

Shaped by Chance

Topline Buoyed by Volatile Income Lines

Union Bank Nigeria Plc (**UBN**)'s gross earnings inched lower (-1.03% YoY) to NGN37.95bn in Q2:2020. In the first half of the year however, gross earnings climbed 7.68% YoY to NGN81.86bn due to a relatively stronger performance in Q1:2020. Foreign exchange revaluation and trading gains were the main drivers of topline growth while fee-based income remained pressured. Growth in interest income was off the back of a significant growth (32.73% YtD to NGN367.98bn) in investment securities particularly treasury bills. The 5.64% YtD growth in loans did not translate to a growth in interest income from loans presumably due to restructuring of loans in the wake of the pandemic. Although fee-based income declined, the 41.71% YoY growth in e-business income despite the reduction in e-banking fees, inspires optimism for future growth. As at H1:2020, the bank had achieved appreciable volume and value growth across most of its electronic channels.

Sustained volume growth (particularly via agent banking) should bode positively for topline in spite of relatively thin margins. While we expect further growth in loan book, do not expect much in terms of earnings from loans in H2:2020 due to ongoing restructuring. We also do not anticipate that the growth in interest on investments recorded in H1:2020 will be replicated in H2:2020 while trading gains are expected to remain flat. Thus, we hold a modest revenue outlook for the bank in H2:2020, with possible upsides from the swift recovery of the economy and even more significant growth in transaction volumes.

Impairment Charges Bear on Weakened Margins

The gains recorded from relatively cheaper deposits in H1:2020 were eroded by higher interest expense on borrowings. The bank's interest expense in H1:2020 was pressured by a 46.34% YtD increase in debt. Net-interest margin thus contracted to 5.20% from 5.60% in H1:2019. The main pressure on bottom line however came from impairment charges which turned from a NGN4.49bn net write-back position in H1:2019 to a NGN4.24bn net write-off due largely to COVID-19 credit risks. The bank managed to keep its OPEX flat at NGN35.51bn (+0.13% YoY) as it continues to implement its Long-term Efficiency Acceleration Programme (LEAP). Cost-to-Income ratio remains elevated at 75.50% notwithstanding the decline from 76.10% in H1:2019. Profitability metrics – Return on Assets and Return on Equity declined to 1.20% and 8.50% (from 1.60% and 10.80%) respectively following the 9.23% YoY fall in Profit after Tax to NGN10.76bn. **We are bearish about bottom line outlook in 2020FY due to our modest gross earnings, although we expect a moderation in impairment charges (based on slow loan growth and improved economic conditions) and OPEX (based on the bank's LEAP).**

Liquidity and Asset Quality Adversely Impacted

The bank used up NGN54.38bn in Cash and cash equivalents during H1:2020 compared with a net addition of NGN82.88bn in H1:2019, indicating that liquidity is pressured. We attribute this to the 63.54% YtD increase in CRR to NGN484.15bn although LDR is compliant at 65.10%. Expectedly, the group's asset quality metrics- NPL and Coverage ratios- deteriorated YtD to 6.30% (vs. 5.80% in 2019FY) and 127.50% (vs. 138.10% in 2019FY) respectively owing to the pandemic. Capital adequacy however remained strong despite a 50bps decline to 19.20% (vs. 19.70% as at 2019FY).

Recommendation

Based on our earnings outlook, we project an **EPS** of **NGN0.80** and a **P/E** of **7.64x** for 2020FY. This yields a December 2020 target price of **NGN6.11** and indicates an upside potential of 24.69%. Hence, we recommend a **BUY** on the ticker.

Company	UBN
Valuation	
Trailing EPS	0.80
BVPS	8.88
P/E	6.75x
P/BV	0.61x
Target PE	7.64x
Dec-2020 Exp. EPS	0.80
Dec 2020 Target price	6.11
Current Price	4.90
Up/Downside Potential	24.69%
Rating	BUY
Key metrics	
ROE	8.50%
ROA	1.20%
Net margin	13.14%
Asset Turnover	0.09
Leverage	8.55x
Share/Share Price Statistics	
Yr Hi	NGN7.60
Yr Lo	NGN5.00
YTD return	-22.45%
Beta	0.65
Adjusted Beta	0.76
52-wk average volume	690,346
Shares outstanding	29.12bn
Market cap [NGN]	142.69bn
Financial year end	December
Most Recent Period (MRP)	H1:2020

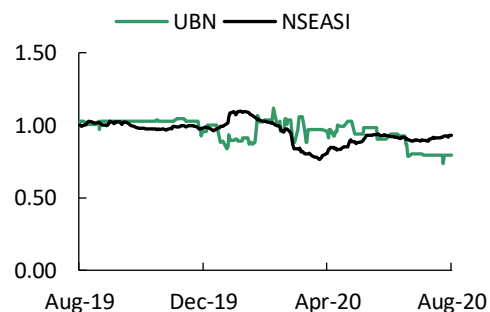


Chart 1: Sensitivity Analysis

Sensitivity Analysis of Dec-2019 Target Price to key model inputs						Min	5.73
EPS						Max	6.50
		0.76	0.78	0.80	0.82	0.84	
Target PE	7.54x	5.73	5.88	6.03	6.18	6.33	
	7.59x	5.77	5.92	6.07	6.22	6.38	
	7.64x	5.81	5.96	6.11	6.26	6.42	
	7.69x	5.84	6.00	6.15	6.31	6.46	
	7.74x	5.88	6.04	6.19	6.35	6.50	

Financial Highlights (NGN billion) UBN PLC H1:2020

Profit & Loss Account	H1:2020	H1:2019	y/y Growth
Gross Earnings	81.86	76.02	7.68%
Interest Income	57.36	54.02	6.19%
Interest Expense	29.10	30.48	-4.52%
Loan Loss Expense	4.24	-4.49	-194.47%
Net Interest income after impairment charges	24.02	28.02	-14.28%
Non-Interest Income	24.50	22.00	11.35%
Operating Income	48.52	50.02	-3.00%
OPEX	35.51	35.56	-0.13%
PBT	11.28	12.13	-7.00%
PAT	10.76	11.85	-9.23%
Balance Sheet	H1:2020	2019FY	
Cash and short-term funds	267.30	320.30	-16.55%
Loans and Advances to customers	581.66	550.61	5.64%
Investment Securities (incl. Pledged assets)	367.98	277.24	32.73%
Property and Equipment	62.34	57.97	7.54%
Other Assets	932.06	666.11	39.93%
Total Assets	2,211.34	1,872.23	18.11%
Deposits from customers	995.01	886.26	12.27%
Financial Liabilities	223.86	152.98	46.34%
Other Liabilities	733.95	580.65	26.40%
Total Liabilities	1,952.82	1,619.89	20.55%
Shareholders' fund	258.52	252.34	2.45%

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Movements in Price Target

Company Name: Union Bank of Nigeria Plc.

Date	Price (NGN)	Previous Target Price (NGN)	New Target Price (NGN)	Previous Recommendation	New Recommendation
10-Mar-2020	7.20	6.90	7.50	HOLD	HOLD
10-Sep-2020	5.40	N/A	6.11	HOLD	BUY

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Company	Disclosure
Union Bank of Nigeria Plc	

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