

|                   |                   |
|-------------------|-------------------|
| Rating            | <b>OVERWEIGHT</b> |
| Price             | ₦9.30             |
| FVE               | <b>₦10.25</b>     |
| 52-week range     | ₦4.13 - ₦10.49    |
| Market Cap. (N'm) | 315,319           |
| 1-month Avg. Vol  | 13,032,460        |
| Curr. PE          | 4.03x             |

| Quarterly EPS    | Q1   | Q2   | Q3   | Q4    |
|------------------|------|------|------|-------|
| <b>2015 A</b>    | 0.47 | 0.41 | 0.46 | 0.31  |
| <b>2016 A</b>    | 0.47 | 0.28 | 0.62 | 0.63  |
| <b>2017A(E*)</b> | 0.62 | 0.55 | 0.51 | 0.62* |

#### UBA.NL - Share Price Trend



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## United Bank for Africa. (UBA.NL)

### Stock Report

#### *Weighed by expensive funding*

- As market watchers say, late Friday is the best time to release bad earnings while early Monday is the perfect timing for an impressive result. With this in mind, UBA's early release on Monday was initially greeted with optimism, with a more critical assessment of the performance revealing concerns on a quarterly basis.
- **9M 17 earnings was spurred by higher asset yields.** Aided by higher yield on assets (+1.3pps YoY) and implied expansion (1pps YoY) in Net Interest Margin (NIM) to 5.8%, UBA posted EPS of ₦1.68 (+28% YoY) over 9M 17. Elsewhere, non-interest revenue (NIR) also remained crucial in the period, with its reported 18% YoY jump, on the back of robust increases across trading income on FI (+143% YoY) and FX (+82% YoY), providing further earnings support. In a word, knock-on effect from the duo unsurprisingly offset pressures from operating expenses (+26% YoY) and loan-loss provision (+42% YoY) to drive PBT to ₦78.3 billion—33% higher relative to 9M 16.
- **Q3 17 results analysis.** That said, quarterly breakdown revealed underlying weaknesses owing largely to higher interest expense and tamer revenues from the non-interest leg. Precisely, while interest income was up 6.3% relative to prior quarter with yield on assets trending higher to 9.5% (+41bps QoQ), interest expense rose by a sharper 13.5% QoQ to ₦32.2 billion with annualized cost of funds (WACF) tracking higher by 41bps to 4.1%. The foregoing drove a contraction (-16bps QoQ) in NIM to 8.2%.

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A parse through the details showed that cost pressures stemmed from a 3pps QoQ decline in CASA ratio to 73.4%. In our view, the bank suffered under the elevated interest rate environment even as cost of borrowings rose by 14.3% QoQ in the period.

- ***FX loss on derivative position restrains NIR growth.*** UBA booked an FX loss of ₦6.4 billion in the review quarter that stemmed from revaluation of its derivative position (notional value ~₦30 billion). We believe that the sharp unwinding of earlier gains, as derivative position neared maturity, drove the loss position. The foregoing, combined with a sizable decline in FX trading income (-32% QoQ), led to a decline in NIR (-40% QoQ). Consequently, cost-to-income ratio expanded by 10.8pps QoQ to 67.7% despite marginal increase in operating expenses (20bps QoQ).
- Elsewhere, asset quality remained intact with NPL ratio same as in prior quarter at 4.2% as loans to Power, General Commerce and O&G remained key weights on the bank's loan book. That said, given lower specific impairment (-64% QoQ) and recoveries (₦414 million), loan loss provision declined 45% QoQ to ₦3.5 billion with annualized cost of risk trending lower to 0.9% (-76bps QoQ) – coverage ratio (excl. regulatory reserve: ~100%).
- Overall, the impact of higher funding cost and decline in NIR drove EPS lower to ₦0.51 (-7% QoQ). ROAE was down 1.7pps relative to prior quarter at 15.0%.

## **Outlook**

- ***Funding cost pressures to subsist in Q4.*** Given the currently lower yield environment, relative to the last nine months, we expect some moderation in asset yields in Q4 17E (-74bps QoQ to 8.7%) and thus forecast Q4 17 interest income at ₦77.6 billion (-6% QoQ). Further down, we expect pressures from funding cost to persist into the last quarter due to expensive term funding and thus forecast WACF at 4.9% (+76bps QoQ). Consequently, NIM should print at 7.6% (-62bps QoQ).
  - ***Higher NIR and lower provisioning should buoy earnings.*** On NIR, given our expectation of near term naira stability, we see limited scope for further FX loss on the company's derivative position. This, alongside expected gains from FI and FX trading as well as net fee income, guides to NIR projections of ₦38.2 billion (58% QoQ). Furthermore, given improvement in key sectors (O&G, Power, and General commerce) on the back of higher production and crude oil prices, FG's power sector intervention and improved dollar liquidity, we forecast NPL and Cost of Risk at 4% and 1.5% respectively. In all, Q4 17E EPS should print at ₦0.58.
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- **Expected cancellation of SSIT shares elevates outlook.** On balance, adjustment for Q4 17 estimate should bring FY 2017E EPS to ₦2.26 (+14% YoY). However, we have adjusted our shares outstanding to factor in the repossession/cancellation of unvested portion of shares under the Staff Share Investment Trust scheme (SSIT) Scheme – 2.08 billion units, for which we expect completion before year-end. Consequently, FY 2017E EPS should print at ₦2.40 (+20% YoY).
- Our revised FVE of **₦10.25** translates to an **OVERWEIGHT** rating on the company. UBA trades at a P/B of 0.66x relative to peer average of 0.9x.

## Summary of Results and Forecasts - Naira (₦)

| ANNUAL                   |           |           |           |           |           |
|--------------------------|-----------|-----------|-----------|-----------|-----------|
| Income Statement (₦'000) | FY 2015A  | FY 2016A  | FY 2017F  | FY 2018F  | FY 2019F  |
| Gross earnings           | 306,273   | 369,659   | 438,555   | 436,490   | 440,679   |
| Interest Income          | 233,969   | 263,970   | 315,703   | 302,698   | 295,451   |
| Interest Expense         | (96,030)  | (98,770)  | (123,060) | (88,464)  | (72,926)  |
| Net interest income      | 137,939   | 165,200   | 192,644   | 214,235   | 222,526   |
| Non-Interest Revenue     | 72,304    | 105,689   | 122,852   | 133,791   | 145,227   |
| OPEX                     | (136,626) | (152,501) | (192,086) | (210,568) | (219,109) |
| Provisions               | (5,053)   | (27,683)  | (20,758)  | (19,464)  | (17,686)  |
| PBT                      | 68,454    | 90,642    | 102,652   | 117,994   | 130,958   |
| Tax                      | (8,800)   | (18,378)  | (20,530)  | (26,549)  | (32,739)  |
| PAT                      | 59,654    | 72,264    | 82,121    | 91,446    | 98,218    |
| Balance Sheet (₦ '000) * |           |           |           |           |           |
| <b>Assets</b>            |           |           |           |           |           |
| Cash & Short-term funds  | 655,371   | 760,930   | 527,602   | 422,082   | 443,186   |
| Net Loans                | 1,036,637 | 1,505,319 | 1,596,790 | 1,769,443 | 1,965,160 |
| Fixed Assets             | 88,825    | 93,932    | 96,089    | 101,417   | 108,086   |
| Total Assets             | 2,752,622 | 3,504,470 | 3,685,156 | 3,928,655 | 4,202,182 |
| <b>Liabilities</b>       |           |           |           |           |           |
| Deposits                 | 2,081,704 | 2,485,610 | 2,647,927 | 2,820,043 | 3,017,446 |
| Borrowings               | 215,516   | 345,905   | 366,269   | 377,258   | 388,575   |
| Total liabilities        | 2,420,001 | 3,056,401 | 3,181,298 | 3,366,967 | 3,578,380 |
| Shareholders' fund       | 332,621   | 448,069   | 503,858   | 561,688   | 623,801   |
| <b>Key Ratios</b>        |           |           |           |           |           |
| EPS                      | 1.64      | 1.99      | 2.40      | 2.67      | 2.87      |
| DPS                      | 0.80      | 0.75      | 0.72      | 1.07      | 1.15      |
| BVPS                     | 9.17      | 12.35     | 14.70     | 16.39     | 18.20     |
| P/B                      | 1.01      | 0.75      | 0.63      | 0.57      | 0.51      |
| ROE                      | 20.0%     | 18.5%     | 17.3%     | 17.2%     | 16.6%     |
| ROA                      | 2.2%      | 2.3%      | 2.3%      | 2.4%      | 2.4%      |
| Loans/Deposit            | 49.8%     | 60.6%     | 60.3%     | 62.7%     | 65.1%     |
| Cost to income           | 65.0%     | 56.3%     | 60.9%     | 60.5%     | 59.6%     |
| WACF                     | 4.0%      | 3.7%      | 4.1%      | 2.8%      | 2.2%      |
| Cost of risk             | 0.5%      | 1.8%      | 1.3%      | 1.1%      | 0.9%      |
| NPL                      | 1.7%      | 2.8%      | 4.0%      | 1.5%      | 1.0%      |

Source: ARM Research \*unless otherwise stated

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