

July, 2015

FBN Holdings Plc

We rate the counter NEUTRAL

Results reflect increased pressure on asset quality, rising cost of funds...

FBNH Plc reported a healthy top-line growth, with interest income accounting for 75.9% of gross earnings. A significant uptick in interest expense moderated net-interest income growth while rising impairment charges weakened profit numbers.

- Gross Earnings grew 28% yoy to N271.3billion for the first half of 2015, up from N211.9billion in HY'14. Growth was driven by a 24.8% yoy increase in interest income to N205.7billion (sustained by treasury and investment activities) and a 41.7% yoy increase in non-interest income (boosted by electronic banking fees and fund transfer & intermediation fees). QoQ, gross earnings rose 13.3% from N126.8billion in Q1'15 to N144.5billion in Q2'15.
- Interest expense was up 47.1% to N73.1billion, moderating Net Interest Income growth which came in higher by 15.2% for the six month period to N132.7billion and 22.8% increase on a QoQ basis. The uptick in interest expense was expected, given the higher interest rate environment as competition for deposits thicken amidst an increase in cash reserve requirements on public and private sector deposits. Also, interest on borrowings rose 169.6% yoy, as a result of the \$450million subordinated Tier 2 debt issued in the international markets in July 2014. Consequently, the bank's cost of funds increased to 4% (June 2014: 3.1%).
- Non-interest income which grew 41.7% yoy to N61.2billion was boosted by a 133.9% increase in foreign exchange income to N16.9billion yoy and a significant rise in gains from investment activities, though fee and commission income declined 5.4% yoy to N33.2billion.

Income Statement

	HY'15	HY'14	Change
Gross E (N'bn)	217.27	211.98	27.97%
Net Int. Inc (N'bn)	132.70	115.16	15.22%
Oper. Inc. (N'bn)	193.86	157.81	22.84%
PBT (N'bn)	52.09	48.25	7.95%
PAT (N'bn)	40.06	37.18	7.75%
EPS (Kobo)	112	114	(2.05%)

Source: NSE, Planet Capital Research

*sharesoutstanding for HY'15 inclusive of bonus

Balance Sheet

	HY'15	FY'14	Change
Cash&Equiv. (N'bn)	727.99	698.10	4.28%
Gross Loans (N'bn)	2,514.50	2,639.89	(4.75%)
Deposits (N'bn)	3,296.34	3,222.00	2.31%
Net Assets (N'bn)	561.75	522.89	7.43%
Sharesout (bn)	35.90	32.63	10.00%
Equity&Liab (N'bn)	4,418.19	4,342.67	1.74%

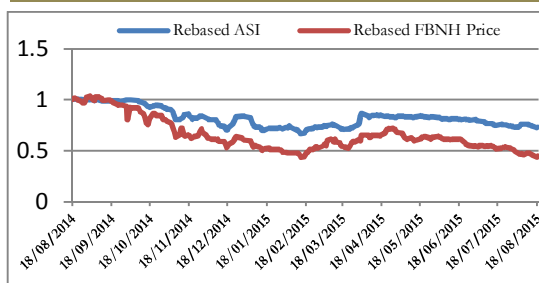
Source: NSE, Planet Capital Research

Stock Data

Ticker Symbol	FBNH:NL
Share Price	N7.22
52-week high	N14.11
52-week low	N5.77
1-month average vol. (mn)	16.01
Current P/E	6.5x
Market Cap (bn)	259.17

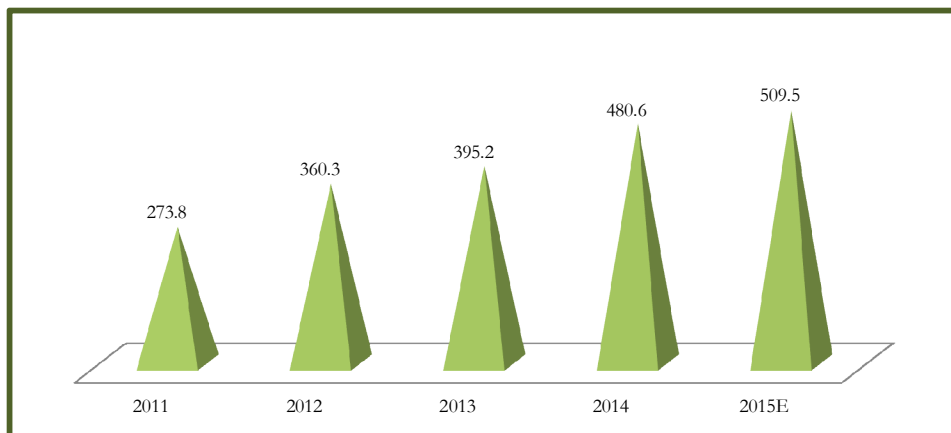
Source: Bloomberg, Planet Capital Research

Share Price Movement

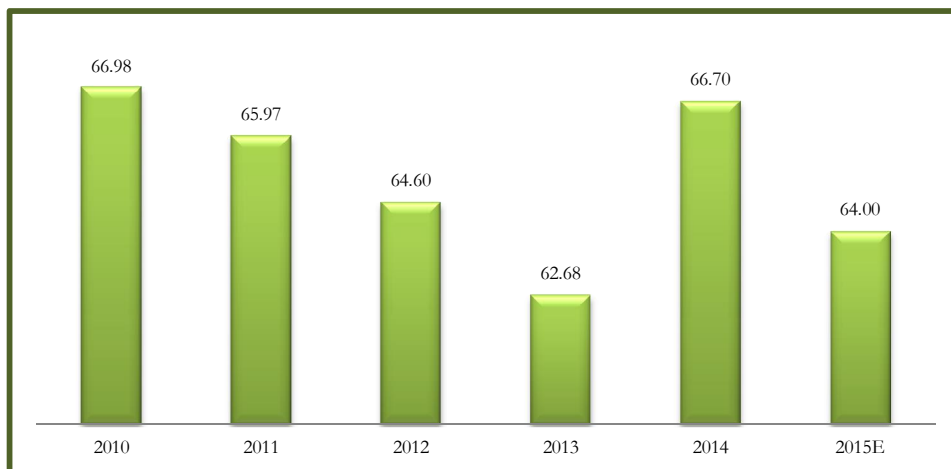


- COT, the major source of fee and commission income declined 18.9% yoy (N6.4billion), a feed through from CBN's directive to reduce COT charges. Management maintains their guidance of FY'15 non-interest income contribution at between 25%-30% of gross earnings despite tougher macro-economic environment, stating that income will be driven by increased treasury activities and e-business transactions.
- Operating expenses rose 15.3% yoy to N119.2billion and 6.22% QoQ to N61.4billion in Q2'15. The higher opex was as a result of an increase in personnel cost, regulatory cost (AMCON, NDIC) and insurance claims. Cost-to-income ratio came in at 61.5%, lower than 66.7% as at FY'14 and 65.5% for the corresponding period of last year, owing to faster growth in operating income in addition to cost improvement initiatives across the group.

Gross earnings 5-year trend (N'bn)



Cost-to-income (6yrs)



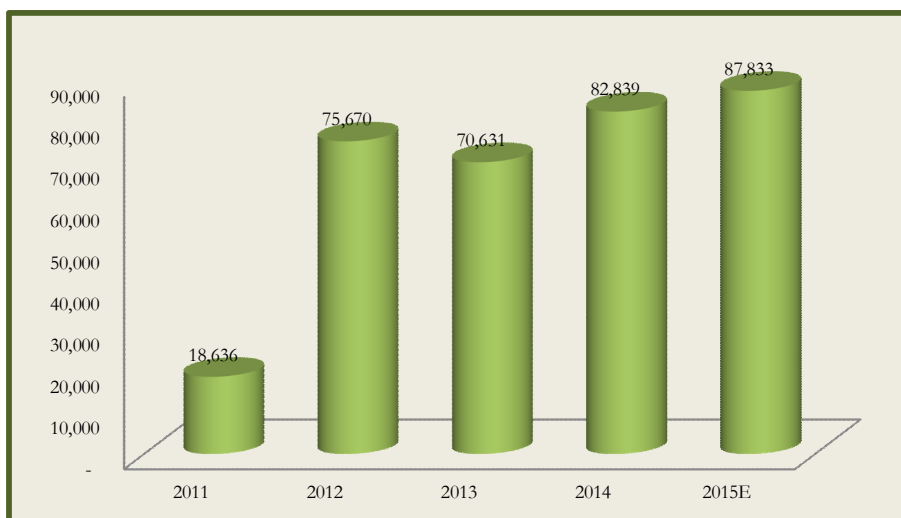
Asset Quality

- Impairment charge on credit losses grew 239.08% to N22.58billion yoy, much of which was recorded in the second quarter (up 353.4% QoQ to N18.5billion); management attributed this to difficulties in the economy such as the delay in salary payments to government workers and contractors as well as risks to general commerce owing to currency concerns, which impacted loan repayments. Also, the weaker asset quality was impacted by the bank's exposure to the Oil&Gas upstream sector. In line with the higher impairment charge, Cost-of-Risk rose to 2.1% from 0.7% in June 2014.

Aggressive provisions slow PAT growth.....

- After tax profit came in at N40billion, up 7.75% yoy though a QoQ decline of 22.8%. Consequently, PAT margin weakened to 14.8% from 15.5% yoy and 17.2% as at December 2014. Current EPS was calculated to be N1.12 (N1.14 for HY'14). Our FY'15 EPS forecast is put at N2.45; marginally down from N2.54 for FY'14 earnings.

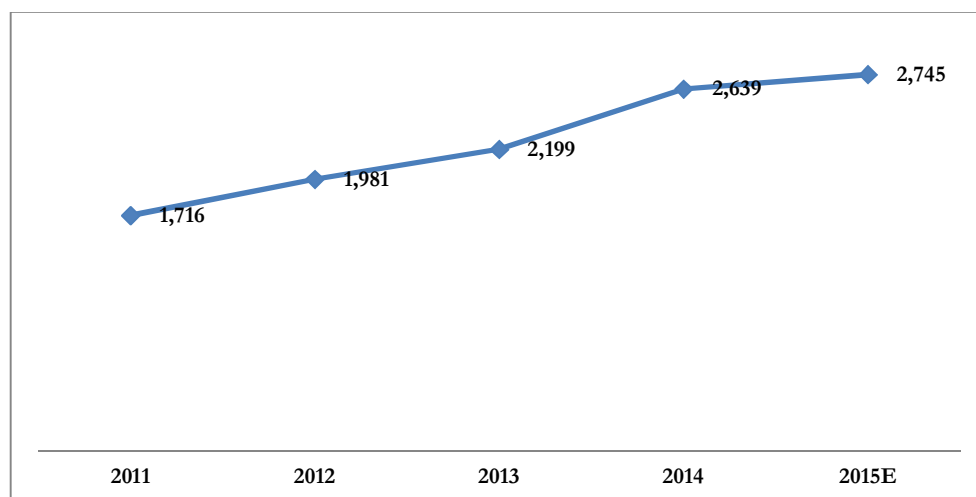
Five year PAT trend (N'bn)



Balance sheet analysis

- Total assets grew marginally by 1.7% to N4.4trillion year-to-date despite 4.8% dip in gross loans and advances to N2.5trillion from N2.6trillion as at Dec 31, 2014. Growth in total assets was driven by an increase in available-for-sale investments (up 50% ytd to N102.8billion). Management gave guidance that loan book expansion for FY'15 is unlikely to grow beyond 5% (which we have plugged into our model) and that exposure to the Oil&Gas sector (currently 35% of loan book for both upstream and downstream as at December 2014) will gradually be reduced.
- Deposits to customers and banks totalling N3.29trillion was up 2.3% ytd from N3.22trillion at the end of 2014, constituted mostly of low-cost deposits. Following the harmonization of the CRR on private and public sector deposits to 31%, the bank has seen a total of N641billion of its deposits sterilized by the CBN with no interest paid on it.
- As a result of weaker asset quality, NPL's ratio rose to 4.1 percent from 2.9 percent as at December 2014. The increase in NPL's was largely driven by activities in the Oil&Gas downstream and services sectors though the bank noted that the assets are producing but the cash flows are reducing so the tenure of the facilities are likely to be extended.
- Net assets grew by 7.43 percent ytd to N561.7billion boosted by an increase in retained earnings (up 33.3% to N144.8billion).

Gross Loans



Capital Adequacy

- The bank's CAR stood at 16.7% in December 2014 but rose to 18.8% at the end of June, boosted by retained earnings. Management gave guidance that going forward, a substantial portion of its profits will continue to be retained to boost capital, shelving any short term plans of capital raising. As a result, dividend payout is likely to remain low in 2015.

Rating downgraded to NEUTRAL

In view of the bank's exposure to the oil and gas sector and the overriding issue of lower oil prices, pressure on loan book growth bearing in mind the impact of further regulatory headwinds on the bank's operations, we downgrade the counter to NEUTRAL from BUY at an estimated fair value of N8.35 using the average of Earnings Multiples and Dividend Discount Methods of valuation. At the current price of N7.22, this gives an upside potential of 15%.

The company's shares are currently trading on a P/B and forward P/E of 0.5x (peer average 0.9x) and 2.84x respectively with year-to-date returns at -17.95%.

Summary of forecasts

	2010	2011	2012	2013	2014	2015E
Gross Earnings	232,079	273,811	360,345	395,229	480,601	509,534
Interest Income	175579	212975	287274	323621	362579	374087.3305
Interest Expense	-53912	-36784	-62082	-93506	-118725	-127484.1067
Net Interest Income	121667	176191	225192	230115	243854	246603.2238
Operating income	178062	221526	298263	296427	355072	374748.8138
Operating Expenses	119274	146145	192669	185787	236845	249026.44
Profit for the year	29177	18636	75670	70631	82839	87832.8738

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