

Deteriorating Capital Adequacy Raises Concerns

Thriving Interest Income Amps Up Gross Earnings

FBN Holdings Plc. (**FBNH**) published its long-anticipated financial scorecard for 2022FY and Q1:2023. In 2022FY, the group recorded a 6.26% YoY growth in gross earnings, surging to NGN804.95bn. The growth in gross earnings was driven by a substantial increase in interest income (+49.56% YoY), primarily fueled by the combination of a 31.48% YoY rise in customer loans and multiple interest rate hikes during the period. Despite this challenge, Yield on Assets (YoA) grew by 108bps to 6.22% in 2022FY. Conversely, non-interest income dipped significantly by 37.73% YoY due to lower trading income (-9.24% YoY) and a dip in other income (-85.01% YoY). The drastic decline in other income was unsurprising, considering the one-off NGN141.03bn Atlantic Energy Ltd loan recovery made in 2021. Contrary to the sluggish growth in 2022FY, **FBNH's** gross earnings in Q1:2023 jumped by 43.72% YoY to NGN259.51bn on the back of double-digit growth in both interest and non-interest income. Notably, the higher transaction volume and value of the group's USSD, mobile and internet banking underpinned the growth in non-funded income. **We expect the elevated interest rate environment to support growth in interest income. Also, higher electronic banking fees and income from other non-banking subsidiaries should shore up non-interest income. Equally, it is expected that the exchange rate unification should bode well for the group's topline performance considering its net long FX position. Therefore, we project a 17.73% growth in gross earnings to NGN947.64bn.**

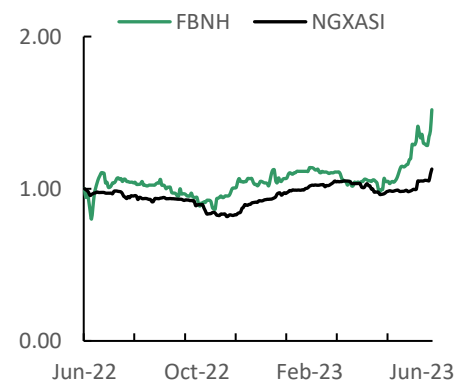
Rising Expenses, Rising Income

Despite the group's intense efforts to increase low-cost funding (which generated a 7bps increase in CASA mix to c.92%) in 2022FY, interest expense grew by 34.01% to NGN188.69bn (vs NGN140.81bn in 2021FY). This increase is associated with the high-interest rate environment. Subsequently, the cost of funds rose by 27bps, reaching 2.33%. Notwithstanding, the higher asset yield ensured that Net Interest Margin improved by 104bps to 4.86%. Additionally, **FBNH** reported an 8.89% increase in operating expenses, primarily driven by higher regulatory costs (+18.48% YoY), operating maintenance expenses (+21.68% YoY), and professional fees (+66.36% YoY). As a result, the group's cost-to-income ratio climbed to 61.65% (vs 56.37% in 2021FY). In Q1:2023, the group's operating expenses equally increased on account of the high inflationary environment. Nonetheless, the high operating income drove a 667bps improvement in the cost-to-income ratio to 60.36%. **We anticipate elevated operating expenses in the near future due to the anticipated rise in inflation throughout the remainder of the year, exacerbated by the significant impact of fuel subsidy removal on operations. However, the persistently high-interest rate environment will contribute to a higher operating income relative to the operating expenses incurred. As a result, this will have a net positive impact on the bank overall.**

Limited Exposure to Ghana's Debt Troubles

During the year, the Government of Ghana announced a suspension of all Debt Service Payments on its External Debt as it faced a debt crisis. **FBNH** held a relatively small portion of its total assets, precisely 0.40%, in Ghana debt securities, amounting to NGN8.86bn (GHS165mn). As part of a debt exchange program, **FBNH's** Ghanaian subsidiary took a haircut of 29.23%, reducing the carrying value of the debt securities to NGN6.27bn (GHS117mn). We therefore conclude that the group's exposure to the Ghana debt crisis is limited and not expected to affect its profitability significantly. As a result, the impairment charge decreased by 25.18% YoY to NGN68.62bn compared to the impairment provision of NGN91.71bn in the previous year. Notwithstanding, **FBNH** reported a lower Profit After Tax (PAT) in 2022FY (NGN136.31bn), a 9.82% YoY decline from its 2021FY figure, as the higher expenses and tax bill weighed suppressed its margins. Despite the decline in profit, the group declared a NGN0.50 final dividend, up from NGN0.35 in 2021FY. Contrary to its 2022FY

Company	FBNH
Valuation	
Trailing EPS	NGN3.79
BVPS	NGN27.53
P/E	3.77x
P/BV	0.49x
Target PE	3.83x
Dec-2023 Exp. EPS	NGN4.36
Dec 2023 Target price	NGN16.70
Current Price	NGN15.95
Up/Downside Potential	+4.73%
Ratings	HOLD
Key metrics	
ROE	14.54%
ROA	1.40%
Net margin	16.93%
Asset Turnover	0.08x
Leverage	10.62x
Yr Hi	NGN15.95
Yr Lo	NGN14.85
YTD return	+46.33%
Beta	0.47
Adjusted Beta	0.65
Proposed DPS	NGN0.50
Shares outstanding	35.90bn
Market cap [NGN]	572.53bn
Free Float	92.09%
Financial year end	December
Most Recent Period	2022FY



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performance, its Q1:2023 PAT rose substantially by 54.48% to NGN50.05bn from NGN32.40bn in 2021FY. **With inflation projected to tower in the coming months due to the subsidy removal, we expect operating expenses to keep trending upwards. Nonetheless, lower impairment charges during the year will limit the pressure on operating income. Thus, we project that PBT and PAT should increase by 14.88% and 14.97% to NGN181.39bn and NGN156.56bn in 2023FY, respectively.**

Improved Asset Quality; Worsened Capital Adequacy

FBNH witnessed remarkable growth in its deposit base, with a substantial increase to NGN7.12trn from NGN5.85trn in 2021FY. This surge in deposits translated into a larger loan book, which expanded by 31.60% to NGN3.79trn, accounting for 35.92% of the group's total asset portfolio. Despite challenging macroeconomic conditions prevailing in the country, **FBNH** took proactive measures to maintain a well-diversified loan book by mitigating concentration risks associated with critical sectors. This strategic approach moderated the group's Non-Performing Loans (NPL) ratio to 4.30% (vs. 6.10% in 2021FY). However, we remain concerned about the group's deteriorating Capital Adequacy Ratio (CAR), which is alarmingly close to the threshold of 16%. Expressly, CAR declined to 16.57% from 17.39%, as the 15.36% increase in risk-weighted assets outweighed the 9.83% increase in regulatory capital. Also, the liquidity ratio remains marginally above the threshold at 31.70%.

Recommendation

Following our PAT forecast, we revised our expected 2023FY EPS upward to NGN4.36. Combining this with a Target PE of 3.83, we arrived at a target price of **NGN16.70**. Compared to the closing price on 14th June 2023, our target price shows that the stock has an upside potential of **+4.73%**. Thus, we rate the ticker a **HOLD**.

Chart 1: Sensitivity Analysis

Sensitivity Analysis of Dec-2023 Target Price to key model inputs						Min	12.86
						Max	21.05
						EPS	
						3.86	4.11
						4.36	4.61
						4.86	
Target PE	3.33x	12.86	13.69	14.52	15.36	16.19	
	3.58x	13.82	14.72	15.61	16.51	17.40	
	3.83x	14.79	15.75	16.70	17.66	18.62	
	4.08x	15.76	16.78	17.80	18.82	19.84	
	4.33x	16.72	17.80	18.89	19.97	21.05	

Financial Highlights and Forecasts (NGN billion)

<i>Profit & Loss Account</i>	2021FY	2022FY	2023F	2024F	2025F	2026F	2027F
Gross Earnings	757.55	804.95	947.64	1,034.28	1,071.02	1,113.42	1,162.40
Interest Income	369.05	551.94	677.65	754.51	779.02	808.44	843.64
Interest Expense	140.81	188.69	221.22	225.66	231.79	237.98	227.16
Net Impairment Charges	91.71	68.62	100.19	112.47	115.17	111.06	102.35
Net Interest income after impairment charges	136.53	294.63	356.23	416.38	432.06	459.41	514.13
Non-Interest Income	427.40	388.51	253.02	270.00	279.77	292.00	304.98
Operating Income	592.81	590.25	697.81	777.71	805.23	838.05	894.11
OPEX	334.18	363.91	416.38	428.18	438.37	450.00	462.38
PBT	166.66	157.90	181.39	237.24	251.88	277.18	329.58
PAT	151.15	136.31	156.59	204.80	217.44	239.28	284.52

<i>Balance Sheet</i>	2021FY	2022FY	2023F	2024F	2025F	2026F	2027F
Cash and Balances with Central Banks	1,586.77	1,790.86	1,900.25	2,091.14	2,973.94	3,259.91	3,641.75
Loans and Advances to Banks and customers	3,897.04	5,012.12	5,187.17	5,200.08	5,117.18	5,038.74	4,964.75
Investment Securities	1,957.48	2,321.89	2,654.48	2,940.34	2,586.41	2,872.09	3,118.56
Property and Equipment	115.99	125.17	142.98	163.56	185.10	208.51	233.42
Other Assets	1,375.10	1,327.67	1,390.40	1,438.33	1,497.80	1,560.44	1,626.44
Total Assets	8,932.37	10,577.71	11,275.28	11,833.45	12,360.45	12,939.71	13,584.93
Deposits from Banks and Customers	6,947.59	8,179.34	8,806.35	9,246.67	9,814.54	10,305.26	10,820.53
Financial Liabilities	1,104.92	1,402.63	1,397.36	1,465.94	1,427.18	1,492.23	1,560.78
Other Liabilities	8,052.52	9,581.97	10,203.72	10,712.61	11,241.72	11,797.49	12,381.31
Total Liabilities	879.86	995.74	1,071.56	1,120.84	1,118.73	1,142.21	1,203.62
Shareholders' fund	1,586.77	1,790.86	1,900.25	2,091.14	2,973.94	3,259.91	3,641.75

<i>Financial Ratios</i>	2021FY	2022FY	2023F	2024F	2025F	2026F	2027F
Asset Yield	6.45%	5.14%	6.22%	6.57%	6.80%	7.09%	7.43%
Cost of Funds	2.06%	2.33%	2.40%	2.30%	2.25%	2.20%	2.00%
Net Interest Margin	3.82%	4.86%	5.67%	6.31%	6.85%	6.92%	7.29%
Cost to Income Ratio	56.37%	61.65%	59.67%	55.06%	54.44%	53.70%	51.71%
Net Margin	19.95%	16.93%	16.52%	19.80%	20.30%	21.49%	24.48%
Return on Asset	1.82%	1.40%	1.43%	1.77%	1.80%	1.89%	2.15%
Return on Equity	18.38%	14.54%	15.15%	18.68%	19.42%	21.17%	24.26%
Earnings Per Share	4.21	3.79	4.36	5.70	6.06	6.66	7.92
Asset Turnover	0.09x	0.08x	0.09x	0.09x	0.09x	0.09x	0.09x
Financial Leverage	10.15x	10.62x	10.52x	10.56x	11.05x	11.33x	11.29x

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Company Name: FBN Holdings Plc.

Date	Price (N)	Previous Target Price(N)	New Target Price (N)	Previous Recommendation	New Recommendation
15-June-2023	15.95	-	16.70	-	HOLD

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