

FBN Holdings Plc.

Earnings to Outperform in FY-2017 Despite Asset Quality Pressure

First Bank of Nigeria Holdings Plc ("FBNH") released unaudited Q3-17 results, wherein gross earnings grew marginally by 1.85% q/q and 0.40% y/y (1.77% above our estimate), while PBT and PAT rose 28.01% q/q (71.19% y/y) and 24.44% q/q (145.47% y/y), respectively. The growth in earnings was supported by (1) growth in funding income (by 7.73% q/q and 17.43% y/y, in line with our estimate), which more than subdued the 6.57% and 37.91% y/y contraction in NIR (above our estimate by 13.30%) and (2) decline in opex by 3.51% q/q (+2.27% y/y).

While the performance over 9M-17 is broadly in line with our estimate, we have now revised estimate for Q4 and FY-2017 upward to reflect the relative consistency over the first three quarters of 2017, compared with same periods in 2016. We revise gross earnings growth forecast slightly higher to 0.81% (previously -4.63%) in 2017F to N586.54 billion, on expected higher growth in interest income and a lower contraction in NIR. While we maintained our 2017F costs or risk estimate, we have lowered net loan growth estimate by 8.76%. As a result, we now forecast PBT and PAT growth of 107.87% and 214.18% (previously 51.78% and 51.74%) to N65.92 billion and N53.85 billion respectively. As a result, our 2017F EPS of N1.50 is now 107.06% higher than the previous estimate of N0.72.

We revise asset yield estimate for 2017F higher to 12.45% (previously 11.65%), on expected continued elevated yields on interest earning assets over Q4 (expanded 210 bps y/y to 12.28% in 9M-17). Overall, we look for interest income growth of 17.88% (previously 12.38%) to N477.76 billion. On NIR, we believe the growth in net insurance revenue, dividend income, and other operating income will persist for the rest of the year. However, we expect a significant contraction in foreign exchange – reflecting the limited legroom for revaluation gains in 2017 with the relative stability of the NGN –, as such, we have lowered the expected contraction in NIR to 45.41% (previously 51.63%).

While we acknowledged the moderation in interest expense in Q3, it has increased 34.45% over 9M-17, with cost of funds expanding 80 bps to 3.50%. We have revised our 2017F cost of funds estimate higher by 16 bps to 3.85% (+62 bps y/y), translating to 31.54% growth in interest expense to N132.64 billion. However, with the upward review of the high yields on interest earning assets, we believe the impact of the expansion in cost of funds will be muted, thus, we estimate net interest margin to decline 13 bps to 8.72% (previously 8.49%).

Over 9M-17, asset quality deterioration persisted, albeit with some respite as NPL ratio moderated 190 bps to 20.10% compared to H1-17. However, annualized cost of risk remains elevated, rising 20 bps to 5.60% (annualized), following additional provisioning of N35.18 billion in Q3-17, which raised total loan loss provision during the period to N97.69 billion, albeit 14.93% lower compared to N114.72 billion in 9M-16. Following the moderation in NPL and the 90.08% y/y growth in net recoveries from loans previously written off (with an additional recovery of N1.32 billion over Q3), we have revised our forecast NPL to 19.55% (previously 21.65%), but maintain our 6.65% estimate - translating to additional provisioning of N45.85 billion for Q4 and total credit loss provision of N143.47 billion for 2017F.

HOLD

Target Price (N)	7.38
Current Price (N)	6.41
Implied Return (%)	12.83

Company Data

NSE Code	FBNH
Bloomberg Code	FBNH:NL
Reuters Code	FBNH.LG
Sector	FINANCIAL SERVICES
Market Cap. (N'bn)	233.68
Free Float (%)	97.66

Ratios	9M-2017	9M-2016	2016FY
Assets Yield	12.3%	10.2%	11.7%
Cost of funds	3.5%	2.7%	2.8%
Net Interest Margin	8.8%	7.5%	8.8%
Cost of Risk	5.6%	6.9%	10.4%
Cost to Income	53.4%	48.4%	47.0%
Liquidity Ratio	47.4%	54.3%	52.7%
CAR	17.2%	15.4%	17.8%
NPL/Total Loans	20.1%	24.9%	24.4%
NPL Coverage	57.6%	43.6%	57.3%

Price movement (FBNH vs. Benchmark Indices)



Source: NSE, Bloomberg, Cordros Research

We estimate opex to rise 5.16% y/y (previously 1.53%) to N232.34 billion in 2017F – translating to a 559 bps y/y expansion in CIR to 52.60% and decline in operational leverage to 4.8x (from 5.0x in FY-16).

While noting the (1) limited room for any significant growth in FX trading and revaluation gains with the relative stability of the naira and (2) impact of the adoption of IFRS 9 from 2018F, which should drive 70 bps expansion in cost of risk, we believe FBNH's long position in fixed income securities (interest earning assets 11.53% y/y) will continue to drive growth in interest income over 2018F. On net, we revise our target price on the stock higher to N7.38 (Previous: N6.41) and roll forward our valuation to 2018F.

Our current 12-month TP implies upside potential of 12.83% from current levels; consequently, we recommend a HOLD on the stock. FBNH is currently trading at 2017F P/BVPS of 0.4x (below the peer average of 0.9x and 5-year average of 0.7x) and 2017 FP/E of 4.1x (below the peer average of 4.7x and the 5-year average of 7.2x).

Highlight (N'Mn)	Q1-2017A	Q2-2017A	H1-2017A	Q3-2017A	9M-2017A	Q4-2017F
Gross Earnings	141,048	147,573	288,621	150,307	438,928	147,609
Interest Income	114,125	118,253	232,378	123,698	356,076	121,679
Interest Expense	(33,825)	(34,468)	(68,293)	(33,438)	(101,731)	(30,908)
Net Interest Income	80,300	83,785	164,085	90,260	254,345	90,771
NIR	22,476	22,352	44,828	20,884	65,712	20,022
Operating Income	104,463	109,959	214,422	113,688	328,110	113,591
Provisions	(28,821)	(33,587)	(62,408)	(35,180)	(97,588)	(45,850)
OPEX	(55,679)	(60,901)	(116,580)	(58,765)	(175,345)	(56,994)
PBT	19,963	15,471	35,434	19,805	55,239	10,491
Taxation	(3,812)	(2,330)	(6,142)	(3,452)	(9,594)	(2,477)
PAT	16,151	13,141	29,292	16,353	45,645	8,015

Source: Company Accounts, Cordros Research

A – Actual

F – Forecast

Financial Statement (N'million).

Income Statement (N'M)	2015A	2016A	2017F	2018F	2019F	2020F	2021F
GROSS EARNINGS	505,190	581,830	586,537	594,876	624,801	659,671	693,755
Interest income	396,190	405,281	477,755	476,510	498,989	526,004	551,817
Interest expense	(131,167)	(100,839)	(132,639)	(131,699)	(144,145)	(159,590)	(168,323)
Net interest income	265,023	304,442	345,116	344,811	354,844	366,414	383,493
Non-interest income	99,417	165,476	96,585	104,907	110,839	117,295	123,710
Total Income	364,440	469,918	441,701	449,718	465,683	483,709	507,203
Total Operating Expenses	(223,606)	(220,933)	(232,339)	(239,442)	(251,898)	(259,655)	(270,802)
Net Operating Income	140,834	248,985	209,362	210,276	213,785	224,054	236,401
Loan impairment charges	(119,322)	(226,037)	(143,438)	(165,459)	(151,424)	(144,405)	(135,855)
Profit before Income tax	21,512	22,948	65,924	44,817	62,361	79,649	100,547
Income tax expense	(6,364)	(5,807)	(12,071)	(10,223)	(13,913)	(19,156)	(24,755)
Profit after Tax	15,148	17,141	53,854	34,594	48,448	60,493	75,792
Financial Position (N'M)	2015A	2016A	2017F	2018F	2019F	2020F	2021F
Cash and Cash Equivalents	715,871	690,165	603,305	670,289	779,481	856,493	968,173
Gross Loans	2,203,060	2,528,765	2,651,151	2,766,907	2,885,534	3,034,024	3,306,561
Assets pledged as collateral	105,646	197,420	126,704	159,060	193,656	231,990	252,279
Investment securities	913,779	1,050,588	1,264,115	1,267,401	1,303,809	1,310,831	1,235,504
Property and equipment	88,398	88,315	83,819	87,407	90,625	93,590	97,540
Total Assets	4,166,209	4,736,805	4,873,225	5,081,799	5,394,330	5,672,138	6,020,974
Interest Earning Assets	3,164,601	3,717,029	3,957,752	4,105,024	4,295,467	4,485,896	4,711,050
Total deposits	3,115,574	3,520,299	3,531,101	3,705,017	3,970,189	4,155,059	4,358,768
Other liabilities	168,441	235,388	259,552	229,530	269,276	283,144	299,141
Liability on insurance contracts	11,837	10,287	16,116	16,709	19,567	18,615	16,561
Borrowings	256,116	316,792	388,480	405,855	348,475	392,384	445,089
Total liabilities	3,587,389	4,154,230	4,241,053	4,397,124	4,658,753	4,898,679	5,175,454
Interest Bearing Liabilities	3,371,690	3,837,091	3,919,582	4,110,871	4,318,664	4,547,444	4,803,857
Statutory Reserve	66,647	76,226	82,309	90,582	100,186	113,080	132,070
Total equity	578,800	582,575	632,172	684,675	735,577	773,459	845,520
Key Ratios	2015A	2016A	2017F	2018F	2019F	2020F	2021F
EPS (N)	0.42	0.48	1.50	0.96	1.35	1.69	2.11
P/E (x)	8.36	8.06	4.90	7.69	14.13	5.86	4.67
BVPS (N)	16.12	16.23	17.61	19.07	20.49	21.55	23.55
P/BVPS (x)	0.22	0.24	0.42	0.39	0.93	0.46	0.42
Earnings yield	11.95%	12.40%	20.43%	13.01%	7.08%	17.08%	21.40%
Dividend Paid (N)	0.15	0.20	0.50	0.50	0.90	1.00	1.10
Dividend Yield	4.25%	5.19%	6.81%	6.75%	4.72%	10.13%	11.15%
RoAA	0.36%	0.39%	1.12%	0.70%	0.92%	1.09%	1.30%
RoAE	2.75%	2.95%	8.87%	5.25%	6.82%	8.02%	9.36%
Cost to income	61.36%	47.02%	52.60%	53.24%	54.09%	53.68%	53.39%
Operational Leverage	5.26	4.96	4.84	4.81	4.81	4.69	4.63
Yield on average earning assets	12.29%	10.73%	12.37%	11.74%	11.80%	11.90%	11.92%
Cost of interest bearing liabilities	-3.77%	-2.80%	-3.42%	-3.28%	-3.42%	-3.60%	-3.60%
Net Interest Margin	7.98%	8.70%	8.93%	8.47%	8.38%	8.28%	8.29%
Cost of Risk	5.08%	10.31%	6.65%	7.35%	6.45%	5.85%	5.05%
LTD Ratio	70.71%	71.83%	75.08%	74.68%	72.68%	73.02%	75.86%
NPL Ratio	18.10%	24.40%	19.55%	19.85%	19.25%	18.82%	17.50%

Source: Company Accounts, Cordros Research

A – Actual, F – Forecast

Disclosures.

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