in 2008 effectively becoming the company's major shareholder.

Kalambaina

Kalambaina Cement Company Limited was a private limited liability company in Kalambaina Sokoto State and a wholly-owned subsidiary of BUA Cement Limited. The company primarily engaged in quarrying, extracting, processing, limestone, and cement manufacturing. The company constructed a 1.5MT installed capacity that was commissioned in 2018. The plant is in Kalambaina Sokoto state (close to the old 0.5MT CCNN plant) and has a 48-megawatt captive power plant and coal mill-efficient kilns. On-site are Cement Silos with a combined total storage capacity of 25,000 tonnes.

Figure 16: Kalambaina Cement Complex (Lines 1,2,3,4 & proposed line 5)

Location: Kalambaina, Sokoto State (North-West Nigeria)	Production Capacity (MT)	Completion date
CCNN Cement Plant (Lines 1&2)	0.5	1964 & 1985
Kalambaina Cement Plant (Line 3)	1.5	2017
BUACEMENT Cement Plant (Line 4)	3.0	2021
BUACEMENT Cement Plant (Line 5)	3.0	2024*

Source: Company Financials, CardinalStone Research

*expected completion date

Listed as the 3rd most capitalized stock on the exchange

BUACEMENT was listed on the Nigerian Stock Exchange in 2020 with a market capitalization of N1.18 trillion, standing out as the 3rd most capitalized stock on the exchange. Its market capitalization raced to N2.5 trillion in less than 18 months on a materially low free float of c.1.6% (vs 9.6% for its domestic peers). The company eventually revealed its intention to liaise with the stock exchange and shareholders to resolve its low free float concerns. This resolution was expected to take the form of a premium board listing or a controlled sell-down of key shareholders' stakes on the exchange that could, inadvertently, lead to some price correction.

The possibility of a large sell-down had investment banking firms and security houses closely hovering around the company for what may have seemed a groundbreaking deal waiting to happen. For context, even a deal structured to take the company's free float to the industry mean level would have seen shares worth over N160.4 billion move to minority shareholders, assuming the transaction occurred at a 20.0% discount to the market price of N74 as of June 15 2021.

However, the moderation in free float to 1.6% vs 1.15% at the time of listing suggested that the company was exploring the premium board option, which would not necessarily require the majority shareholder to relinquish significant holdings. Obtaining a premium board listing would require the company to meet the conditions below:

- Have a minimum free float of 20% of its issued share capital or have a free float value equal to or above N40 billion on the date the exchange receives the application
- Achieve a market capitalization that is equal to or above N200 billion
- Score at least a 70% rating on the NGX's Corporate Governance Rating System (CGRS)
- Give a binding undertaking to promptly provide information about its operations and follow administrative procedures set out in the NGX Rulebook Review of BUACEMENT's operations across the country.



Investment Proposition

Well-positioned to consolidate stronghold in Northern Nigeria market

BUACEMENT currently controls a material chunk of cement sales in the Northwest, aided by its old 0.5MT "former CCNN" facility and the new 1.5MT Kalambaina line 3 in Sokoto State. The company also launched a new 3.0MT BUACEMENT line 4 in January 2022 to bring total installed capacity in the Northwest to 5.0MT, in contrast to its peers with zero presence in the region. For further context, the Northwest encompasses the economic centres of Kano and Kaduna, which, according to the National Bureau of Statistics (NBS), rank 3rd and 7th in GDP size by states across the country. The factories are also close to the State Capital – Abuja.

On December 22 2020, the company announced that it entered into a contract with Sinoma CBMI of China to build three production lines with a cumulative capacity of 9.0MT by the end of 2024. Two of these plants will be located in Sokoto and Adamawa, further broadening BUACEMENT's footprint in Northern Nigeria. Given its potential scale benefits, the 3.0MT Adamawa plant could be a competitive threat to Lafarge Africa Plc's Ashaka operations in the Northeast region (0.9MT plant in Gombe state). The proposed Sokoto and Adamawa plants will also be located at border states, close to export markets – the Republic of Niger and Cameroon. Exports could also be supported by the African Continental Free Trade Area (AfCTA) agreement. The AfCTA aims to eliminate tariffs between members on 90% of line items over the next five years and reduce non-tariff barriers on goods and services. However, the plans for the Adamawa plant are still in the early stages.

“The company also launched a new 3.0MT BUACEMENT line 4 in January 2022 to bring total installed capacity in the Northwest to 5.0MT”

Capacity expansion to deepen Southern penetration

BUACEMENT's mid-term expansion plans also cover an additional 3.0MT line in Obu, Edo State, Southern Nigeria. The proposed line is also expected to raise the installed capacity at Obu to 9.0MT by 2024. Obu is located at the heart of Southern Nigeria and is strategically close to several economic centers in the West. The facility is also reasonably close to the country's capital, Abuja. Upon completion, BUACEMENT will be better equipped to compete with WAPCO's combined 10.5MT installed capacity and DANGCEM's 12.0MT Ibese plant in Southern Nigeria.

Cost savings likely to drive EBITDA margin beyond three-year average by 2025

We expect the new additions to BUACEMENT's lineup to slightly reduce the group's costs, with the effects likely to materialize from 2025. The kiln at Sokoto Line 1 is solely optimized for the relatively expensive LPFO - a bane on energy costs. The introduction of BUACEMENT Line 4 in 2022 and the further rollout of Line 5 in 2024 should soften average energy and distribution costs. In addition, BUACEMENT's new plants are better suited to be adapted to Alternative Fuels (AF) (0.6x cheaper than gas), supporting the bottom line and margins in the long run. However, short-run costs are expected to remain elevated.

Stellar creditworthiness to finance future expansion plans

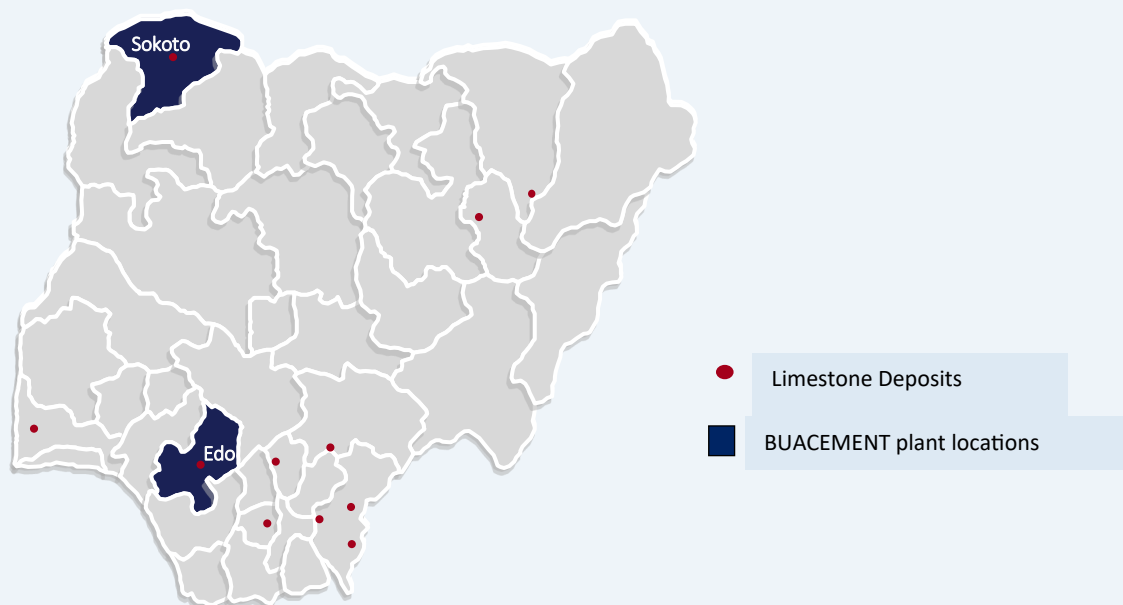
In December 2020, BUACEMENT successfully concluded its N115billion Series 1 fixed rate senior unsecured bond issue (the "Bond or Issue") under its maiden N200billion bond issuance programme - the largest ever corporate bond issued in the Nigerian Debt Capital Markets, signalling growing investor confidence in the company. The offer was oversubscribed with a bid to cover 1.2x, N22.8 billion above the N115 billion provision according to regulatory guidelines. Before the recent issuance, the company's capital structure had traditionally been equity-biased, with debt only taking about 3% of total invested capital. The firm's considerable acceptance and track record in the capital markets provided a good antecedence for additional capital-raising activities needed to finance its expansion projects like the \$500 million IFC facility obtained in June 2023.

We are wary of the future impact of interest expense on earnings based on recent debt raises. In particular, the combination of bond issuance and shareholder loans shot up the debt/equity ratio to 58.2% in FY'22 vs a 4-year average of 17.4%. We expect future interest payments associated with its new loan obligations to weigh on earnings, but only immediately, as the company policy is to capitalize borrowing costs on plants once they are commissioned.

Proximity of plants to raw materials and key markets

One of BUACEMENT's business cases is its proximity to limestone deposits - one of the essential raw materials for cement production. Alongside other cement manufacturers, BUACEMENT plants in Sokoto and Edo are close to massive quarries with large limestone deposits. The proposed plant in Adamawa also has proximity to limestone deposits. This proximity gives the company an advantage in controlling its raw material cost. It limits its production to logistical and cashflow challenges since the decision to mine more or fewer minerals for cement production is within its control.

Figure 17: Map of Nigeria with areas with limestone deposits



Source: Company Financials, CardinalStone Research

Potential tax benefits could provide further support

The company applied to the Nigerian Investment Promotion Commission (NIPC) for a pioneer status for its production line 2 in Okpella, Edo State and Kalambaina line 4 in Sokoto State in 2021. The pioneer status was approved on 30th July 2021, covering the period from 1st June 2021 to 1st April 2022, respectively. As a result, no current income tax was accrued on the pioneer profits over the period. On 1st January 2022, production line 3 in Kalambaina exited its pioneer status and has been subject to the company's income tax rules accordingly. Nevertheless, the expected commissioning of Kalambaina line 5 and Obu line 3 in 2024 suggests potential pioneer tax credits in the near term.

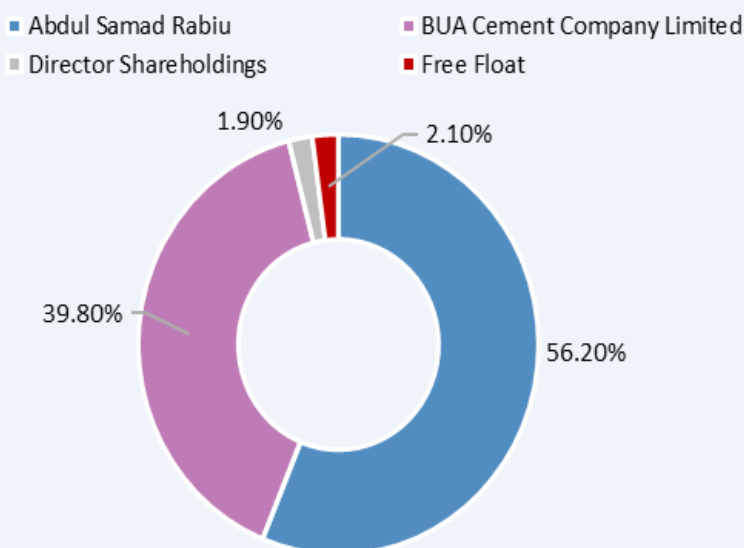
Experienced management team and parent company

The company's affairs are overseen by its Chief Executive Officer and Managing Director - Yusuf Haliru Binji. Mr. Binji is a successful chemical engineer with nearly three decades of experience in the cement sector. Mr Binji obtained his first degree in Chemical Engineering in 1990 from Ahmadu Bello University and a Master's degree in Chemical Process Engineering with Distinction from the University College, the University of London in 1993. Before his current role at BUACEMENT, he headed technical operations at CCNN Plc and BUA Group before he was appointed Managing Director of Obu Cement Company Limited (a subsidiary of the BUA group at the time) on February 1, 2017.

The company's Chief Financial Officer (CFO) - Jacques Piekarski, is an equally seasoned finance professional with over 30 years of cognate finance experience across FMCG, cement, trading and mining sectors. Before BUACEMENT, Mr Piekarski held CFO roles at Holcim Group, Flour Mills of Nigeria Plc and Tropical General Investments (TGI) Group. He has an MBA from the prestigious Robert Kennedy College, Zurich, Switzerland.

BUACEMENT is also backed by its parent, BUA group – a leading food and infrastructure conglomerate headed by one of Nigeria's leading investors, Alhaji Abdul Samad Rabiu. The group has a diversified portfolio covering sugar refining and plantations, rice, flour milling, pasta production, oil and gas, construction, real estate and logistics.

Figure 18: Ownership composition



Source: Company Financials, CardinalStone Research



Financial Analysis — How has it fared so far?

Sales have more than tripled since 2018

Since listing on the exchange, BUACEMENT has recorded impressive revenue growth over the last two years. Revenues have grown over 3x to N361.0 billion over the past five years, driven mainly by volume and price growth. The company has been able to ramp up production by introducing the BUACEMENT Line 4 plant in 2022 alongside higher utilization of its existing plants. The company's aggressive pricing in line with inflation, albeit lower than its peers, has also supported cement sales.

Figure 19: Steady revenue (N' million) growth

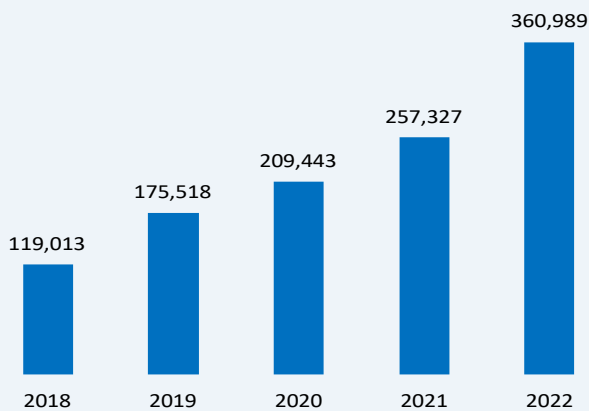


Figure 20: Steady volume (KT) growth



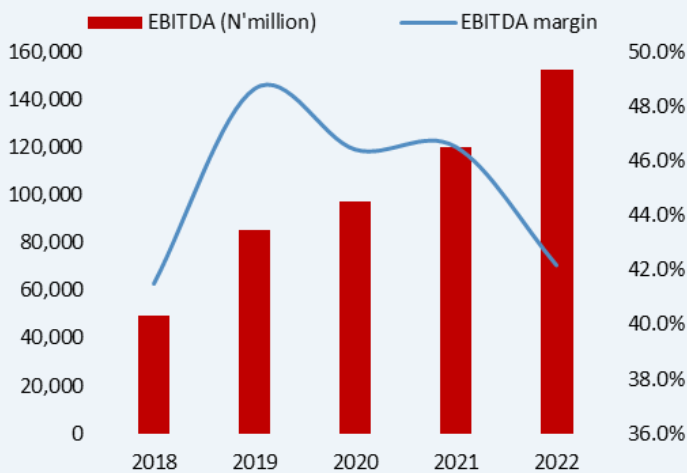
Source: Company Financials, CardinalStone Research

High operating costs pressure EBITDA margins

EBITDA is our preferred indicator of profitability and scalability as it provides investors with a clear and undiluted perspective on the company's strength of operations. Between FY'18 and FY'21, BUACEMENT's EBITDA grew faster than revenues, underscored by controlled increases in selling and distribution costs, lower technical and management fees, prudence in administrative-related expenses, and the effect of impairment writebacks.

However, in FY'22, there was a surge in distribution costs occasioned by the conflict-induced rise in diesel prices and naira devaluation. Further breakdown also revealed pressures from the LPFO-powered Sokoto Line 1 plant. That said, there are initiatives to address cost pressures. These initiatives include 1)—greater reliance on modern and more efficient plants (70.0% of total production) and 2)—active efforts to replace coal with LNG in some plants (30.0% of the energy mix in the Sokoto plants). The latter is also used to power the 15 MW electricity generation at the Kalambaina plant.

Figure 21: Selling and Distribution costs pressure EBITDA margin in 2022

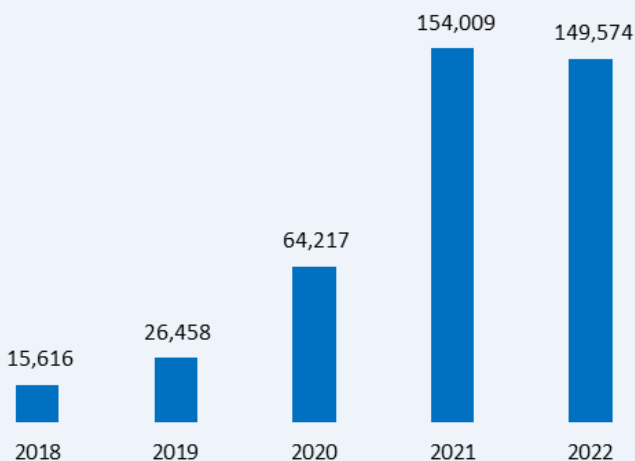


Source: Company Financials, CardinalStone Research

Improving operating cashflows

Operating cashflows and efficient working capital management have benefitted from its stellar operating performance over the years. Over the last four years, operating cash flows have grown by nearly 10x to N149.6 billion. The working capital balance has moved from a negative N39.6 billion in 2018 to a negative N5.8 billion by the end of 2022.

Figure 22: Operating cashflows (N'million) have grown nearly 10x



Source: Company Financials, CardinalStone Research

Figure 23: BUACEMENT's Earnings Quality (EQ) has been on a downtrend

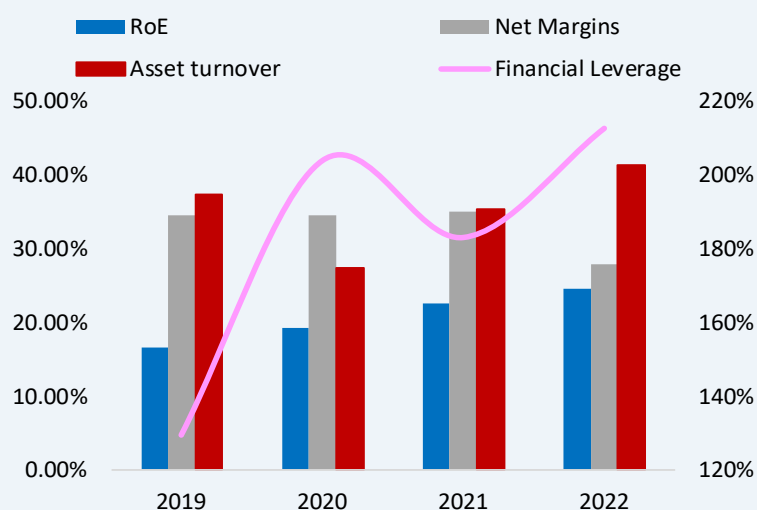
EQ Component	Formula	FY'19	FY'20	FY'21	FY'22
Cashflow Margin	$(CFO_t/S_t)*10^1$	1.5	3.1	6.0	4.1
Operating Cash Ratio	$CFO_t/EBIT_t^2$	0.4	0.8	1.5	1.2
Repeatable Earnings Ratio	COI_t/NI_t^3	1.0	1.0	1.0	1.0
Leverage Ratio	$(CFO_t/TL_t)*5^4$	1.3	0.8	2.3	1.6
Receivables Accruals Ratio	$((S_t/AR_t)-(S_{t-1}/AR_{t-1}))+1^5$	19.1	-63.5	5.3	-1.3
EQ Score		23.3	-57.8	16.1	6.6

Source: Company Financials, CardinalStone Research

Return on equity has been driven by financial leverage

Across the review period, BUACEMENT's average returns on assets (ROA) and equity (ROE) exceeded that of WAPCO but underperformed that of DANGCEM. Furthermore, ROE breakdown using the three-way Dupont analysis revealed that return on equity was primarily upheld by high financial leverage and asset turnover, with net margins having a relatively negative impact. BUACEMENT's net margin has been hit by higher effective tax rates year on year. The firm received a tax credit of N24.9 billion in FY'18, followed by effective tax rates of 8.5%, 8.5%, 12.7% and 16.7% in FY'19, FY'20, FY'21 and FY'22, respectively, as its various lines of tax credits dried up over the period. On the other hand, the higher level of leverage reflects the company's recent move away from its previously equity-dominated capital structure, following its maiden bond raise in December 2020, which effectively increased its Debt/Equity ratio to 58.2% in FY'22 from 5.9% in FY'19.

Figure 24: Financial leverage has been the main driver of ROE



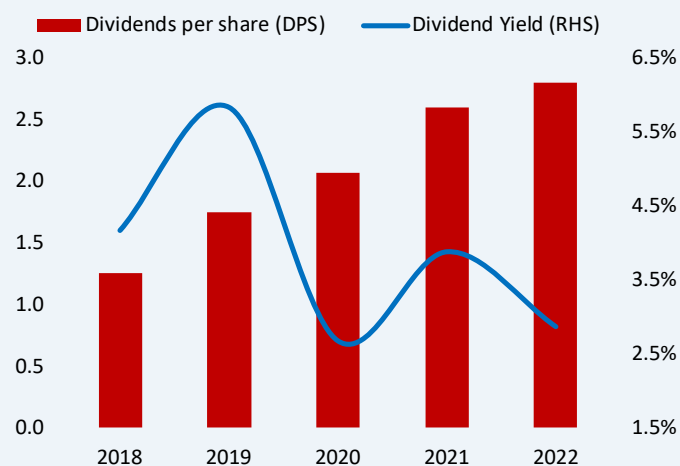
Source: Company Financials, CardinalStone Research

¹(Cash Flow from Operations in year t/Sales in year t)*10, ²Cash Flow from Operations in year t/Earnings before Interest and Taxes in year t, ³Income from Continuing Operations in year t/Net Income for year t, ⁴Cash Flow from Operations in year t/Total Liabilities in year t)*5, ⁵((Sales in year t/Receivables in year t)-(Sales in year t-1/Receivables in year t-1)+1)

BUACEMENT has steadily increased dividends

The company has rewarded its shareholders over the last three years, paying an average of 82.0% of its after-tax earnings to shareholders. Given its current phase in the maturity ladder, we consider this an impressive feat. Nonetheless, a dividend yield of 2.6% materially underperforms its domestic peers due to its share price.

Figure 25: Dividend payments (N/share) since 2018



Source: Company Financials, CardinalStone Research

Performance expectations over a five-year horizon**We expect sales to double over our forecast horizon**

BUACEMENT is expected to grow revenue at a CAGR of 34.6% over our forecast period. This view hinges on an anticipated increase in demand for cement in the light of record high infrastructure deficit, low cement consumption per capita, and aggressive capacity expansion. In contrast with peers, BUACEMENT now has the lowest ex-factory price, following efforts to reduce the cement market price. We expect the firm to continue underpricing its peers in a bid to gain market share and increase its market penetration. Higher government spending towards infrastructure projects (c.9.0% of the FGN Capex) and rising bias towards cement roads are pivotal to the midterm revenue growth expectations. The cement subsector GDP has grown by an average of 5.4% over the past three years, while the construction subsector of GDP has increased by 3.8% over the last two years. We are also optimistic about the strong position of the new administration on infrastructure matters. In addition, we expect exports to improve materially from FY'24, following the re-opening of borders and increased enforcement of the African Continental Free Trade Area (AfCFTA).

Figure 26: Production capacity projections (MT)

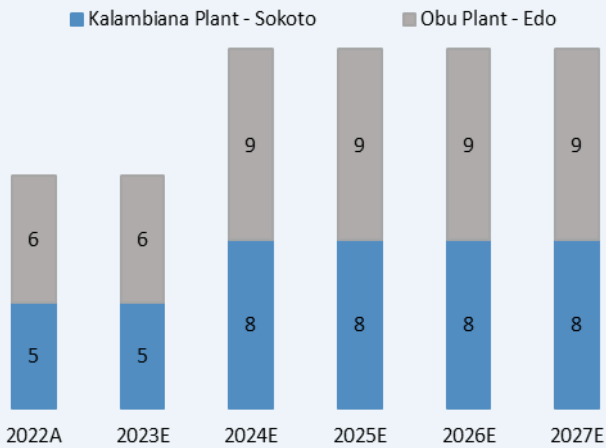


Figure 27: Annual Projected Volumes (MT)

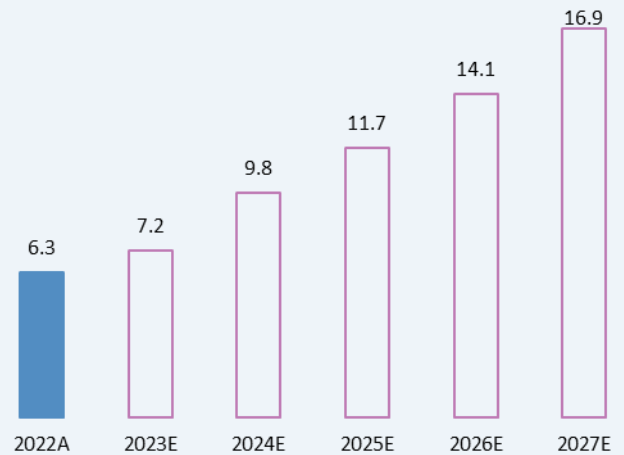
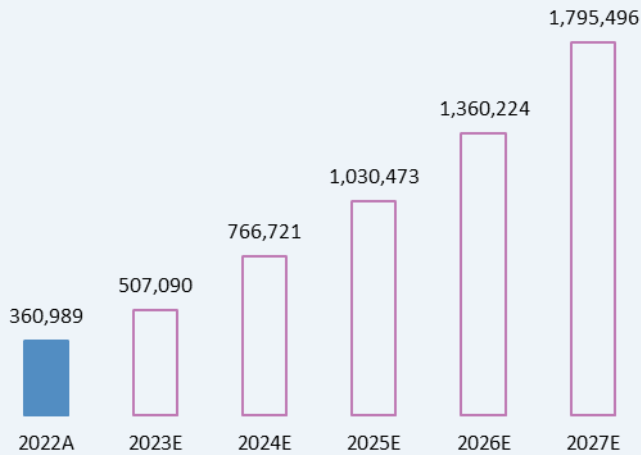


Figure 28: Revenue (N' million) over our forecast horizon



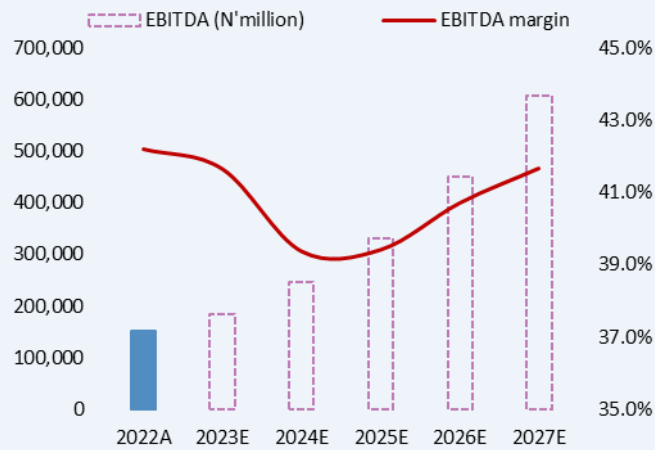
Source: Company financials, CardinalStone Research

FX liberalisation, VAT charge on AGO to push energy costs higher

We forecast an average EBITDA margin of 41.2% across FY'23E to FY'27E, largely driven by potential shocks to energy costs owing to the implementation of the 7.5% VAT on Automotive Gas Oil (AGO, also known as diesel) and the liberalisation of the foreign exchange market. This pressure will likely offset some efficiency gains from economies of scale in the short to medium term. We anticipate product churn rates as the company gradually replaces output from the old "CCNN" plants with those from new plants. While the company seeks to reduce its reliance on diesel, we are still worried about the impact of the devaluation of the Naira, especially on Liquefied Natural Gas (LNG) pricing—an alternative energy source—as a major factor in keeping costs elevated. Before the recent devaluation, the company had sought to rein in costs by substituting locally sourced LNG for imported coal at its Sokoto plant and recently signed an agreement with Wartsila OY of Finland to construct a 70megawatts dual-fuel power plant for its Obu Line 3 project in Edo State to improve energy utilization.

Gas supply, however, has some perennial problems related to availability and pricing. Nevertheless, it is cheaper than LPFO and more environmentally friendly than coal. The latter indicates that gravitation to gas aligns more with the federal government's effort around reducing gas flaring and ESGs. Overall, we project an EBITDA CAGR of 34.8% over the period.

Figure 29: EBITDA/EBITDA margin forecast period

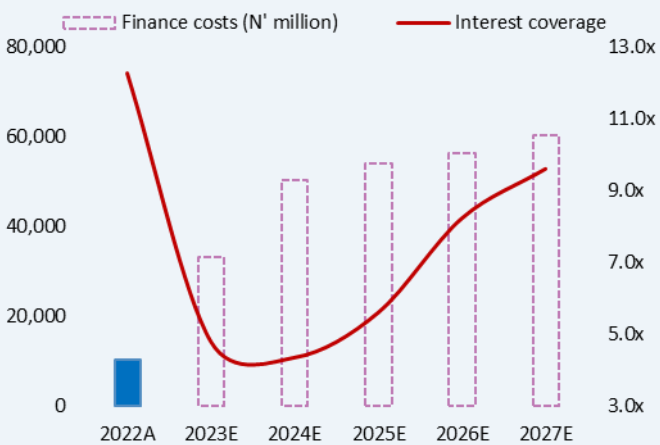


Source: Company financials, CardinalStone Research

Tax incentives to alleviate margin pressure from surging interest expense

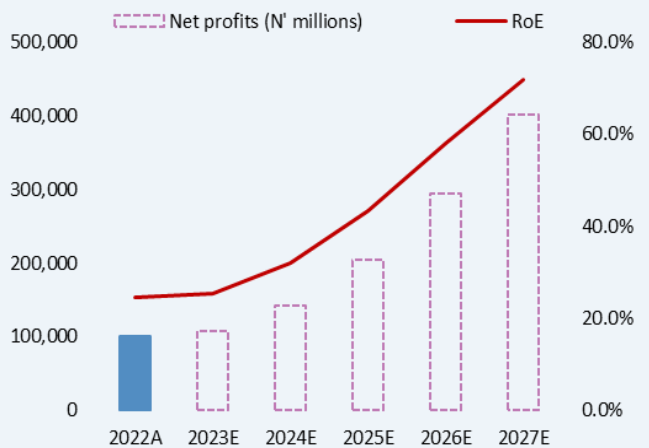
We project an uptrend in net margin over our forecast horizon despite expectations of a gradual increase in interest expense. This view is due to the company's policy of capitalizing borrowing costs on newly built plants until commissioned. We envisage a shrinkage in interest coverage ratio from 12.3x in FY'22 to 9.6x by FY'27 on the back of debt raises to finance capacity expansion. We note that the pioneer tax incentives on Obu Line 1 and Kalambaina Line 2 will expire in 2023. However, an upside risk is that the company should obtain pioneer tax status on its Obu Line 3 and Sokoto Line 5 plants when they go live in FY'24.

Figure 30: Interest expense vs Interest coverage



Source: CardinalStone Research

Figure 31: Net Profits & ROE forecast



Strong EPS growth to support high dividend payout

BUACEMENT's dividends per share (DPS) outpaced its earnings per share (EPS) expansion between 2018 and 2022. During this period, EPS grew by a CAGR of 12.1%, while DPS grew by a CAGR of 22.3%. The company's dividend payout ratio also moved from 2.0% in 2018 to 87.0% in 2022. Over our forecast period, we expect EPS to grow at a CAGR of 38.7%, with DPS set to follow a similar trajectory, provided the company maintains its payout ratio.

Valuation

We initiate coverage on BUACEMENT with a HOLD rating, using a blend of DCF and relative valuation (PE and EV/EBITDA) derived target price of N93.13 (vs ref price of N105.80).

DCF

Using DCF methodology, we arrive at an equity value of N3,302.9 billion for BUACEMENT, translating to a target price of N97.53. Our valuation assumes a beta of 0.40 (using Bloomberg's adjusted beta estimate), a risk-free rate of 14.5% (yield on the 10-year Nigerian government bond), and a cost of equity of 19.01%. Other assumptions of our DCF are as shown in the table below:

Figure 32: Discounted Cashflow main assumptions

Equity beta	0.40
Risk free rate	14.5%
Equity risk premium	16.38%
Cost of equity	21.05%
Cost of Debt	5.36%
Marginal tax rate	30.00%
After tax cost of debt	3.75%
WACC	19.01%

Source: CardinalStone Research

Figure 33: DCF table

N'million		2023E	2024E	2025E	2026E	2027E
EBIT		183,059.56	270,559.18	374,093.55	520,908.39	714,501.83
Cash Taxes		(29,165.78)	(43,106.57)	(59,602.08)	(82,993.21)	(113,837.29)
NOPAT		153,893.77	227,452.61	314,491.47	437,915.18	600,664.54
Depreciation & Amortization		24,541.92	25,712.96	26,524.74	27,181.54	27,727.56
Capex		(84,177.01)	(61,337.66)	(51,523.63)	(47,607.84)	(44,887.39)
Changes in NWC		15,454.67	46,500.39	32,731.11	41,897.83	52,896.47
Unlevered FCFF		109,713.35	238,328.30	322,223.68	459,386.72	636,401.19
Discounted Free Cashflow		93,564.18	173,330.84	199,851.67	242,984.67	287,065.85
Perpetual growth rate	4.0%					
Terminal Value	5,603,097.41					
Discounted Terminal Value	2,527,427.60					
Present Value of FCF	3,524,224.80					
Net Debt	221,299.04					
Fair Value of Equity	3,302,925.77					
FV per share	97.53					

Relative valuation

BUACEMENT is currently trading at a forward EV/EBITDA of 19.6x, which looks expensive relative to our select EMEA average of 14.1x and ahead of its four-year mean of 18.7x. However, the company also boast a LTM ROE of 22.1%, which is at a premium to its historical mean of 21.5% and the average of EMEA peers (13.4x), suggesting some little justification for its EV/EBITDA.

Figure 34: Comparable companies across emerging markets

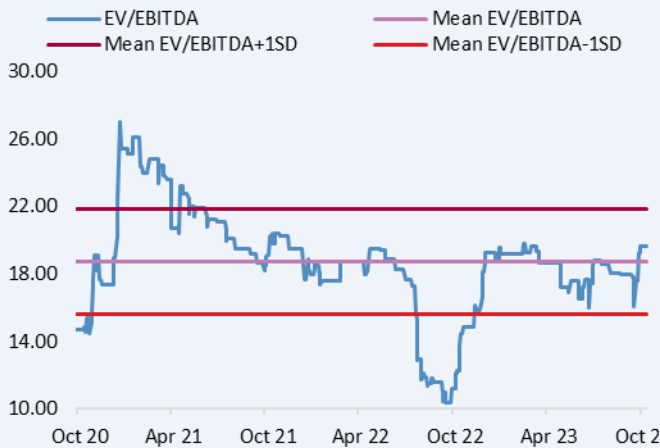
Ticker	Company	Market Cap (\$'m)	EBITDA (LTM, \$m)	EBITDA Margin (LTM)	Fwd EV/EBITDA	Fwd P/E
NGSE:WAPCO	Lafarge Africa Plc	618.10	143.30	29.1%	2.6x	7.3x
NGSE:DANGCEM	Dangote Cement Plc	7,350.50	990.40	43.9%	7.5x	13.5x
NSEI:SHREECEM	Shree Cement Limited	11,058.80	380.70	17.1%	20.9x	47.6x
SASE:3050	Southern Province Cement Company	1,646.20	116.80	37.0%	13.6x	25.7x
NSEI:ULTRACEMCO	UltraTech Cement Limited	8,641.20	850.10	15.8%	16.8x	28.0x
BSE:532644	J.K. Cement Limited	2,956.30	155.50	12.7%	14.7x	32.5x
	Mean	5,378.52	439.47	25.9%	12.7x	25.8x
	Median	5,153.40	268.10	23.1%	14.1x	26.8x
NGSE:BUACEMENT	BUA Cement Plc	3,709.70	207.20	41.1%	19.6x	24.8x

Source: Capital IQ, CardinalStone Research

Figure 35: Relative valuation sheet

EV/EBITDA valuation summary, N'billions (unless otherwise stated)	
Peer forward multiple	14.1x
FY23F EBITDA	208
Enterprise value	2,934
Plus: Cash	364
Less: Debt	(585)
Equity value	2,713
Shares outstanding (m)	34
Value per share (N)	80.12
P/E valuation summary	
Peer forward multiple	26.8x
FY23 EPS (N)	3.74
Value per share (N)	100.27

Figure 36: BUACEMENT at a premium to historical average



Source: Capital IQ, CardinalStone Research

Figure 37: Strong ROE justifies premium rating

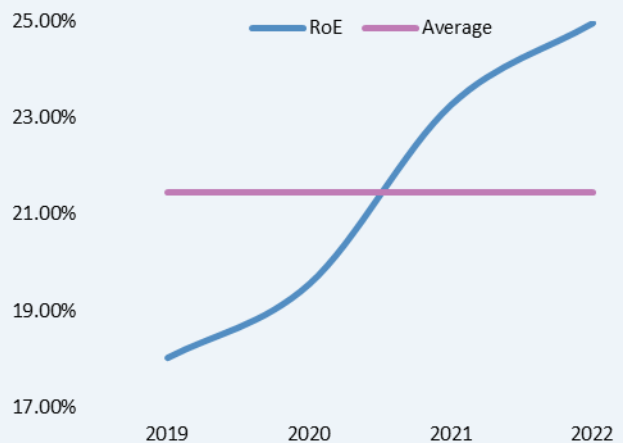


Figure 38: Valuation summary, Naira per share

Methodology	Fair values	Weight
DCF	97.53	40%
EV/EBITDA	80.12	30%
P/E	100.27	30%
TP	93.13	

Valuation Summary

Our application of relative valuation methodology assumes a 12-month target PE and EV/EBITDA of 26.8x and 14.1x, respectively. Our estimate using this approach suggests a target price of N93.13 per share.

Risk to expectations

Pricing

Given the recent reduction in ex-factory prices aimed at expanding market share, there is a potential risk associated with price volatility. The strategic decline in prices seeks to capture a larger market segment; however, market conditions or external factors may lead to unexpected price fluctuations within the cement industry, especially a potential price war led by the market leader. In addition, other factors like fluctuations in production costs could impact cement pricing in a manner that deviates from initial expectations.

Slower market share capture

The potential market share capture expected to offset the impact of lower prices might take time. Hence, BUACEMENT could lose on the volume and pricing front for an extended period following unanticipated variations in construction demand and the inability to pull additional customers due to high switching costs. Even well-planned pricing strategies may encounter unforeseen market forces. Therefore, continuous monitoring and adaptation to changing market conditions will be essential to manage this risk effectively.

Gas supply

Given that the operation of BUACEMENT's plant is heavily dependent on gas supply, we highlight this as an inherent risk to our forecasts. Despite several short-term challenges and bottlenecks associated with gas availability and pricing, we believe:

- I. It is cheaper than LPFO and more environmentally friendly to extract and burn than coal.
- II. The Federal Government's efforts around reducing Gas flaring are expected to stabilize the gas supply to cement producers in the near term.

Currency devaluation and inflationary pressures

We recognize the margin-pressuring impact of currency devaluation as an inherent risk to our costs forecast, considering that about 30.0% of production costs are FX-linked, especially energy. The combination of high inflation and free-floating currency volatility remains a considerable risk to our projections.

Region insecurity

BUACEMENT is the major cement producer in the North-West region of Nigeria, which has experienced insecurity in recent years. The risk posed here is the threat of disruption to operations, vandalism of BUACEMENT's plants and equipment, and possible disruptions to LNG supply to BUACEMENT and product haulage to its customers.

Climate changes

Climate change may also directly impact the operations of the company. Periods of torrential rainfall tend to limit the demand for cement, as witnessed in Q3 2022.

Figure 39: BUACEMENT Summary of financials and forecasts

Income Statement (N'million)					Cash Flow Statement (N'million)				
	2021A	2022A	2023E	2024E		2021A	2022A	2023E	2024E
Revenue	257,327	360,989	507,090	766,721	Cash flow from operating activities	154,009	149,574	198,001	303,272
COGS	(136,390)	(197,944)	(278,900)	(444,698)	o/w Depreciation & amortization	15,344	22,135	25,398	26,610
Gross profit	120,937	163,045	228,191	322,023	o/w Changes in working capital	34,445	(5,827)	15,455	46,500
Other Income	2,628	2,786	3,042	2,207	Cash flow from investing activities	(58,077)	(102,275)	(84,339)	(62,349)
OPEX	(19,340)	(36,111)	(48,174)	(53,670)	o/w Capital expenditure	(57,614)	(102,285)	(84,177)	(61,338)
EBIT	104,225	129,720	183,060	270,559	as % of sales	22.4%	28.3%	16.6%	8.0%
Net Interest	(1,351)	(9,566)	(30,636)	(46,125)	Cash flow from financing activities	(157,453)	(61,628)	202,264	(9,335)
PBT	102,873	120,154	152,423	224,434	o/w Dividends paid	(70,000)	(88,047)	(110,275)	(160,417)
Tax	(12,794)	(19,143)	(25,912)	(40,398)	o/w Debt issued/(repaid)	(72,895)	41,467	354,448	235,667
PAT	90,079	101,011	126,511	184,036	Opening Cash and cash equivalents (incl. FX diff.)	123,859	62,377	48,047	363,972
EPS	2.66	2.98	3.74	5.43	Net change in cash	(61,521)	(14,330)	315,926	231,588
DPS (NGN)	2.60	2.80	3.26	4.74	Closing Cash and cash equivalents	62,338	48,047	363,972	595,561
Payout ratio	77.7%	87.2%	87.2%	87.2%					
Shares outstanding ('000)	33,864.35	33,864.35	33,864.35	33,864.35					

Balance Sheet (N'million)					Ratio Analysis				
	2021A	2022A	2023E	2024E		2021A	2022A	2023E	2024E
Cash and cash equivalents	62,338	48,047	363,972	595,561	Gross Margin	47.0%	45.2%	45.0%	42.0%
Accounts receivable	38,017	16,548	16,548	16,548	EBITDA Margin	46.5%	42.2%	40.9%	38.6%
Inventories	39,068	52,468	59,324	63,524	EBIT Margin	40.5%	35.9%	36.1%	35.3%
Other current assets	4,776	80,708	90,304	105,030	Net Profit Margin	35.0%	28.0%	24.9%	24.0%
Current assets	144,199	197,770	530,148	780,663	ROE	22.6%	24.6%	29.6%	40.8%
PP&E	578,888	669,013	727,792	762,519	ROA	12.4%	11.6%	10.0%	11.8%
Intangible Assets	5,343	7,139	10,028	15,163	ROIC	16.6%	17.3%	10.0%	10.4%
Other non-current assets	77	89	129	129	ROCE	17.9%	21.0%	20.0%	25.3%
Total assets	728,507	874,012	1,268,097	1,558,474	OPEX/Sales	7.5%	10.0%	9.5%	7.0%
Short-term borrowings	39,810	80,695	143,965	214,665	Net debt/Equity (x)	0.0	0.1	0.1	0.1
Payables	22,278	78,112	110,059	175,486	Net debt/EBITDA (x)	0.2	0.5	0.6	0.4
Other short-term liabilities	83,266	98,753	98,753	98,753	Sales/Assets (x)	0.4	0.4	0.4	0.5
Current liabilities	145,355	257,561	352,777	488,904	Assets/Equity (x)	0.6	0.9	1.2	1.7
Long-term debt	43,685	44,740	335,918	500,885	Interest cover (x)	61.1	12.3	5.5	5.4
Other long-term liabilities	141,350	160,598	152,053	117,718	Tax Rate	12.7%	16.7%	17.0%	18.0%
Total liabilities	330,391	462,899	840,749	1,107,507	Revenue Growth	22.9%	40.3%	40.5%	51.2%
Shareholders' equity	398,117	411,113	427,349	450,967	EBITDA Growth	23.1%	27.2%	36.3%	42.7%
Minority interests	-	-	-	-	EPS Growth	24.3%	12.1%	25.2%	45.5%
Total liabilities & equity	728,507	874,012	1,268,097	1,558,474					

Valuation				
	2021A	2022A	2023E	2024E
BVPS	11.76	12.14	12.62	13.32
Growth	5.9%	3.3%	3.9%	5.5%
Net debt/(cash)	21,157	77,389	115,911	119,989
P/E (x)	39.8	35.5	28.3	19.5
P/BV (x)	9.0	8.7	8.4	7.9
EV/EBITDA (x)	30.1	24.0	17.8	12.5
Dividend Yield	2.5%	2.6%	3.1%	4.5%

Source: Company Financials, CardinalStone Research estimates

Note: N in millions (except per-share data). Fiscal year ends in December. o/w - out of which

Disclosure

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CardinalStone employs a 3-step rating system for equities under coverage: Buy, Hold, and Sell.

Buy $\geq +15.00\%$ expected share price performance

Hold $+0.00\%$ to $+14.99\%$ expected share price performance

Sell $< 0.00\%$ expected share price performance with weak fundamentals

A BUY rating is given to equities with strong fundamentals, which have the potential to rise by at least $+15.00\%$ between the current price and the analyst’s target price

An HOLD rating is given to equities with good fundamentals, which have upside potential within a range of $+0.00\%$ and $+14.99\%$,

A SELL rating is given to equities that are highly overvalued or have weak fundamentals, where potential returns of less than 0.00% are expected between the current prices and the analyst’s target prices. However, for equities with potential returns of less than 0.00% , HOLD ratings may be assigned if they have recent histories of strong earnings and/or their outlooks are favourable for the next 12 months, even if they appear to be currently overvalued by the market.

A NEGATIVE WATCH is given to equities whose fundamentals may deteriorate significantly over the next six (6) months, in our view.

A POSITIVE WATCH is given to equities whose fundamentals may improve significantly over the next six (6) months, in our view

CardinalStone Research distribution of ratings/Investment banking relationships as of October 25, 2023

Rating	Buy	Hold	Sell	Negative watch
% of total recommendations	50%	27%	23%	0%
% with investment banking relationships	0%	0%	0%	0%

Valuation and Risks: Please see the most recent company-specific research report for an analysis of valuation methodology and risks on any security recommended herein. You can contact the analyst named on the front of this note for further details.

Frequency of Next Update: An update of our view on the company (ies) would be provided when next there are substantial developments/ financial news on the company.

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