

Achieving Less with More

Topline Growth Moderates as Low-base Effect Wanes

In 2019FY, Wema Bank Plc (**WEMABANK**) reported double-digit topline growth (32.66% YoY), which we attributed to, inter alia, the relatively low base in the corresponding period in the previous year. Q1:2020 results however reveal a significantly lower growth rate (+4.64% to NGN20.78bn) which suggests the diminished impact of a low base on growth. Be that as it may, the growth in topline was supported by sustained expansion of the banks interest earning assets (5.09% YtD to NGN559.35bn). Consequently, interest income grew by 5.07% to NGN16.86bn. Non-interest income on the other hand, recorded much slower growth (+2.85% YoY to NGN3.88bn) on the back of the regulatory reduction in fees and commission. **We maintain our expectation of a moderated growth in 2020FY on account of downside risks stemming from the COVID-19 pandemic, and the regulatory environment. In particular, the implementation of loan forbearance to vulnerable sectors (Oil & Gas, Manufacturing and Agriculture), is expected to bear on interest income.**

Cost Inefficiencies Further Constrain Profitability

WEMABANK's interest expense declined marginally by 2.92% to NGN16.89bn in Q1:2020, despite sustained growth in deposits (+11.59% YtD to NGN648.25bn). Although this is a positive development given the bank's history of elevated interest expense, we note the bank's increasingly costly funding mix, reflected by a further decline in CASA mix to 39.00% (vs.48.96% in 2019FY). Net interest margin declined to 5.41% (vs. 7.29% in Q1:2019) following a depression in asset yield to 13.63% (vs. 17.82% in Q1:2020). Loan book expansion continued to drive impairment charges which increased markedly by 59.81% YoY to NGN0.57bn. **We expect a significant rise in impairment charges in 2020FY in view the anticipated economic contraction and the impact of a depreciating Naira on impaired dollar-denominated assets.** Branch expansion activities further pressured bottom line through a 15.85% YoY growth in OPEX to NGN8.90bn. Consequently, cost-to-Income Ratio (CIR) increased to 88.74% (vs. 85.23% in Q1:2019). Hence, profit before tax (PBT) fell by 15.13% to NGN1.13bn while profit after tax (PAT) settled at NGN0.98bn (-14.58%). **Going forward, we expect a slow-down (if not a complete halt) in physical branch expansion activities due to the realities of COVID-19. This may reduce pressure on OPEX and hence PAT. However, slower top line growth and high impairment charges as a result of prevailing macroeconomic uncertainties are expected to bear on PAT growth.**

Loans-to-Deposits Ratio (LDR) Remains Below Regulatory Minimum

Although LDR increased to 52.61% in Q1:2020 (vs 49.79% in 2019FY), it remains below regulatory benchmark. The shortfall in LDR, coupled with the official CRR hike resulted in a NGN49.37bn CRR debit against the bank. This may put a strain the bank's liquidity position. Total assets however remain relatively robust at NGN794.50 (11.06% YtD). A sustained faster-paced loan growth is required to meet benchmark. The persistent decline in capital adequacy to 11.60% (vs. 13.60% in 2019FY) reflects growth in risk assets which is expected to moderate in 2020FY.

Recommendation

Wema Bank's continued asset expansion and digital banking focus is expected to bode positively for earnings in the medium to long term. However, short term outlook is fraught with cost inefficiencies, regulatory headwinds, and the economic consequences of the COVID-19 pandemic. Applying our target P/E of **5.21x** with an expected **EPS** of **0.13**, yields a December 2020 target price of **NGN0.68**. This indicates an upside potential of +17.24%. Hence, we rate the ticker a **BUY**.

| Company | WEMABANK |
|-------------------------------------|-------------|
| Valuation | |
| Trailing EPS | 0.13 |
| BVPS | 1.46 |
| P/E | 4.31x |
| P/BV | 0.38x |
| Target PE | 5.21x |
| Dec-2020 Exp. EPS | 0.13 |
| Dec 2020 Target price | 0.68 |
| Current Price | 0.58 |
| Up/Downside Potential | +17.24% |
| Rating | BUY |
| Key metrics | |
| ROE | 10.75% |
| ROA | 1.06% |
| Net margin | 4.70% |
| Leverage | 14.15x |
| Share/Share Price Statistics | |
| Yr Hi | 0.79 |
| Yr Lo | 0.44 |
| YTD return | -21.62% |
| Beta | 1.28 |
| Adjusted Beta | 1.19 |
| 52-wk average volume | 23,450,633 |
| Shares outstanding | 38.57bn |
| Market cap [NGN] | 22.73bn |
| Financial year end | December |
| Most Recent Period (MRP) | Q1:2020 |

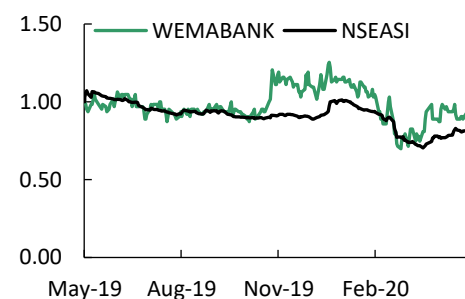


Chart 1: Sensitivity Analysis

| Sensitivity Analysis of Dec-2020 Target Price to key model inputs | | | | | | Min | 0.41 |
|---|-------|------|------|------|------|------|------|
| EPS | | | | | | Max | 1.13 |
| | | 0.11 | 0.12 | 0.13 | 0.14 | 0.15 | |
| Target PE | 3.77x | 0.41 | 0.45 | 0.49 | 0.53 | 0.57 | |
| | 4.49x | 0.49 | 0.54 | 0.58 | 0.63 | 0.67 | |
| | 5.21x | 0.57 | 0.63 | 0.68 | 0.73 | 0.78 | |
| | 6.38x | 0.70 | 0.77 | 0.83 | 0.89 | 0.96 | |
| | 7.54x | 0.83 | 0.90 | 0.98 | 1.06 | 1.13 | |

Financial Highlights (NGN billion) WEMA BANK PLC Q1:2020 Result

| <i>Profit & Loss Account</i> | Q1:2020 | Q1:2019 | y/y Growth |
|--|---------------|---------------|---------------|
| Gross Earnings | 20.78 | 19.85 | 4.64% |
| Interest Income | 16.89 | 16.08 | 5.07% |
| Interest Expense | 10.18 | 10.48 | -2.92% |
| Loan Loss Expense | 0.57 | 0.35 | 59.81% |
| Net Interest income after impairment charges | 6.15 | 5.24 | 17.35% |
| Non-Interest Income | 3.88 | 3.78 | 2.85% |
| Operating Income | 10.03 | 9.02 | 11.28% |
| OPEX | 8.90 | 7.68 | 15.85% |
| PBT | 1.13 | 1.33 | -15.13% |
| PAT | 0.98 | 1.14 | -14.58% |
| <i>Balance Sheet</i> | Q1:2020 | 2019FY | |
| Cash and short-term funds | 69.90 | 65.97 | 5.95% |
| Loans and Advances to customers | 313.80 | 289.24 | 8.49% |
| Investment securities (incl. pledged assets) | 175.65 | 177.03 | -0.78% |
| Property and Equipment | 20.84 | 20.64 | 1.00% |
| Other Assets | 214.31 | 162.48 | 31.90% |
| Total Assets | 794.50 | 715.36 | 11.06% |
| Deposits from customers | 596.44 | 577.28 | 3.32% |
| Financial Liabilities | 47.03 | 48.77 | -3.57% |
| Other Liabilities | 94.90 | 34.66 | 173.84% |
| Total Liabilities | 738.37 | 660.71 | 11.75% |
| Shareholders' fund | 56.13 | 55.16 | 1.76% |

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Movements in Price Target

Company Name: Wema Bank Plc.

| Date | Price (N) | Previous Target Price(N) | New Target Price (N) | Previous Recommendation | New Recommendation |
|-------------|-----------|--------------------------|----------------------|-------------------------|--------------------|
| 29-Apr-2020 | 0.61 | 0.73 | 0.77 | BUY | BUY |
| 20-May-2020 | 0.58 | 0.77 | 0.68 | BUY | BUY |

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|---------------|------------|
| Wema Bank Plc | |
| | |

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