

A Stellar Performance While Risk Build-up is Being Forestalled

Foreign Exchange Gains Push Topline by More Than Half

Fidelity Bank Plc. (FIDELITYBK) has consistently reported solid financial performance, evident in its H1:2023 results. During the period, the bank amassed gross earnings of NGN247.10bn, representing a 59.58% YoY increase from the figure reported in H1:2022. Expectedly, this significant improvement was driven by interest and non-interest income growth. Indeed, higher lending rate following multiple hikes of the benchmark lending rate and an expansion in the bank's loans to customers by one-fourth YtD served as the primary push factors for the increase in interest income. For non-interest income, a consequential surge in the bank's net foreign exchange gains (*unrealized gains from the revaluation of foreign currency-denominated assets and liabilities held in the non-trading books driven by the FX reforms*) catalyzed the expansion witnessed. In particular, the line item jumped to NGN32.16bn (vs a negative value of NGN1.51bn in H1:2022) – accounting for c.13% of the total gross earnings. Likewise, higher fees and commissions (due to increased e-banking activities) increased by half of its H1:2022 value YoY. **Our expectation for 2023FY is that higher asset yield would complement an increase in loan book and investment securities to push interest income up. Also, the bank's drive to deepen growth through digital banking would improve e-banking transaction volume and fees. We also expect the net foreign exchange gains to play a significant role in boosting its gross earnings by year-end, though; unsustainable beyond 2023FY. Therefore, we project a 41.82% YoY increase in gross earnings to NGN478.00bn in 2023FY.**

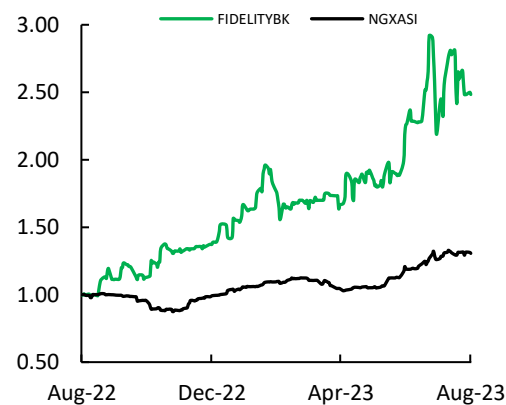
Profit After Tax Doubles Despite Higher Operating Expenses

During the review period, FIDELITYBK's net interest margin increased marginally by c. 10bps to 3.29%. This was primarily driven by the 43bps increase in asset yield despite the 4bps increase in funding cost to 2.13%. Considering the high inflationary environment, operating expenses increased by 36.10% YoY. This increase was traced to the higher AMCON levy, marketing, communication & entertainment costs (which jointly accounted for over half of the total operating expenses). Notwithstanding, the bank's cost-to-income ratio moderated to 51.99% during the period (vs 69.60% in H1:2022) due to the solid operating income growth (+82.26% YoY) recorded during the period. Thus, the bank's profit after tax increased to a record high of NGN53.30bn (+128.67% YoY). **We anticipate a continuation of the positive momentum in H2:2023. The impressive improvement in the topline performance, bolstered by increased revaluation gains and robust operating income, is well-positioned to offset the challenges posed by escalating operating expenses. Consequently, our projection points towards a Profit After Tax (PAT) of NGN92.94bn in 2023FY, reflecting a notable YoY growth of 98.92%.**

Lower But Sufficient Prudential Ratios

In H1:2023, FIDELITYBK's gross loan stock expanded by 25.03% YtD (exceeding its 15% target for 2023FY), primarily driven by higher loans to corporates (+26.04% YtD). In our view, this rather significant increase was partly triggered by the higher exchange rate used to convert the bank's foreign currency-denominated loans to Naira. One of the adverse implications of the higher risk-weighted assets is the worsening of the Capital Adequacy Ratio (CAR), which we believe informed the bank's decision to undertake a NGN6.60bn capital raising exercise through a combination of public offer and right issue. As such, we believe that upon completion of this exercise (which we expect to be in 2024), it would inadvertently result in ownership dilution and lower EPS. For the review period, although the group's Non-Performing Loans (NPL) ratio rose marginally to 3.01% (vs 2.94% in 2022FY), it is below the prudential benchmark of 5%. In addition, the NPL coverage ratio remains sufficient at 116.84% despite declining by 776bps from its 2022FY figure.

Company	FIDELITYBK
Valuation	
Trailing EPS	2.66
BVPS	11.33
P/E	3.14
P/BV	0.68
Target PE	3.19x
Dec-2023 Exp. EPS	NGN2.90
Dec 2023 Target price	NGN9.25
Current Price	NGN7.30
Up/Downside Potential	+26.77%
Ratings	BUY
Key metrics	
ROE	20.08%
ROA	1.53%
Net margin	18.02%
Asset Turnover	0.08x
Leverage	13.14x
Yr Hi	NGN8.93
Yr Lo	NGN4.36
YTD return	+67.82%
Beta	0.67
Adjusted Beta	0.78
Proposed DPS	Nil
Shares outstanding	32.01bn
Market cap [NGN]	233.69bn
Free Float	98.92%
Financial year end	December
Most Recent Period	H1:2023



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Recommendation

Following our PAT forecast, we revised our expected 2023FY EPS upward to NGN2.90 (previous estimate: NGN2.23). Combining this with a Target PE of 3.19x, we arrived at a target price (TP) of **NGN9.25**. Compared to the closing price on 16th August 2023, our estimated TP shows that the stock has an upside potential of **+26.77%**. Thus, we rate the ticker a **BUY**.

Chart 1: Sensitivity Analysis

Sensitivity Analysis of Dec-2023 Target Price to Key Model Inputs						Min	6.46
EPS						Max	12.55
		2.40	2.65	2.90	3.15	3.40	
Target PE	2.69x	6.46	7.13	7.80	8.47	9.15	
	2.94x	7.06	7.79	8.53	9.26	10.00	
	3.19x	7.66	8.46	9.25	10.05	10.85	
	3.44x	8.26	9.12	9.98	10.84	11.70	
	3.69x	8.86	9.78	10.71	11.63	12.55	

Financial Highlights and Forecasts (NGN billion)							
<i>Profit & Loss Account</i>	H1:2022	H1:2023	2023F	2024F	2025F	2026F	2027F
Gross Earnings	154.84	247.10	478.00	531.16	560.37	589.96	625.84
Interest Income	136.23	189.91	394.22	463.50	490.98	516.19	546.66
Interest Expense	60.59	82.14	189.82	221.18	228.44	236.33	248.15
Net Impairment Charges	1.99	16.78	15.71	18.36	17.84	14.85	13.49
Net Interest income after impairment charges	73.65	90.98	599.76	703.05	737.26	767.37	808.30
Non-Interest Income	13.46	54.63	83.77	67.66	69.39	73.77	79.18
Operating Income	89.10	162.39	273.25	288.65	308.93	329.84	353.09
OPEX	62.03	84.42	150.76	171.02	181.38	191.09	200.68
PBT	25.08	61.19	106.78	99.27	109.71	123.90	138.93
PAT	23.31	53.30	92.94	86.41	95.50	107.85	120.93

<i>Balance Sheet</i>	2022FY	H1:2023	2023F	2024F	2025F	2026F	2027F
Cash and Balances with Central Banks	165.12	255.24	165.12	255.24	298.72	263.01	313.57
Loans and Advances to Banks and customers	3,992.79	4,160.82	3,992.79	4,160.82	4,390.74	4,678.69	4,898.72
Investment Securities	786.14	825.67	786.14	825.67	867.79	912.25	959.12
Property and Equipment	47.21	52.92	47.21	52.92	57.78	62.65	68.38
Other Assets	118.21	114.06	118.21	114.06	121.87	130.73	139.04
Total Assets	5,109.47	5,408.72	5,109.47	5,408.72	5,736.90	6,047.34	6,378.82
Deposits from Banks and Customers	3,081.46	3,220.13	3,081.46	3,220.13	3,413.33	3,584.00	3,763.20
Financial Liabilities	554.44	472.95	554.44	472.95	501.48	526.76	553.33
Other Liabilities	1,086.10	1,274.29	1,086.10	1,274.29	1,378.76	1,486.53	1,603.49
Total Liabilities	4,722.00	4,967.37	4,722.00	4,967.37	5,293.57	5,597.29	5,920.01
Shareholders' fund	387.47	441.35	387.47	441.35	443.33	450.04	458.81

<i>Financial Ratios</i>	2021FY	2022FY	2023F	2024F	2025F	2026F	2027F
Asset Yield	8.35%	10.57%	10.65%	9.90%	9.76%	9.62%	9.62%
Cost of Funds	4.23%	4.69%	5.20%	5.30%	5.20%	5.10%	5.10%
Net Interest Margin	4.24%	5.80%	5.61%	5.25%	5.30%	5.29%	5.34%
Cost to Income Ratio	74.92%	67.14%	55.17%	59.25%	58.71%	57.93%	56.83%
Net Margin	9.21%	13.86%	19.44%	16.27%	17.04%	18.28%	19.32%
Return on Asset	0.77%	1.29%	2.04%	1.64%	1.71%	1.83%	1.95%
Return on Equity	8.27%	15.58%	26.49%	20.85%	21.59%	24.14%	26.61%
Earnings Per Share	0.51	1.03	2.90	1.91	2.11	2.39	2.67
Asset Turnover	0.08x	0.09x	0.11x	0.10x	0.10x	0.10x	0.10x
Financial Leverage	10.81x	12.12x	12.96x	12.69x	12.60x	13.19x	13.67x

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Asset allocation: The recommended weighting for equities, cash and fixed income instrument is based on a number of metrics and does not relate to a particular size change in one variable.

Movements in Price Target

Company Name: Fidelity Bank Plc.

Date	Price (N)	Previous Target Price(N)	New Target Price (N)	Previous Recommendation	New Recommendation
07-July-2023	8.12	-	8.77	-	HOLD
17-Aug-2023	7.30	8.77	9.25	HOLD	BUY

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