

- Fidelity Bank Plc. (Fidelity) released unaudited 9M 2016 results wherein PBT and PAT both declined 29% and 24% YoY to ₦9.82 billion and ₦8.8 billion respectively. The reading marks a an improvement from H1 16 when PBT and PAT were down 35% and 32% YoY respectively as stronger net interest income more than offset weaker noninterest revenues in Q3 16. Relative to our estimates, earnings are modestly ahead due to a strong net interest income than in our forecasts.

*Higher asset yields offsets funding cost blues*

- In line with sector wide trends for banks that have reported thus far, stronger asset yields (+170bps QoQ) a fallout of the upward loan repricing paved the way for an expansion in interest income (+22.6% QoQ to ₦34.3billion). As in Q2 16, net loan growth remains driven by FX translation impact. That said, Fidelity, as with Tier II piers over Q3 16, reported sizable expansion in interest expense with annualized WACF climbing 90bps QoQ to 5.5%. Given improvement in term mix (CASA+3.3pps to 58%), funding pressures emanated from spike in other borrowings (+60% QoQ).

**Income Statement Data**

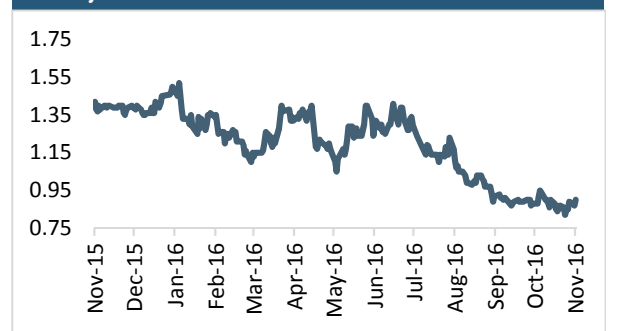
	2016 – 9M'm	2015 – 9M'm	%chg
<b>Gross Earnings</b>	107,444	106,570	0.8%
<b>PBT</b>	9,835	13,789	-28.7%
<b>Tax</b>	(1,082)	(2,344)	-53.8%
<b>PAT</b>	8,753	11,445	-23.5%

**Balance Sheet Data**

	2016-Sept 'm	2015 -Dec 'm	%chg
<b>Cash</b>	215,599	229,567	-6%
<b>Loans</b>	547,703	729,023	33%
<b>Deposits</b>	795,592	765,785	4%
<b>Fixed Asset</b>	40,735	41,278	1%
<b>Net Assets</b>	180,339	184,985	3%

**Stock Data**

<b>Price</b>	₦0.89
<b>52-week range</b>	₦0.82 – ₦1.52
<b>Market Cap. (N'm)</b>	25,208
<b>1-month Avg. Vol</b>	8,592,521
<b>Curr. PE</b>	2.3x
<b>Bloomberg Ticker</b>	FIDELITY:NL

**Fidelity Bank Plc- Share Price Trend**

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- Elsewhere, NIR declined 25% QoQ to ₦4.9 billion (Q3 16E: ₦5.2 billion) as declines across credit related fees (-11%), COT (-22%), e-banking (-60%) and fees (-51% QoQ to ₦3 billion) more than offset gains in both other operating income (+92%) and FX translation gain (₦1.7 billion) over Q3. Management attributes the suspension of international card transactions on its naira cards as the key underpin for NIR slowdown.
- That said, interest income strength shone through as it offset NIR weakness and higher OPEX (+8.7% to ₦17 billion, Q4 16E ₦15.4 billion) leading to an 80bps QoQ cutback in CIR to 73.3%. The QoQ OPEX expansion stems from higher marketing, communication and entertainment (+81% QoQ), computer expenses (+58% QoQ) and depreciation (+54% QoQ).

#### *Impairment charges moderate, for now*

- Despite a rise in NPL ratio (+20bps QoQ to 4.5%) in line with the weak macro landscape, loan loss charges declined 22% QoQ to ₦3.2 billion with annualized cost of risk sliding 50bps QoQ to 1.7% (9M 16: 1.5%). However, the line item remains the key drag on Fidelity's results over 9M 16. Fidelity links the asset quality issues to adverse fall-out from NGN depreciation on trade finance facilities in general commerce and manufacturing.

#### *Asset quality concerns to weigh on earnings outlook*

- Going into the last quarter of 2016, we think the CBN is more likely to maintain monetary tightening over Q4 16 and accordingly, recast our asset yields upward to match the 9M 16 run rate which translates Q4 16E interest income at ₦34.8 billion (+4% YoY). The Q4 16E reading by extension results in FY 16E of ₦126 billion—down from ₦132 billion previously. Similarly, we expect funding cost pressures to persist and adjust our 2016 WACF assumption higher to 5.6% which translates to interest expense at ₦16 billion for Q4 16 and ₦56.8 billion for FY 16E.
- Following disappointment in NIR and OPEX we adjust our forecasts to match the 9M 16 run rate. On asset quality, persisting dollar paucity, which drove higher NPLs

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in Manufacturing and General Commerce, stoke worries over Q4 16E impairment charges. In addition, we think Fidelity's exposure to upstream O&G (18%) and Power (11%) leaves it susceptible to pass through from worsening macro land scape. Consequently, we see scope for cost of risk, which currently tracks behind our FY 16 estimate of 2% for Fidelity to rise from current levels. Cumulative impact of our adjustments drive a moderation in FYE 16 earnings (PBT: -46 YoY, PAT: -52%YoY).

- Though Fidelity's CAR had declined 190bps YTD to 16.8%, management revealed that Fidelity has obtained approval from CBN to allow re-classification of non-distributable reserves in line with proper definition <sup>[1]</sup>which should raise CAR to 18% on FY audits. Should this process go as planned, Fidelity intends to stick to its dividend pay-out policy of 30-50%. We assume pay-out at the lower band which yields FY 16E DPS of N0.07 – 7.8% dividend yield on current pricing.
  - Fidelity currently trades at P/E and P/B of 2.3x and 0.14x which are at discount to peer average at 4.6x and 0.4x respectively. Though our FVE declines to ~~N1.03~~, the stock has declined 41% YTD with last trading price of ~~N0.89~~ implying a **NEUTRAL** rating on the stock.
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## Summary of Results and Forecasts - Naira (₦)

QUARTERLY					
Income Statement (₦'000)*					
	Q1 2016A	Q2 2016A	Q3 2016A	Q4 2016E	
Gross earnings	33,895	34,422	39,127	38,446	
Interest Income	29,204	27,959	34,265	34,790	
Interest Expense	(13,100)	(12,435)	(15,373)	(15,952)	
Net interest income	16,104	15,524	18,892	18,837	
Non-Interest Revenue	4,691	6,463	4,862	3,656	
OPEX	(16,031)	(15,670)	(17,040)	(17,693)	
Provisions	(739)	(4,059)	(3,162)	(7,033)	
PBT	4,025	2,258	3,552	(2,233)	
Tax	(443)	(248)	(391)	246	
PAT	3,582	2,010	3,161	(1,987)	
ANNUAL					
Income Statement (₦'000)*					
	FY 2014A	FY 2015A	FY 2016F	FY 2017F	FY 2018F
Gross earnings	130,055	144,189	145,890	144,893	155,635
Interest Income	104,307	121,158	126,218	123,673	131,703
Interest Expense	(55,481)	(60,294)	(56,860)	(54,540)	(59,959)
Net interest income	48,826	60,864	69,357	69,133	71,744
Non-Interest Revenue	25,748	23,031	19,672	21,220	23,932
OPEX	(54,753)	(64,107)	(66,434)	(66,876)	(69,303)
Provisions	(4,306)	(5,764)	(14,993)	(9,548)	(7,025)
PBT	15,515	14,024	7,602	13,928	19,348
Tax	(1,719)	120	(836)	(2,089)	(2,902)
PAT	13,796	14,144	6,766	11,838	16,445
Balance Sheet (₦ '000)*					
Assets					
Net Loans	258,131	185,332	194,599	204,329	214,545
Fixed Assets	541,686	578,203	749,665	636,563	702,523
LT investment	37,958	39,985	41,193	42,853	45,462
Other Assets	160,390	297,343	318,041	340,356	364,428
Total Assets	1,187,025	1,231,722	1,439,490	1,504,096	1,573,794
Liabilities					
Deposits	820,034	769,636	845,802	888,209	931,785
Borrowings	1,719	2,332	2,332	2,332	2,332
Total liabilities	124,521	151,406	278,271	292,185	306,794
Shareholders' fund	1,013,914	1,048,206	1,251,237	1,307,557	1,365,742
Key Ratios					
EPS	0.47	0.55	0.23	0.41	0.57
DPS	0.18	0.16	0.07	0.12	0.17
BVPS	5.98	6.34	6.50	6.79	7.18
ROE	8.2%	7.8%	3.6%	6.2%	8.1%
ROA	1.2%	1.2%	0.5%	0.8%	1.1%
Asset yields	12.4%	13.4%	12.0%	11.3%	12.0%
WACF	6.1%	6.5%	5.6%	4.7%	5.0%
Cost of risk	0.8%	1.0%	2.0%	1.5%	1.0%
Loan to Asset	46%	47%	52%	42%	45%
Loan to deposits	66%	75%	89%	72%	75%
Cost to income	73%	76%	75%	74%	72%

Source: ARM Research \*unless otherwise stated

## 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
<b>STRONG BUY</b>	>20%	<b>BUY</b>	>20%
<b>OVERWEIGHT</b>	10% — 20 %	<b>NEUTRAL</b>	5% — 20 %
<b>NEUTRAL</b>	0% — 10 %	<b>SELL</b>	<5%
<b>UNDERWEIGHT</b>	-5% — 0%		
<b>SELL</b>	<-5%		

RECOMMENDATION KEY	
Rating	Recommendation
<b>BUY</b>	Accumulate security to a substantial extent constrained only by portfolio diversification considerations
<b>OVERWEIGHT</b>	Accumulate security to an extent moderated by cognizance of its benchmark weight
<b>NEUTRAL</b>	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
<b>UNDERWEIGHT</b>	Minimise exposure to security taking cognizance of its index weighting
<b>SELL</b>	Sell-off security completely from portfolio

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