

## Concerted Efforts Opening New Frontiers

### Double-Digit Growths Across Business Lines Spurs Top-Line Performance

**NEM Insurance Plc (NEM)** reported its best top-line performance in four years, as gross premium income for 2019 rose by 34.25% YoY to NGN19.26bn. This flowed from the impressive double-digit growth across its business lines, which was a direct result of its enhanced marketing campaign in the period. Worthy of note was the strong performance of its general accident (+51.40% YoY), marine (+41.91% YoY) and Fire (+36.61% YoY) segments respectively. Similarly, the company reported ample unearned income of NGN4.65bn (+12.07% YoY), providing further free float to the company for liquidity and Investment purposes. *Growth in gross premium income in 2020FY is expected to be weaker, largely due to the effect of the Corona Virus disease on the business environment. Nonetheless, after consideration of its NGN4.65bn unearned income from 2019FY and its renewed marketing drive, we forecast a modest 6.00% growth in premium income.*

### Underwriting Profit falls amid Soaring Underwriting Costs

The total claims paid by **NEM** in 2019 spiked by 22.66% YoY to NGN7.37bn. Hence, claims ratio rose to 31.21% (vs 23.89% in the 2018FY), signifying a weaker cost efficiency in 2019. Nevertheless, the company recovered NGN3.44bn from reinsurers, which softened the growth in net claims expenses by 46.68% to NGN3.94bn (vs. NGN2.55bn in the 2018FY). The company's higher cost profile during the period came to the fore once more, as an increase in commissions paid to brokers (+23.57% YoY) and maintenance expenses (+36.35% YoY) culminated in higher underwriting expenses (+29.34% YoY). Consequently, combined ratio spiked to 74.84%, while underwriting profit for the period fell by 5.91% to NGN4.35bn. *While the slowdown of economic activities is expected to negatively affect the insurance industry, we expect NEM, being a non-life insurer, to witness lower claims this year as the lower level of business activity will slow down the manifestation of loss. Hence, we estimate a claims ratio of 30.00% for 2020, vs 31.21% in 2019FY.*

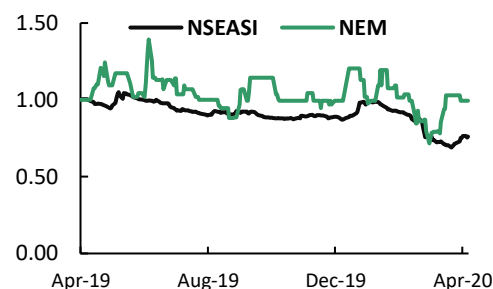
### Tax Credit Prevents Bottom Line Decline

The firm was not shielded from the depressed yield environment in 2019, as its yield on investments fell to 6.24%, from 10.55% in the 2018FY. Hence, investment Income dipped by 14.67% YoY to NGN0.94bn. Quite worryingly, costs continued to rise, as management and other operating expenses grew by 25.07% YoY to NGN3.54bn. This growth was on the back of the significant rise recorded on generator expenses (+502.25% YoY), advertising costs (+263.85% YoY) and general office charges (+72.80% YoY) respectively. Hence, Profit Before Tax dipped by 28.52% to NGN1.92bn, albeit the company recognized tax credits of NGN0.48bn, which was able to lift bottom line for the period by 17.61% to NGN2.40bn. Consequently, return on equity improved to 16.99% (vs. 16.39% in 2018FY). In the same vein, there was an improvement in solvency margin to 66.00% (vs 62.10% in the 2018FY), indicating its improved capacity towards risk underwriting. *Yields are expected to remain depressed in 2020FY which will dampen bottom line performance. Furthermore, underwriting costs are expected to increase this year, due to the impact of the Corona Virus on business activity. Hence, we project an 8.38% YoY decline in bottom-line.*

### Recommendation

Given our above expectations, we expect the company's Earnings per share in 2020 to settle lower at **NGN0.61** (-8.38% YoY) which, when combined with our Target P/E ratio of **3.11x**, gives a target price of **NGN1.90**. This translates to a downside of **13.64%** when compared with its current price of **NGN2.20**. Hence, we place a **SELL** rating on this stock.

Company	NEM
<b>Valuation</b>	
EPS	0.63
BVPS	2.72
P/E	3.11x
P/BV	0.71x
Target PE	5.13
Dec-2020 Exp. EPS	0.61
Dec 2020 Target price	1.90
Current Price	2.20
Up/Downside Potential	13.64%
<b>Ratings</b>	<b>SELL</b>
<b>Key metrics</b>	
ROAE	17.30%
ROAA	9.99%
Net margin	12.44%
Yr Hi	2.40
Yr Lo	1.48
YTD return	62.16%
Beta	0.58
Adjusted Beta	0.72
Shares outstanding	5.28bn
Market cap [NGN]	10.93bn
Financial year end	Dec
Most Recent Period (MRP)	2019FY



**Chart 1: Sensitivity Analysis**

Sensitivity Analysis of Dec-2020 Target Price to key model inputs						Min	0.46	
						Max	4.14	
		EPS						
		0.41	0.51	0.61	0.71	0.81		
Target PE	1.11x	0.46	0.57	0.68	0.79	0.90		
	2.11x	0.87	1.08	1.29	1.50	1.71		
	3.11x	1.28	1.59	1.90	2.21	2.52		
	4.11x	1.69	2.10	2.51	2.92	3.33		
	5.11x	2.10	2.61	3.12	3.63	4.14		

## Financial Highlights (NGN billion) NEM PLC 2019

<b>Profit &amp; Loss Account</b>	<b>2019FY</b>	<b>2018FY</b>	<b>y/y Growth</b>
Gross Premium Written	19.76	15.05	31.3%
Gross Premium Earned	19.26	14.35	34.2%
Re-Insurance Costs	6.64	3.65	81.8%
Net Premium Earned	12.62	10.69	18.0%
Claims Incurred	3.94	2.55	54.1%
Underwriting Expenses	5.51	4.26	29.2%
Underwriting Profit	4.35	4.62	-5.9%
Investment Income & Other income	1.14	0.93	23.3%
OPEX	3.55	2.84	25.2%
PBT	1.92	2.69	-28.5%
PAT	2.40	2.04	17.6%
<b>Balance Sheet</b>	<b>2019FY</b>	<b>2018FY</b>	<b>y/y Growth</b>
Cash and bank balances	8.10	6.70	21.0%
Financial Assets	4.69	3.60	30.0%
Trade, other Receivables & Prepayments	0.89	0.99	-10.0%
Reinsurance assets	5.53	4.81	14.9%
Investment properties	1.59	0.68	132.7%
Fixed Assets	3.03	4.16	-27.1%
Other Assets	1.86	1.49	24.8%
<b>Total Assets</b>	<b>25.68</b>	<b>22.43</b>	<b>14.50%</b>
Insurance contract liabilities	9.00	7.13	26.3%
Trade payables	0.30	0.32	-6.6%
Other payables and Provisions	1.39	1.25	11.1%
Other Liabilities	0.90	1.31	-31.4%
Total Liabilities	11.59	10.01	15.8%
Shareholders' fund	14.10	12.42	13.5%

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We estimate stock's fair value by computing a weighted average of projected prices derived from discounted cash flow and relative valuation methodologies. The choice of relative valuation methodology (ies) usually depends on the firm's peculiar business model and what in the opinion of our analyst is considered as a key driver of the stock's value from a firm specific as well as an industry perspective. However, we attach the most weight to discounted cash flow valuation methodology.

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- HOLD:** Target Price of the stock ranges between **-10 percent and 10 percent** from the current market price.
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## Movements in Price Target

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**Company Name:** Custodian Investment Plc.

Date	Price (N)	Previous Target Price(N)	New Target Price (N)	Previous Recommendation	New Recommendation
23-April-2020	2.20	3.05	1.90	BUY	SELL

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