

Earnings Contract Despite Improved Efficiency

Life and Non-life Segment Drive Premium Growth

Custodian Investment Plc (**CUSTODIAN**) grew gross premium income at an impressive 18.63% YoY to NGN13.89bn in Q1:2020. This performance was driven by growth across both Life and non-life insurance segments. While premiums from the non-life business — which typically accounts for c.51.00% of gross premiums — increased by 15.96% YoY to NGN6.96bn, life business premium income rose by +21.44% YoY to NGN6.92b, in the process, beating its historical contribution to total premium income ceiling of 49.00%. **For the rest of 2020FY, we expect the downside effect of COVID19 to pressure disposable income among the middle-class population. Consequently, hampering performance in the non-life segment and slowing-down GPI growth to 12.00% YoY.**

Improved Efficiency Spurs Underwriting Performance

Claims and benefit payments rose by 9.23% YoY to NGN4.23bn in Q1:2020. This was caused by lower (-102.48% YoY) recovery from reinsurers plus the impact of NGN1.88bn provision for outstanding claims and life funds. Hence, net claims and benefit incurred grew by 11.61% to NGN6.13bn. Nevertheless, loss ratio for the period declined to 73.34% (vs. 80.43% in Q1:2019), reflecting that the firm paid a lesser proportion of premium income as claims and benefit—a positive sign for the business in Q1:2020. Although underwriting expenses grew by 37.64% YoY to NGN1.37bn, combined ratio fell to 83.21% from 88.94%, outperforming the Industry-peer-average of 95.06% in the period. Thus, underwriting profit increased by 39.09% to NGN2.01bn in Q1:2020.

Bottom-line Pressured by Revaluation Loss

Interest on fixed income assets grew significantly by 31.87% to NGN2.70bn and accounted for 96.43% of total investment income earned in the quarter. This flowed from the 20.58% increase in investment asset in the period. Nonetheless, there was a decline in asset yields, from 2.80% in Q1:2019 to 2.47% in Q1:2020. Furthermore, there was a 7.59% rise in Management and other operating expenses which was underpinned by the spike in Auditors remuneration (78.17% YoY), Directors Expenses (106.90%) and Levies & Assessments (1,124.93%) respectively. This, coupled with the revaluation loss of NGN0.97bn on its quoted securities in the period, resulted in a dip in profit after tax by 3.69% YoY to NGN1.86bn, which pegged net margin for the period lower at 13.37% (vs.16.47% in the corresponding period of 2019).

Recapitalization Worries Resolved as Assets Rise

As at Q1:2020, the firm's solvency capital amounted to NGN25.05bn, firmly above the regulatory minimum of NGN18.00bn required for a composite business. This bodes well for the going concern and risk underwriting capacity of the business. Furthermore, the firm's financial asset grew by 13.36% to NGN155.20bn (vs. NGN136.19bn in Q1:2019) in Q1:2020. Also, an improvement of its cash position to NGN23.03bn (+146.02% Ytd) puts the firm in a stronger liquidity position and allows it to deploy more float to grow financial assets.

Recommendation

Earnings per share is expected to settle at NGN1.14 in 2020FY, while we estimate a trading P/E multiple of 6.88x for the firm. This yields a target price of NGN7.50, indicating an upside potential of 19.05% from its current price of NGN6.30. Therefore, we rate the ticker a **BUY**.

Company	CUSTODIAN
Valuation	
Trailing EPS	1.01
BVPS	7.92
P/E	5.69x
P/BV	0.84x
Target PE	6.88x
Dec-2020 Exp. EPS	1.14
Dec 2020 Target price	7.50
Current Price	6.30
Up/Downside Potential	+19.05%
Ratings	BUY
Key metrics	
ROAE	13.01%
ROAA	4.64%
Net margin	13.37%
Yr Hi	6.30
Yr Lo	4.95
YTD return	3.00%
Beta	0.58
Adjusted Beta	0.72
Shares outstanding	5.88bn
Market cap [NGN]	37.06bn
Financial year end	December
Most Recent Period (MRP)	Q1:2020

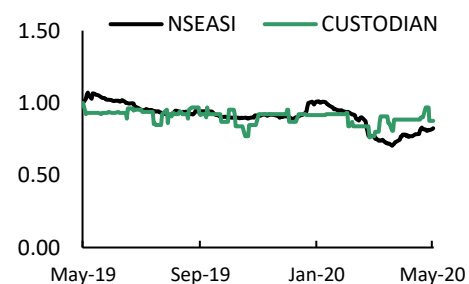


Chart 1: Sensitivity Analysis

Sensitivity Analysis of Dec-2020 Target Price to key model inputs						Min	6.22
						Max	8.90
						EPS	
		1.04	1.09	1.14	1.19	1.24	
Target PE	5.98x	6.22	6.52	6.82	7.12	7.42	
	6.28x	6.53	6.85	7.16	7.47	2.70	
	6.58x	6.84	7.17	7.50	7.83	3.85	
	6.88x	7.16	7.50	7.84	8.19	5.01	
	7.18x	7.47	7.83	8.19	8.54	8.90	

Financial Highlights (NGN'bn) CUSTODIAN INVESTMENT Q1:2020			
Profit & Loss Account	Q1:2020	Q1:2019	y/y Growth
Gross Premium Written			
Gross Premium Earned	13.89	11.71	18.63%
Re-Insurance Costs	5.53	4.88	13.36%
Net Premium Earned	8.35	6.83	22.40%
Fees and Commission Income	1.16	1.11	4.40%
Claims Incurred	6.13	5.49	11.61%
Underwriting Expenses	1.37	1.00	37.64%
Underwriting Profit	2.01	1.45	39.09%
Investment Income & Other income	1.90	2.55	-25.52%
OPEX	1.63	1.52	7.59%
PBT	2.28	2.48	-8.07%
PAT	1.86	1.93	-3.69%
Balance Sheet	Q1:2020	2019FY	y/y Growth
Cash and bank balances	23.03	9.36	146.02%
Financial Assets	86.11	81.16	6.11%
Trade, other Receivables & Prepayments	2.57	2.79	-7.77%
Reinsurance assets	10.32	9.15	12.74%
Investment properties	9.28	9.28	0.05%
Fixed Assets	4.23	4.28	-1.06%
Other Assets	2.55	2.00	27.25%
Total Assets	138.10	118.02	17.02%
Insurance contract liabilities	64.24	59.07	8.74%
Investment contract liabilities	4.73	3.99	18.77%
Trade payables	15.94	3.32	379.52%
Other payables and Provisions	2.69	3.42	-21.31%
Other Liabilities	3.90	3.48	12.08%
Total Liabilities	91.50	73.28	24.86%
Shareholders' fund	46.60	44.74	4.16%

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Movements in Price Target

Company Name: Custodian Investment Plc.

Date	Price (N)	Previous Target Price(N)	New Target Price (N)	Previous Recommendation	New Recommendation
23-March-2020	5.20	7.11	5.85	BUY	BUY
19-May-2020	6.30	5.85	7.50	BUY	BUY

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Custodian Investment Plc.	

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