

United Bank for Africa Plc. (UBA.NL)

Stock Report

Higher NIR greases our valuation

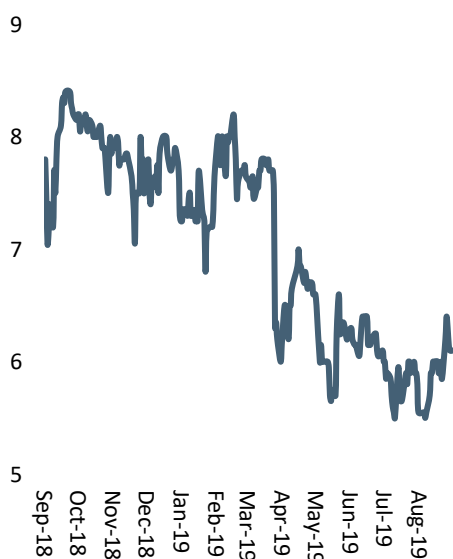
• **We have made some adjustments to our FY 19 forecasts for UBA following clarification at the management H1 19 conference call last week Thursday. We raised FY 19E non-interest revenue to reflect increased proportion of trading instruments in total investment securities than we had previously forecast. Elsewhere, management guided to possible writebacks from exposure to Ghana bulk purchasing company. However, given the increase in stage 2 loans YtD, we see some provisioning in the offing, with our FY 19E cost of risk revised lower to 0.6%. The impact of these adjustments was moderated by cut in NIM due to upward review of funding cost, with PBT revised 7% higher to ₦126 billion (+18% YoY). Accordingly, we raised FVE to ₦13.87/share (previously: ₦13.04/share) and maintain our BUY rating on the stock.**

• Key highlights for us from the call were: 1) management update on its exposure to Ghana bulk purchasing companies. With the resumption of payments to the individual companies by the government, they see some improvement which could necessitate reclassification and writebacks; 2) On the jump in the stage 2 loans (up ₦233 billion YtD, vs. improvement in absolute NPL by ₦18 billion), management stated that at least 60% of the Stage 2 is due to change in credit ratings and not necessarily deterioration in the loans; and 3) Swap positions was estimated at \$800 million with a net long position of \$328 million. The major issue for us on the call is the lack of clear guidance on the steps to address the gap in the bank's loan to deposit ratio, which settled at 48% as at H1 19, compared to regulatory benchmark of 60%.

• Coming into the year, we had expected a faster moderation in the trading book, to account for 45% of total investment securities from 61% in FY 18. As at H1 19, the trading book accounted for 58% of the investment book, with the bank booking total gain of ₦11 billion. We have adjusted the proportion accordingly. Coupled with gains on FX trading and the derivative book, we raised FY 19E net trading income higher to ₦50 billion (previous: ₦34 billion), with net fee income unchanged. Following the sharp growth in term deposits (19% YtD), with CASA growing 1% YtD and proportion declining to 74% (FY 18: 76%), we have adjusted funding cost to 4.4% (previous: 3.9%), with NIM forecast lowered to 4.5% for FY 19, from 4.7%. On its exposure to Ghana bulk purchasing companies (estimated at \$88.3

Rating	STRONG BUY
Price	₦6.10
FVE	₦13.87
52-week range	₦5.40-8.45
Market Cap. (₦'bn)	208,616
1-month Avg. Vol	3,696,873
Current PB	0.37x

UBA.NL - Share Price Trend



Analyst

Oluwasegun Akinwale

Oluwasegun.akinwale@arm.com.ng

See previous report: Rest of Africa to drive earnings growth in near term

H1 19 Initial View: Strong NIR offsets moderation in NIM

million with total provisions of \$51.8 million), management expects some writebacks in the course of the year with the resumption of payment by the government to the concerned obligors. However, we are cautious on the impact of this on the overall provisioning given the elevated levels of the Stage 2 loans and lack of improvement on its exposure to the downstream oil and gas sector (accounting for bulk of NPL). As a result, we lowered FY 19E cost of risk marginally to 0.6% (previous: 0.7%).

- The impact of these adjustments translated to a revised PBT of ₦126 billion (+18% YoY). Accordingly, we increase our sustainable RoE assumption to 16.4%, from 15% previously, following upward review of our three-year forecast to 16.4-16.7% (previous: 14.1%-15.4%). The adjustment is a 7% increase in our FVE to **₦13.87** and maintain our **BUY** recommendation. At current pricing and based on our FY 19E dividend of ₦0.96, we view expected dividend yield of 16% as attractive and could be compelling to investors. However, given the limited guidance by management on the impact a short fall in the loan to deposit/loan to funding could have on the Nigeria operation post the CBN's deadline of September 30th, we think valuation may remain depressed in the near-term. On our numbers, UBA is trading on FY19 P/E and P/B multiples of 3.4x, and 0.4x

Table 1: UBA's Previous vs. new estimates

	FY 2019E			FY 2020E			FY 2021E		
N'Million	Prev. estimates	New estimates	Change	Prev. estimates	New estimates	Change	Prev. estimates	New estimates	Change
Gross Earnings	518,368	532,878	3%	569,959	564,662	-1%	604,278	588,198	-3%
NII	225,822	217,110	-4%	246,362	222,618	-10%	250,342	242,437	-3%
NIR	116,714	127,792	9%	119,267	142,560	20%	126,321	139,305	10%
OPEX	-212,589	-208,818	-2%	-223,218	-214,571	-4%	-232,230	-221,924	-4%
Impairment	-12,627	-10,823	-14%	-15,224	-15,949	5%	-11,784	-12,346	5%
PBT	117,739	125,261	6%	127,606	134,658	6%	133,067	147,473	11%
PAT	87,127	94,260	8%	95,704	102,659	7%	99,801	112,398	13%

Summary of Results and Forecasts - ₹ Million

Balance Sheet	2017	2018E	2019E	2020E	2021E
Assets					
Inv. Securities	1,247,951	1,656,571	1,838,794	1,562,975	1,641,123
Net loans	1,650,891	1,715,285	1,803,823	1,993,600	2,057,604
Interest-earning assets	3,817,565	4,608,249	5,064,469	5,049,519	5,266,319
Total assets	3,435,587	4,237,347	4,346,500	4,923,520	5,452,989
Liabilities					
Borrowings	567,950	713,391	642,052	738,360	849,114
Deposits	2,733,348	3,349,120	3,520,871	3,979,554	4,377,708
Interest-bearing liabilities	3,435,587	4,237,347	4,346,500	4,923,520	5,452,989
Total liabilities	3,540,040	4,367,130	4,476,283	5,053,303	5,582,772
Shareholders Equity	529,434	502,608	573,390	648,126	729,951
Income Statement	2017	2018E	2019E	2020E	2021E
Gross Earnings	444,590	465,494	532,878	564,662	588,198
Interest Income	325,657	362,922	405,086	422,101	448,892
Interest Expense	(118,025)	(157,276)	(187,976)	(199,484)	(206,455)
Net Interest Income	207,632	205,646	217,110	222,618	242,437
Trading income	49,063	31,675	50,680	55,748	47,386
Net Fee Income	65,970	65,446	71,062	80,036	84,465
Other Income	3,900	5,451	6,051	6,777	7,454
Non-Interest Revenue	118,933	102,572	127,792	142,560	139,305
Staff Costs	(68,972)	(71,158)	(73,919)	(75,375)	(78,420)
Other Costs	(120,680)	(126,184)	(134,899)	(139,196)	(143,503)
Total Costs	(189,652)	(197,342)	(208,818)	(214,571)	(221,924)
Operating Profit	136,913	110,876	136,084	150,607	159,819
Provision Charge	(32,895)	(4,529)	(10,823)	(15,949)	(12,346)
PBT	104,018	106,347	125,261	134,658	147,473
Tax	(26,674)	(28,159)	(31,420)	(32,419)	(35,494)
Minorities	2,544	3,248	6,598	7,186	7,868
Net Profit	77,548	78,607	94,260	102,659	112,398
Dividend Paid	(29,070)	(29,070)	(32,991)	(37,984)	(41,587)
Key YoY growth rates	2017	2018E	2019E	2020E	2021E
Loans	9.7%	3.9%	5.2%	10.5%	3.2%
Interest Earning Assets	15.3%	20.7%	9.9%	-0.3%	4.3%
Deposits	10.0%	22.5%	5.1%	13.0%	10.0%
Interest Bearing Liabilities	16.8%	23.3%	2.6%	13.3%	10.8%
Assets	16.1%	19.7%	3.7%	12.9%	10.7%
Gross Earnings	20.3%	4.7%	14.5%	6.0%	4.2%
Costs	24.4%	4.1%	5.8%	2.8%	3.4%
PBT	15.0%	2.4%	17.7%	7.5%	9.5%
PAT	7.3%	1.4%	19.9%	8.9%	9.5%
EPS	7.3%	1.4%	19.9%	8.9%	9.5%
Per-share data (N)	2017	2018E	2019E	2020E	2021E
No of common shares (Mn)	34,199	34,199	34,199	34,199	34,199
EPS	2.27	2.30	2.76	3.00	3.29
DPS	0.85	0.85	0.96	1.11	1.22
BVPS	15.48	14.70	16.77	18.95	21.34
Balance-sheet ratios (%)	2017	2018E	2019E	2020E	2021E
Loan/Assets	40.6%	35.2%	35.7%	35.0%	32.6%
Deposit/Liabilities	77.2%	76.7%	78.7%	78.8%	78.4%
Loans/Deposits	60.4%	51.2%	51.2%	50.1%	47.0%
Assets/Equity	7.69	9.69	8.81	8.80	8.65

Asset Quality	2017	2018E	2019E	2020E	2021E
NPLs (N'million)	114,497	115,673	104,377	104,377	119,407
NPL reserves (N'million)	58,014	92,108	93,939	93,939	113,437
NPLs/Gross Loans (%)	6.7%	6.4%	5.5%	5.0%	5.5%
Reserves/NPLs (x)	0.51	0.80	0.90	0.90	0.95
Credit charge (%)	2.0%	0.3%	0.6%	0.8%	0.6%
Margins (%)	2017	2018E	2019E	2020E	2021E
Asset Yield	9.1%	8.6%	8.4%	8.3%	8.7%
WACF	3.7%	4.1%	4.4%	4.3%	4.0%
NIM	5.82%	4.88%	4.49%	4.40%	4.70%
Costs (%)	2017	2018E	2019E	2020E	2021E
Cost/Income	58.1%	64.0%	60.5%	58.8%	58.1%
Effective tax rate	25.6%	26.4%	25.0%	24.0%	24.0%
Profitability ratios (%)	2017	2018E	2019E	2020E	2021E
RoAE	15.9%	15.2%	17.5%	16.8%	16.3%
RoAA	2.0%	1.8%	1.9%	1.9%	1.9%

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
STRONG 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 reas portfolio constraints
UNDERWEIGHT	Minimize exposure to security taking cognizance of its index weighting
SELL	Sell-off security completely from portfolio

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