



Equity Research | Ecobank Transnational Inc.

ARM Research

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Interim Earnings Report

6 months ended 30<sup>th</sup> June, 2013

**Recommendation: BUY**

### ***Operating performance shows expected improvements***

- Ecobank Transnational Incorporated (ETI) reported a 20% YoY growth in gross earnings to N193.5 bn for 6 months ended June 2013 while PBT and PAT rose 55% and 90% YoY to N31.7bn and N26.9bn respectively.
- Revenues were 4% ahead of our N97bn forecast with both interest (+4%) and non-interest income (+3%) moderately outperforming our expectations. The improvement in interest income (+8% QoQ to N64.4bn) largely reflected expansion in earning asset volumes especially as asset yields moderated 30bps QoQ. Relative to our estimates, stronger 13% QoQ loan growth (Q1: -3%) to reach N1.62trn, matching our FY 13 estimate, was the key driver of the mild outperformance. Similarly, our expectations that the impact of regulatory changes expected to dampen fee income for the industry would be tempered on ETI due to its geographic diversification as well as its focus on bolstering capital market activities in FY 13, largely panned out. Non-interest revenue rose 6% QoQ to N35.8bn.

#### Income Statement Data

	2013- 6 'm	2012 - 6 'm	%chg
Revenue	193,485	161,626	20%
PBT	31,713	20,426	55%
Tax	(4,804)	(6,289)	-24%
PAT	26,909	14,137	90%

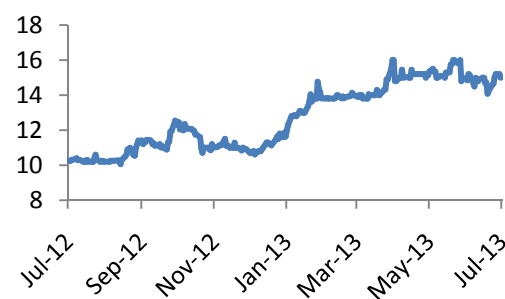
#### Balance Sheet Data

	2013-Jun 'm	2012 -Dec 'm	%chg
Cash	337,096	309,491	9%
Loans	1,616,164	1,474,487	10%
Deposits	2,521,075	2,341,113	8%
Fixed Asset	137,024	134,520	2%
Net Assets	364,830	339,921	7%

#### Stock Data

Price	N14.46
52 week range	N10.06– N16.01
Market Cap. (N'm)	248,888
1-month Avg. Vol	3,644,968
Curr. PE	5.3x
Bloomberg Ticker	ETI NL
Reuters Ticker	ETI.LG

#### ETI - Share Price Trend



#### Analyst(s)

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- Although a 7% QoQ expansion in deposit base to N2.52trn had helped drive the improvement in earning asset volumes, outcomes with interest expense, which was flat QoQ at N21.5bn, were also better than expected. Accordingly, WACF moderated 30bps to 3% which was 20bps ahead of our estimates; we had expected 7% QoQ jump in interest expense in view of deposit growth. The benign outcome for ETI reinforces an emerging pattern of relatively subdued funding costs in line with its scale.

### ***Provisions derail percolation to profit margins***

- ETI's operating expenses rose 6% QoQ and was 2% ahead of our estimates. Importantly, after see-sawing over the last 3quarters opex continues to lag revenue growth, reinforcing benefits of ETI's efforts to enhance cost efficiencies by centralizing operations and expanding technology driven channels. Consequently, CIR extended its steady downtrend to five straight quarters, declining a further 130bps QoQ to 71.3%, 200bps below our FY 13E target. Overall, operating profit was 7% ahead of our estimates with corresponding margin 200bps higher.
  - However, a 78% QoQ jump in impairment charges to N7.3bn, 44% ahead of our estimates, helped undo much of the earlier discussed gains. The sharp reversal comes on the heels of a positive Q1 13 surprise when charges came below our estimate which aimed to capture asset quality challenges, relating to either acquisitions or civil unrests in some of its African operations. The recent outcome appears to vindicate our decision to maintain our cost of risk estimates in spite of the initial positive signal.
  - Thus, provisions were primarily responsible for pegging back PBT growth to 3% QoQ at N16.1bn which put corresponding margins 100bps lower QoQ at 16%. However, this was 100bps higher than our estimate reflecting stronger revenue and 7% lower interest expense than we forecast. A 400bps QoQ decline in tax rate to 13% bolstered 9% PAT growth to N14bn with associated margin of 14% 200bps ahead of our estimate which factored in a 22% tax rate.
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***Forecasts still robust as we seek clarity on provisions***

- Interest income has again matched our estimates as expected earning asset volume-driven improvements continues to materialize. However, with the pace slightly stronger than expected we have made mild upward adjustments to earning asset volumes. We have also made similar upward adjustments to non-interest revenue encouraged by its resilience to last year's CRR hike as well as apparently limited impact from regulatory charges which kicked in Q2 13. Overall, our Q3 13E revenues are 3% higher from previous to match Q2 13 levels.
  - Perhaps more evidently, funding cost pressures are not as strong as initially envisaged as post-acquisition synergies appear to become more entrenched; the flat performance in H1 13 puts run-rate 8% behind our FY 13 estimates. Regardless we have only cut back our interest expense estimates by approximately half this magnitude as competition should intensify further with the recent CRR hike. Accordingly, our FY 13E WACF is 20bps lower at 3% while we expect Q3 13E interest expense to come in 5% higher QoQ at N21.6bn.
  - Whilst opex remains broadly in line, we have slightly raised our estimates to account for moderately faster QoQ growth. Nonetheless, the impact is offset by the relatively faster growth in revenues resulting in a 150bps cutback in our CIR estimate to 72% which is more in line with recent improvements.
  - However, the sharp reversal in impairments gives us cause for concern especially as it punctuates recent stability in an erstwhile trouble spot. Thus, pending clarity from management on exact drivers, we have raised our already conservative estimates to match the run-rate in H1 figures even though Q2 13 jump could yet prove a one-off. Adjustments to interest income and revenue are primarily responsible for 10% higher FY 13 PBT estimate while a 3ppt cut-back in tax rates to match average over the past four quarters is responsible for PAT estimate being 14% higher than previous from previous (EPS: N3.04).
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***Upside potential sustains BUY rating***

- The higher revisions to profits have resulted in 9% increment in our fair value to **N24.7**. ETI trades at a current PE multiple of 5.3x and 4.6x FY13EPS compared to Tier 1 average of 6x and 5.9x respectively. Price to book of 0.7x is also much lower than 1.4x average for peers. Reflecting the wider 71% upside variation in our fair value estimate to current price after recent declines, we maintain a **BUY** rating on the stock.

## Summary of Forecasts

<b>Quarterly</b>					
<b>Income Statement (N'm)</b>	<b>Q3 2013E</b>	<b>Q4 2013E</b>	<b>Q1 2014E</b>	<b>Q2 2014E</b>	
Net interest income	40,348	41,081	44,803	46,632	
Non-interest income	35,709	36,357	36,516	38,006	
<b>Total Revenue</b>	<b>76,056</b>	<b>77,438</b>	<b>81,319</b>	<b>84,638</b>	
Total Operating Costs	(54,957)	(55,955)	(58,550)	(60,940)	
<b>Operating Profit</b>	<b>21,100</b>	<b>21,483</b>	<b>22,769</b>	<b>23,699</b>	
Impairment Charge	(4,796)	(4,883)	(4,989)	(5,192)	
<b>Pre-tax Profit</b>	<b>16,304</b>	<b>16,600</b>	<b>17,781</b>	<b>18,506</b>	
Tax	(3,703)	(3,771)	(4,090)	(4,256)	
<b>Post-tax Profit</b>	<b>12,602</b>	<b>12,831</b>	<b>13,691</b>	<b>14,250</b>	
<b>Annual</b>					
<b>Income Statement (N'm)</b>	<b>2012A</b>	<b>6m' 2013</b>	<b>2013E</b>	<b>2014E</b>	<b>2015E</b>
Net interest income	135,636	80,956	162,384	182,871	206,932
Non-interest income	130,957	69,548	141,614	149,044	150,611
<b>Total Revenue</b>	<b>266,593</b>	<b>150,504</b>	<b>303,998</b>	<b>331,916</b>	<b>357,543</b>
Total Operating Costs	- 200,089	- 107,359	- 218,270	- 238,979	- 250,280
<b>Operating Profit</b>	<b>66,504</b>	<b>43,145</b>	<b>85,727</b>	<b>92,936</b>	<b>107,263</b>
Impairment Charge	- 22,358	- 11,428	- 21,107	- 20,362	- 21,166
<b>Pre-tax Profit</b>	<b>44,049</b>	<b>31,713</b>	<b>64,620</b>	<b>72,574</b>	<b>86,097</b>
Tax	- 9,723	- 4,804	- 12,278	- 16,692	- 21,524
<b>Post-tax Profit</b>	<b>34,326</b>	<b>26,909</b>	<b>52,342</b>	<b>55,882</b>	<b>64,573</b>
<b>Balance Sheet (N'm)</b>					
<b>Assets</b>					
Cash & Short term funds	452,979	634,494	620,858	667,518	808,617
Due from banks	339,716	301,969	313,522	372,046	301,468
Net Loans	1,474,487	1,616,164	1,665,556	1,793,075	1,929,900
Fixed Assets	134,520	137,024	156,761	167,421	158,667
Other Assets	714,141	652,337	731,552	725,490	773,504
<b>Total Asset</b>	<b>3,115,843</b>	<b>3,341,988</b>	<b>3,488,249</b>	<b>3,725,549</b>	<b>3,972,156</b>
<b>Liabilities</b>					
Deposits	2,341,113	2,521,075	2,597,236	2,753,070	2,918,255
Due to banks	103,423	155,843	77,299	98,913	105,479
Borrowings	196,053	161,816	228,804	230,796	210,958
Other liabilities	135,334	138,425	163,873	187,934	253,150
<b>Total liabilities</b>	<b>2,775,922</b>	<b>2,977,159</b>	<b>3,067,212</b>	<b>3,270,714</b>	<b>3,487,842</b>
<b>Shareholders' fund</b>	<b>339,921</b>	<b>364,830</b>	<b>421,037</b>	<b>454,836</b>	<b>484,315</b>
<b>Key Data</b>					
EPS Rep GAAP	1.65	1.38	3.06	3.26	3.77
DPS	0.62	-	1.05	1.45	2.24
BVPS	19.75	21.20	24.46	26.43	28.14
ROE	13%	6%	12%	12%	13%
ROA	1.4%	1.1%	1.5%	1.5%	1.6%
<b>Key Ratios</b>					
Loan to Asset	47%	48%	48%	48%	49%
Cost to income	75%	71%	72%	72%	70%
Net Profit Margin	10%	14%	13%	13%	14%
Liquidity ratio	32%	35%	35%	36%	37%
Capital adequacy ratio	19%	19%	18%	18%	18%

Source: Company financials, ARM Estimates

### 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
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 reasonable portfolio constraints
UNDERWEIGHT	Minimise exposure to security taking cognizance of its index weighting
SELL	Sell-off security completely from portfolio

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