

Core Insurance Business Remains Solid as Bottom-line Declines

Underwriting Profit Undeterred by Rising Underwriting Expenses

NEM sustained its double-digit top-line growth streak in 2021FY as Gross Premium Income (GPW) rose by 26.50%YoY to NGN27.87bn. The performance was broad based across all its business lines with the motor segment (+28.52% YoY) and fire segment (+22.72% YoY) being the major growth drivers. Underwriting expenses surged by (+65.42%YoY) due mainly to the increase in commissions paid during the period. However, combined ratio moderated marginally to 49.38% (vs.49.98% in 2020FY). The moderation in combined ratio was due mainly to decline in the reductions in net claims expenses (-8.15% YoY) as claims recovered from reinsurer increased. Thus, underwriting profit improved (+16.98% YoY to NGN6.99bn), while underwriting margin declined to 26.35% (below the 5-year average of 28.67%) as growth in expenses outweighed topline growth. **We anticipate an underwriting profit growth of 10.41% YoY based on the firm's aggressive marketing strategy to acquire new businesses which is expected to drive top-line growth and ultimately trickle down to strong underwriting performance.**

Lower Fair Value Gains Drags Earnings

Contrary to our expectation of earnings growth in 2021FY, NEM's bottom-line declined (down 12.12% YoY to NGN4.43bn) due mainly to the decrease in fair value of financial assets to NGN358.32mn from NGN1.12bn in 2020FY given the rise in the general yield environment. Also, spike in OPEX by 30.34% to NGN4.19bn (vs. NGN3.22bn) because of the increase in employee benefit expense and impairment provisions further pressured earnings. Although investment income expanded (+12.96% YoY) driven by significant increase in dividend income, the expansion was not strong enough to support earnings growth. Thus, net margin weakened to 15.90% (vs. NGN22.89% in 2020FY). **Going forward, we do not expect a dramatic change in direction of yields witnessed in 2021, hence we do not expect a significant reduction in fair valuation of financial assets in 2022FY. Thus, we project a PAT growth of 8.52% YoY supported by expansion in investment income. However, the downside to this outlook remains the continuous rise in the firm's OPEX.**

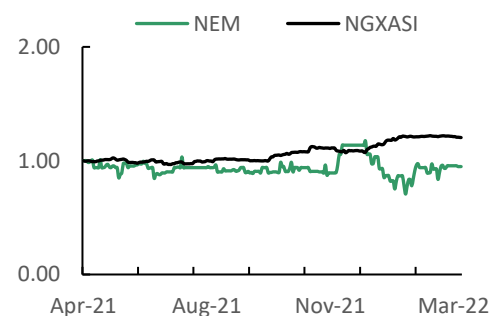
Solvency and Liquidity Remains Solid

NEM's total asset base stood at NGN38.26bn in 2021FY with earnings asset up by 22.58% to NGN23.82bn (vs. NGN19.43bn in 2020). Thus, solvency capital improved to NGN21.47bn from NGN16.33bn in 2020, with solvency margin above the regulatory benchmark (1.15x in 2021 vs 0.63x in 2020) which signifies strong underwriting capacity. Although earnings quality declined to 0.69x from 0.81x in 2020, the firm's liquidity remains strong with (short-term asset to total liabilities coverage of 1.52x in 2021FY).

Recommendations

Given the decline in profitability, we revise our 2022FY EPS to NGN0.96 and target PE of 4.96x, which implies a target price of **NGN4.76** and an upside potential of +19.94% based on the closing price on 1st April 2022. Thus, we rate the ticker a **BUY**.

Company	NEM
Valuation	
EPS	NGN0.88
BVPS	NGN4.57
P/E	4.49
P/BV	0.87
Target PE	4.96x
Dec-2022 Exp. EPS	NGN0.96
Dec 2022 Target price	4.76
Current Price	3.97
Up/Downside Potential	19.94%
Ratings	
	BUY
Key metrics	
ROE	19.35%
ROA	11.59%
Combined Ratio	49.38%
Loss Ratio	27.48%
Yr Hi	4.50
Yr Lo	3.01
YTD return	-0.12
Beta	-0.32
Adjusted Beta	0.12
Shares outstanding	5.01bn
Market cap [NGN]	19.88
Financial year end	December
Most Recent Period (MRP)	2021FY



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Chart 1: Sensitivity Analysis

Sensitivity Analysis of Dec-2022 Target Price to key model inputs						Min	4.35
						Max	5.15
						EPS	
Target PE	4.76	0.86	0.91	0.96	1.01	1.06	
	5.06	4.35	4.60	4.86	5.11	5.36	
	5.01	4.31	4.56	4.81	5.06	5.31	
	4.96	4.27	4.51	4.76	5.01	5.26	
	4.91	4.22	4.47	4.71	4.96	5.20	
	4.86	4.18	4.42	4.67	4.91	5.15	

Financial Highlights and Forecasts (NGN billion)

<i>Profit & Loss Account</i>	2020A	2021A	2022 F	2023F	2024F	2025F	2026F
Gross Premium Written	22.04	27.88	30.66	32.2	33.81	35.5	37.27
Gross Premium Income	21.68	26.55	29.2	30.66	32.19	33.8	35.49
OPEX	16.83	21	23.04	23.91	24.62	25.34	26.23
Net Premium Income	15.86	19.31	21.33	22.07	23.03	24.02	25.59
Claims Expenses (Net)	6.05	5.56	6.19	6.25	6.31	6.53	6.86
Underwriting Expenses	4.96	8.2	8.98	9.07	9.15	9.02	9.47
Total Investment Income	1.00	1.13	1.26	1.42	1.55	1.73	1.93
PBT	5.14	4.57	5.93	5.62	6.52	7.16	8.3
PAT	5.04	4.43	5.77	5.45	6.33	6.96	8.07

<i>Balance Sheet</i>	2020A	2021A	2022F	2023F	2024F	2025F	2026F
Investment Assets	19.43	23.82	19.72	21.26	34.4	37.76	49.08
Insurance Contract Liabilities	9.78	12.22	15.48	15.64	15.77	15.55	16.33
Total Assets	31.2	38.26	47.53	52.05	57.89	64.18	72.6
Total Equity	18.34	22.91	27.56	32.02	37.45	43.68	50.75
Total Liabilities	12.84	15.35	19.97	20.03	20.44	20.5	21.85

<i>Financial Ratios</i>	2020A	2021A	2022F	2023F	2024F	2025F	2026F
GPI Margin	98.40%	95.23%	95.23%	95.23%	95.23%	95.23%	95.23%
Underwriting Margin	27.14%	25.10%	25.19%	26.22%	27.51%	29.00%	30.01%
Net Margin	22.89%	15.90%	18.82%	16.93%	18.73%	19.60%	21.65%
Return on Asset	16.16%	11.59%	12.14%	10.47%	10.94%	10.84%	11.12%
Return on Equity	27.50%	19.35%	20.94%	17.03%	16.91%	15.92%	15.90%
Investment Yield	5.17%	4.76%	6.39%	6.69%	4.49%	4.59%	3.93%
Expense Ratio	22.51%	29.43%	29.27%	28.17%	27.06%	25.41%	25.41%
Loss Ratio	27.48%	19.95%	29.02%	28.33%	27.40%	27.19%	26.79%
Combined Ratio	49.98%	49.38%	58.30%	56.50%	54.46%	52.60%	52.20%

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Company Name:

Date	Price (N)	Previous Target Price(N)	New Target Price (N)	Previous Recommendation	New Recommendation
01-Apr-2022	3.97	5.38	4.76	BUY	BUY

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Company	Disclosure
NEM Insurance Plc	

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