LAFARGE

Lafarge Cement Zimbabwe Limited

Third Quarter Trading Update

TRADING ENVIRONMENT

The operating environment in the second half of the year continues to be challenging for the business as the effects of hyperinflation become more evident due to cost inflation caused by devaluation. Following the suspension of the publication of official year on year inflation data in July 2019, the published ZIMSTATS month on month inflation rates indicate an implied year on year inflation rate in excess of 350% as at September 2019. The high inflation rate has become the biggest threat to volume growth as it has eroded disposable income resulting in a 19% decline in year to date cement consumption per capita against prior year. This decline is in line with the International Monetary Fund projection of a 5.3% contraction in Zimbabwe's 2019 Gross Domestic Product.

The business environment remained volatile weighed down by cost inflation, foreign currency exchange rate and the increased cost of borrowing. As a result demand from individual home builders decreased necessitated by mortgage financing cost increase driven by an escalation in average lending rates to over 30%. This affected the execution of a number of construction projects as well as delays in investment into new projects. In addition, the business experienced forex constraints on which Lafarge relies on for its import requirements. This has created a backlog of payments to suppliers for critical spares and capex projects. We are, however, working closely with our bankers to ensure that operations are not compromised

The business remains vigilant in managing its costs and ensuring prices reflect the changing cost structure with regular but modest price reviews in consideration for the decreasing disposable incomes that are lagging behind inflation.

BUSINESS PERFORMANCE

The business has remained focused on implementation of its 2019 Strategic agenda with a key focus on building financial strength and mitigating against the negative effects of the current trading environment. Despite the challenges production output has recorded a marginal 1% decline against prior year owing to plant reliability which encountered unplanned stoppages and power supply challenges. Above this significant cost reduction actions have been taken in the quarter to keep the business competitive.

Volumes for Dry Mortar Mix products (DMX) excluding Agricultural Lime have recorded marked growth compared to prior year. The late kickoff of the financing arrangements for the Government assisted 'Smart Agriculture' program has affected Agricultural Lime which is one of the main DMX products and its demand peaks during the agricultural preparation season. Management is actively driving production and logistics to ensure that the volumes committed to the program are fulfilled before the full onset of the rains.

KEY ISSUES AFFECTING THE BUSINESS

The business sees opportunities in the growth of the construction sector beyond 2020. In this vein, Management has successfully concluded financing arrangements for a US$15m facility to fund expansion cement milling capacity and the Dry Mortar Mix (DMX) plant. In addition, in order to mitigate the effect of erratic power supply, the business has embarked on alternative power supply to supplement ZESA generation as part of our expansion efforts. The capex expansion program has been rolled out and the power generating unit is now on site whilst the DMX plant is being manufactured. Work on the cement milling expansion project will commence in January 2020.

The company is actively engaging the Reserve Bank of Zimbabwe to conclude the registration of our external shareholder loan of USD28.5m and expect to conclude the matter before the end of the 2019 financial year.

In October 2019, the Public Auditors and Accountants Board (PAAB) pronounced that all financial statements for reporting periods after 1 July 2019 must comply with IAS 29 "Financial Reporting in Hyperinflation Economies". The Institute of Chartered Accountants of Zimbabwe (ICAZ) has issued guidelines on how to implement IAS 29 and has recommended the use of the Consumer Price Index (CPI) from the Zimbabwe Statistical Office (ZIMSTATS) as the general price index to be used to restate historical financial figures and arrive at inflation adjusted figures. Full year financial figures will, therefore, be restated using the CPI in order to comply with this pronouncement.

The business has engaged valuers to conduct a revaluation of its specialised equipment and other fixed assets and this exercise is expected to be concluded by the end of the year. The revaluation of the assets to reflect the correct ZWL values will result in revaluation income which the business will recognise in its full year financial reporting.

OUTLOOK

The onset of the rainy season usually heralds a tapering off in cement demand. We expect Q4 to remain relatively flat compared to last year with demand sustained by inflows from the diaspora during the festive season. The business will undertake a major plant shutdown in Q4 to carry out critical maintenance work on its manufacturing platform ahead of the 2020 financial year. We expect a continuation of the constrained macro conditions in the short term with improvements in the broader operating environment anticipated thereafter. Our focus will therefore remain on driving for operational improvements, seeking to improve cash generation and managing our costs. We believe our current portfolio provides us with a strong platform and foundation from where growth and value extraction can be derived in future, particularly when the trading environment improves.

By order of the Board

Flora Chinhaire

F.Chinhaire
Company Secretary

Tuesday, 26 November 2019

Tried & Trusted Strength