

United Bank for Africa Plc.

First Glance: Impressive Performance Despite Opex Pressure; PBT and PAT expanded 42.86% and 29.79% y/y

This afternoon, United Bank for Africa Plc (UBA) released audited H1 2017 results, wherein gross earnings grew 34.51% y/y, driven by significant growth across income lines – interest income (+44.25%, in line with our estimate) and non-interest revenue (+16.01% and 29.77% above our estimate). Despite opex pressure (+37.35% and 10.25% above our estimate), PBT and PAT expanded 42.86% (25.21% above our estimate) and 29.79% (7.56% above our estimate) y/y respectively, with EPS growing 29.10% y/y (7.56% above our estimate of N1.15) to N1.24. Consistent with its dividend payment, UBA is proposing an interim dividend of N0.20 (same as previous year) – translating to a payout ratio of 16.15% and a dividend yield of 2.06%.

The y/y growth in NIR was driven by the 238.43% y/y surge in FX trading income (due to fx related gains and derivative transactions) and 170.57% y/y growth in fixed income securities trading, the cumulative impact of which shielded the marginal decline in fee incomes (down 1.27% y/y, and 5.53% behind our estimate) due to a steep contraction in E-banking income (45.92% y/y).

In line with industry peers, the growth in interest income, was driven by improved yields on interest earning assets (+205 bps to 12.32%) from repricing of loans due to the elevated interest rate environment; loans and advances to customers (+49.41% y/y), and investment securities – treasury bills (+52.71% y/y) and bonds (+24.20% y/y). Still reflecting the high interest rate environment, interest expense rose 23.77% y/y (in line with our estimate) driven by the elevated interest charge on borrowings (+299.01%), a development we attribute to its recently issued USD500 million at a yield of 7.875% and Fed Rates hikes impact on LIBOR linked borrowings. However, the expansion in asset yields outweighed the 38 bps y/y rise in cost of funds (to 3.75%), and as a result, net interest margin advanced 140 bps y/y to 7.30%.

The change in AMCOM levy treatment (computed as 0.5% of total assets on a preceding year basis) resulted in a one-off charge on other opex (+57.07% y/y, 15.54% above our estimate) rather than amortized as in previous year. Also, increases in personal expenses (+16.00% y/y, in line with our estimate) and depreciation expense (+17.88% y/y, in line with our estimate) further supported the 37.35% y/y (10.25% above our estimate) growth in opex. Specifically, on the performance in Q2-17, gross earnings advanced by 19.97% q/q (+32.83% y/y), driven largely by the significant growth in NIR (+87.91% q/q and +11.84% y/y), which made up for the marginal q/q growth in interest income (1.86% q/q and +49.00% y/y). Despite the 15.35% q/q (+37.69% y/y) rise in opex, PBT rose 26.02% q/q (+44.05% y/y), while PAT declined by 10.45% q/q (+27.28% y/y) due to 286.92% q/q (+84.25% y/y) expansion in tax provisions during the period.

On asset quality, UBA made an additional N8.57 billion provisions on specific credit loss impairment during the period, which by our understanding, relates to its exposure to general commerce, manufacturing, oil & gas, and power. Accordingly, loan loss provision (+104.25% q/q and 8.94% y/y) during the period surged, resulting in 129bps y/y uptick in cost of risk to 1.93%, above management's 1.5% guidance for 2017F. NPL came in ahead of 2016 level (3.90%) at 4.20% in H1-17.

HOLD

Target Price (N)*	11.25
Current Price (N)	9.71
Implied Return (%)	15.86

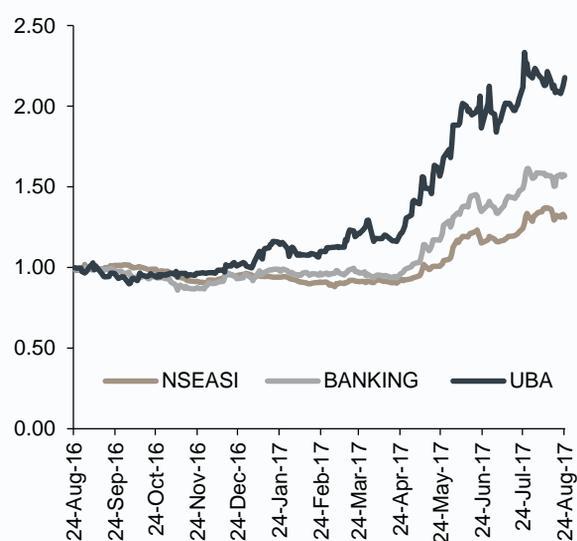
Company Data

NSE Code	UBA
Bloomberg Code	UBA:NL
Reuters Code	UBA.LG
Sector	FINANCIAL SERVICES
Market Cap. (N'bn)	340.30
Free Float (%)	93.80

Ratios	H1-2017	H1-2016	2016FY
Yield on Assets	12.3%	10.3%	11.7%
Cost of Funds	3.8%	3.4%	3.7%
Net Interest Margin	7.3%	5.9%	6.7%
Cost of Risk	1.9%	0.6%	1.8%
Cost to Income	58.6%	59.4%	62.7%
Liquidity Ratio	44.2%	45.5%	43.4%
CAR	19.7%	18.7%	19.7%
NPL/Total Loans	4.2%	2.4%	3.9%
Loan-to-Deposit Ratio	63.7%	53.5%	58.9%

*Under Review

Price movement (UBA vs. Benchmark Indices)



Source: NSE, Bloomberg, Cordros Research

We believe gross earnings will be impressive in 2017F, given the surge in FX related and derivative gains, which will be further supported by the higher yields on interest earning assets. However, the deterioration in asset quality, with cost of risk already ahead of management's guidance of 1.5%, portends a major risk to our earnings outlook. Based on our last TP of N11.25, which is at 15.58% discount to the current market price of N9.71, we have a HOLD recommendation on the stock. Our estimates are under review.

Management will be hosting a conference call for investors and analysts on Tuesday 29 August, 2017 at 15:00hrs Lagos time to discuss the H1-2017 results.

Highlight (N'Mn)	H1-2017	H1-2016	Y/Y	Cordros'		Q2-2017	Q1-2017	Q/Q	Cordros'	
				Estimate	Variance				Estimate	Variance
Gross Earnings	222,718	165,580	34.51%	200,340	11.17%	121,469	101,249	19.97%	99,091	22.58%
Interest Income	154,954	107,418	44.25%	146,576	5.72%	78,190	76,764	1.86%	69,812	12.00%
Interest Expense	(53,575)	(43,286)	23.77%	(52,553)	1.94%	(28,400)	(25,175)	12.81%	(27,378)	3.73%
Net Interest Income	101,379	64,132	58.08%	94,022	7.82%	49,790	51,589	-3.49%	42,433	17.34%
NIR	60,398	52,064	16.01%	46,541	29.77%	39,420	20,978	87.91%	25,563	54.21%
Operating Income	161,777	116,196	39.23%	140,564	15.09%	89,210	72,567	22.93%	67,997	31.20%
Provisions	(9,441)	(6,821)	38.41%	(8,650)	9.14%	(6,338)	(3,103)	104.25%	(5,547)	14.26%
OPEX	(94,804)	(69,026)	37.35%	(85,994)	10.25%	(50,781)	(44,023)	15.35%	(41,971)	20.99%
PBT	57,531	40,270	42.86%	45,949	25.21%	32,061	25,441	26.02%	20,479	56.55%
Taxation	(15,192)	(7,649)	98.61%	(6,585)	130.70%	(12,072)	(3,120)	286.92%	(3,465)	248.39%
PAT	42,339	32,621	29.79%	39,364	7.56%	19,989	22,321	-10.45%	17,014	17.48%

Disclosures.

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Cordros Capital uses the following rating system:

BUY (OVERWEIGHT) - Over the next twelve months, we expect the stock to return at least 20% above the current market price.

HOLD (NEUTRAL) - Over the next twelve months, we expect the stock to range between <-10% and <+20% from the current market price.

SELL (UNDERWEIGHT) - Over the next twelve months, we expect the stock to be more than 10% below the current market price.

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