A Progressive Powerhouse: *Energizing Tomorrow's Horizons*

Transcorp Power Plc | March 2024

Analyst

Esther Otusanya

estherotusanya@meristemng.com

+234 811 111 4360

Initiation of Coverage Report

Executive Summary

Although generating electricity in Nigeria dates back to the late 1800s, the sector still faces significant challenges such as gas supply constraints and mechanical faults, impacting energy generation and production in the country. To address these issues, the Nigerian government has implemented various initiatives, including the privatization of the power sector and the establishment of the Transmission Company of Nigeria (TCN). A competitive analysis underscores the sector's competitiveness, high entry barriers, and reliance on thermal power. The need to address grid electricity access, meet energy demand from industrialization, urbanization, and renewable energy, as well as export potential, all portend opportunities for players in the Nigerian power sector. These opportunities can however be handicapped by prevalent threat to its growth including irregular billing system, revenue collection challenges, weak grid systems, and gas shortages.

Transcorp Power Plc (TPP), a subsidiary of Transnational Corporation Plc, stands as a leading player in Nigeria's upstream power sector, boasting an installed capacity of 972MW. The company's strategic location, commitment to self-sufficiency, and sustainability initiatives position it for continued growth. The firm’s core service offerings include capacity charges, energy delivered, and ancillary services. TPP also boasts a robust supply chain network and an experienced management team, which gives the firm an edge over other power sector players.

Our assessment of the firm’s financial performance reveals a resilient ascent marked by consistent revenue growth and strategic asset optimization. Looking ahead, we anticipate sustained revenue expansion for Transcorp Power, driven by existing capabilities and emerging opportunities. The company's strategic initiatives, international market presence, and focus on operational efficiency position it for long-term success.

We arrived at a fair value of NGN305.33 per share for Transcorp Power Plc by using a blend of various valuation models considering the company’s growth potential, risks, and overall market factors.

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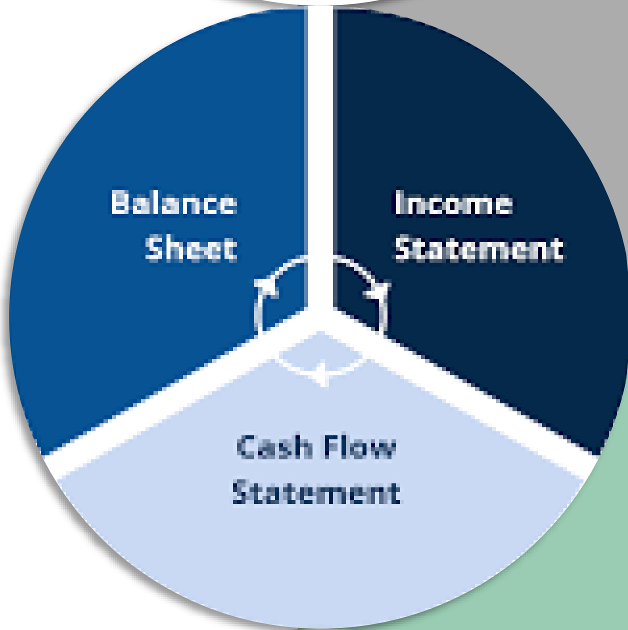
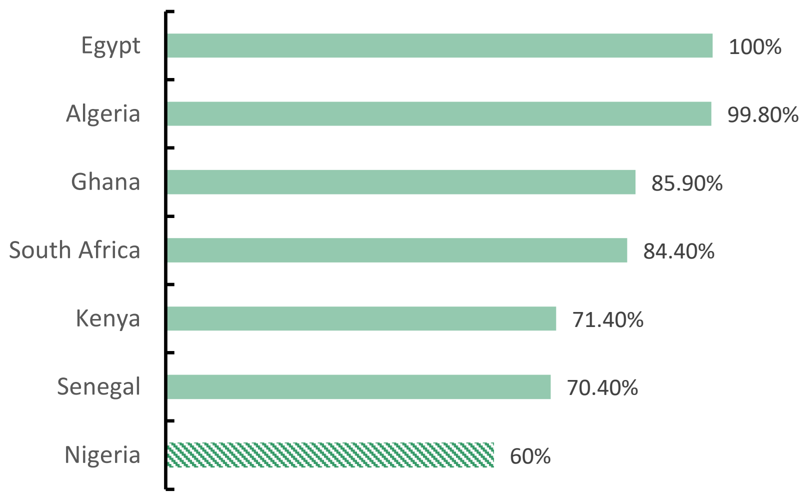


The Nigeria Power Sector

Industry Overview: A Long Way Coming

Electricity generation in Nigeria began in 1896, but a myriad of challenges has impeded growth of the power sector. As of Q3: 2023, the country's daily average electricity production stands at 3,587MV, lagging significantly behind that of many other African nations. These countries however trail Nigeria's 211mn estimated population, reflecting the significant gap in Nigeria's power sector. According to the World Bank, only 60% of the Nigerian population has access to grid electricity as of 2021.

Chart 1: Electricity Access Across African Countries (2021)



Source: World Bank, Meristem Research

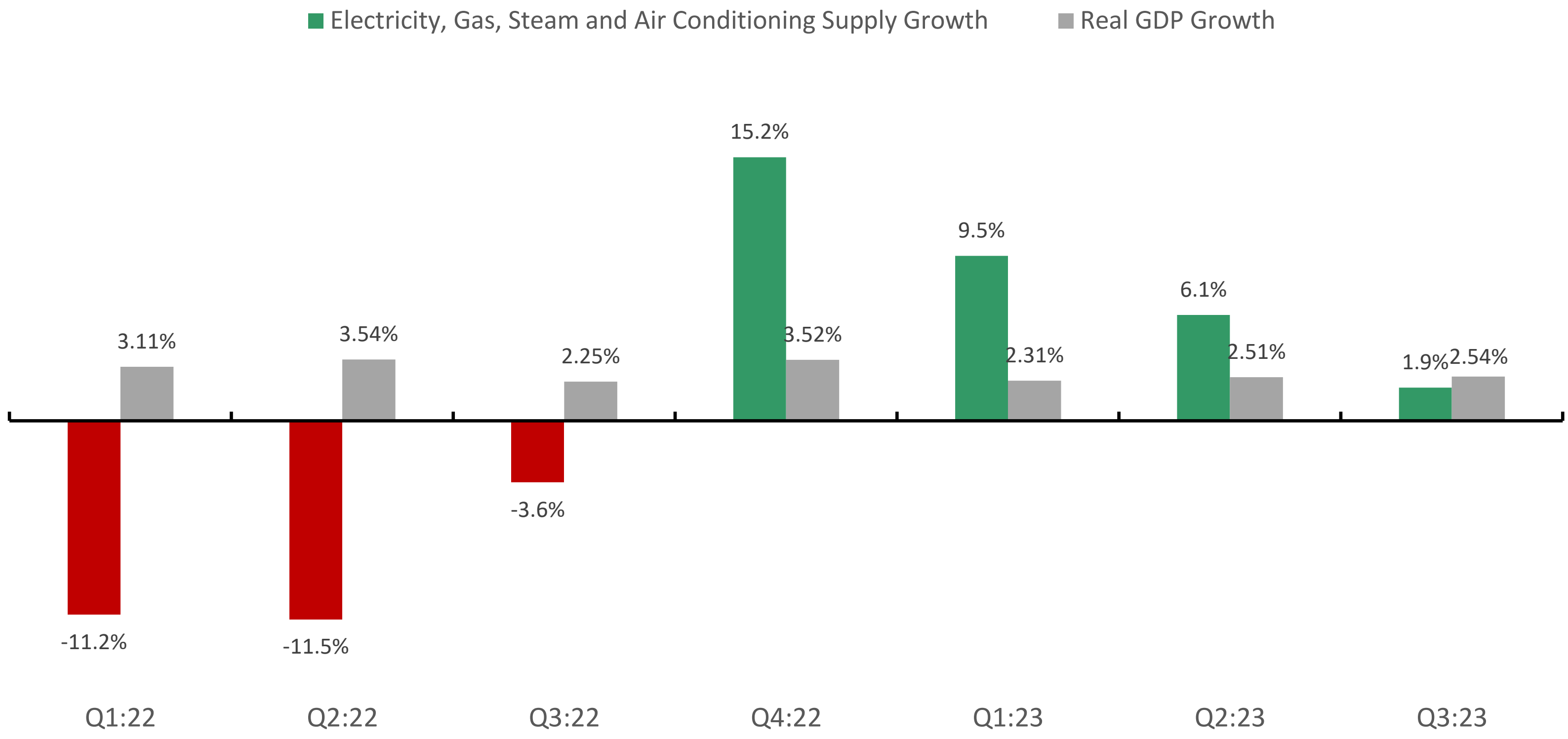
In Q3:2023, the electricity, gas, steam and air conditioning supply sector contributed 0.37% to Nigeria's real GDP, growing by 1.91% in the same period (vs 6.10% in Q2:2023). Existing challenges in the sector continues to impede growth potentials. Some of which includes weak grid system, poor revenue collection at the downstream, non-cost reflective tariff system level, insufficient transmission infrastructure etc.

In an attempt to address these challenges, the Nigerian government has undertaken various initiatives, including the privatization of the power sector through the Electric Power Sector Reform Act of 2005 and the launch of the Roadmap for Power Sector Reform in 2010. This restructuring saw the transformation of the former National Electric Power Authority (NEPA) into the Power Holding Company of Nigeria (PHCN), which was subsequently unbundled into separate generation and distribution companies, along with the establishment of the Transmission Company of Nigeria (TCN), the only transmission company in Nigeria.

To further enhance efficiency across the power value chain, the Federal government of Nigeria (FGN) privatized its 11 Distributing Companies (**DISCOs**) and 6 Generating Companies (**GENCOs**) in 2013.

According to the Quarterly report published by Nigerian Electricity Regulatory Commission (NERC) as of Q3:2023, Nigeria boasts of twenty-seven (27) grid-connected power plants, comprising of nineteen (19) gas, four (4) hydro, two (2) steam, and two (2) gas/steam-powered plants. The average available generation capacity stood at 4,211.44V while the total electricity generated in the quarter was 8,664.82GWh. The fluctuation in power generation is attributed to the reduced available generation capacity of grid-connected power plants, with persistent challenges such as gas supply constraints and mechanical faults significantly impacting energy production in gas-fired thermal plants.

Chart 2: Sector Growth and Contribution to GDP (Q1:2022 – Q3:2023)

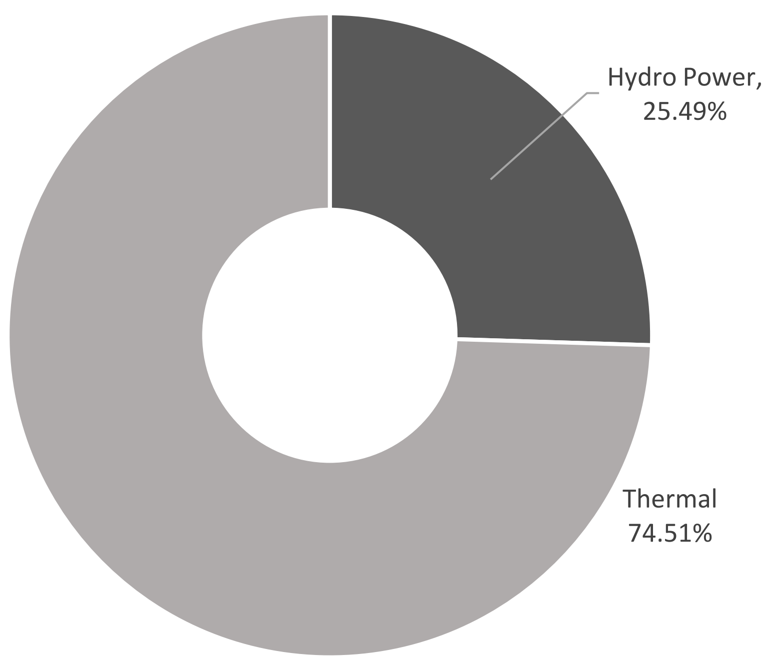


Source: National Bureau of Statistics, Meristem Research

Beyond Hydro: The Strategic Leap into Thermal Dominance

With thermal energy generating sources becoming a major electricity generation source in the country. The country's significant gas reserves is amongst the largest in the world (c. 209trn cubic feet, as per NUPRC estimates) and this is expected to aid in the growth of thermal energy sources in the medium term. This abundance of fuel resources makes thermal power generation a reliable and readily available option for meeting the country's growing electricity demand. According to the Nigerian Electricity Regulatory Commission, the thermal power generation capacity increased to 74.51% in Q3:2023, signifying the heavy reliance of the country's power sector on thermal power and evolution from hydro energy sources.

Chart 3: Power Generation Mix (as of Q3:2023)



Source: NERC, Meristem Research

Key Sector Stakeholders and Regulators

Nigerian Electricity Regulatory Commission (NERC)

The Nigerian Electricity Regulatory Commission operates as an autonomous entity tasked with the technical and economic regulation of the Nigerian Electricity Supply Industry. Its responsibilities encompass licensing operators, defining operational codes and standards, outlining customer rights and obligations, and establishing industry tariffs that reflect the costs involved.

Transmission Company of Nigeria (TCN)

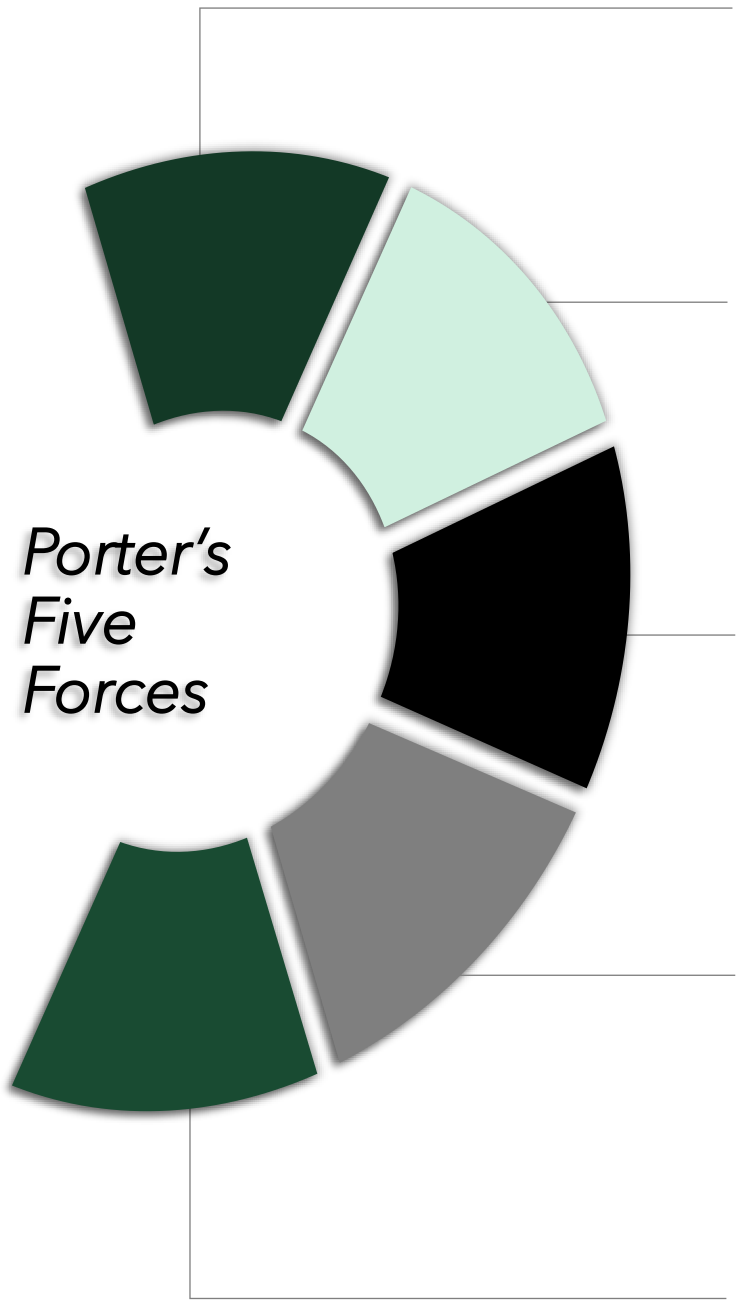
The strategic focus of the TCN involves the operation, expansion, and upgrading of transmission facilities to optimize the efficient and effective conveyance of generated electricity. Additionally, there is a concerted effort to construct a Transmission Grid with the capacity to seamlessly evacuate all generated power, and reduction of transmission losses to less than 5%.

Nigerian Bulk Electricity Trading Plc (NBET)

The Nigerian Bulk Electricity Trading (NBET) Plc. is the manager and administrator of the electricity pool in the Nigerian electricity supply industry (NESI). It was incorporated on the 29th day of July 2010 and is 100% owned by the Federal Government of Nigeria.

Competitive Analysis of the Upstream Power Sector : Porter’s Five Forces

The Porter’s five forces analysis explores the industry’s attractiveness, possible strategic positions for new entrants, regulatory levers preventing new entrants, competitiveness, and struggle for leadership in the industry. It also examines the power of suppliers and buyers. Considering the industry is at the **Growth stage** of its life cycle, the five forces are:



Rivalry - High

The Nigerian Upstream Power sector is highly competitive. The industry is dominated by a few large players.

Bargaining Power of Suppliers - Moderate

The industry heavily depends on imported equipment and technology, granting suppliers bargaining power. Also, various gas supply links are available to GENCos due to regulated prices. Nevertheless, occasional reductions in gas supply could enhance the bargaining power of suppliers.

Bargaining Power of Buyers – Moderate

The bargaining power of buyers stands at a moderate level due to the adequate, at times excessive generation of power. The grid's limitations in accommodating all generated power necessitate off-takers’ involvement to mitigate losses.

Threats of Substitute Products - Low

The threat of substitutes in the Nigerian Upstream Power sector is relatively low. There are few alternative power sources in the country, and the industry is heavily regulated.

Barriers to Entry- High

The Nigerian Upstream Power sector has a high barrier to entry due to the capital-intensive nature of the industry. Additionally, the industry is highly regulated, which further increases the barrier to entry.

Analysis of Opportunities and Threats

Digging Diamonds or Digging Dust?

Opportunities

i. **Supply Deficit:** Addressing the significant supply deficit provides a clear opportunity for the power sector to expand and improve grid access. Initiatives focused on infrastructure development, such as building new power plants and extending the reach of the electricity grid, can bridge the gap and contribute to achieving universal access to electricity. This represents a growth prospect for the entire power value chain.

ii. **Rising Demand**: The increasing energy demand resulting from industrialization, urbanization, and the penetration of renewable energy sources presents an opportunity for the power sector to meet these growing needs.

iii. **Export Potential**: Exploring and fully utilizing the potential for power exportation can significantly benefit the power sector and the country's economy. Leveraging this potential could contribute significantly to maintaining a positive trade position for the country.

iv. **Energy Transition Driving Demand**: Embracing an energy transition by harnessing abundant renewable resources can enhance the sector's overall capacity. This approach not only addresses the escalating demand for electricity but also facilitates access for more communities, promoting a sustainable and inclusive power market.

Threats

- **Shortfall in Billings:** In 2023/Q3, the total energy received by all Distribution Companies (DisCos) amounted to 7,184.45 gigawatt-hours (GWh). However, the energy billed to end-use customers stood at 5,682.11 GWh. If end-use customers are not accurately billed for the electricity consumed, it directly impacts the revenue streams of Distribution Companies (DisCos) and other stakeholders in the sector.
- **Weak National Grid System:** The country's weak national grid system hampers power sector growth by limiting accessibility, causing frequent outages, and deterring investors. Addressing these grid weaknesses is crucial for a resilient and sustainable power sector.
- **Insecurity, theft, and vandalism of transmission Infrastructure:** These pose severe threats to the growth of the power sector. These issues limit the extent of investment and utilization of existing infrastructure, leading to frequent disruptions and hindering the sector's ability to provide reliable and consistent electricity supply. The constant threat of equipment damage not only incurs high maintenance costs but also deters potential investors.
- **Shortages of Gas Supply**: As a primary fuel source for many power plants, a scarcity of natural gas limits electricity generation capacity, leading to potential power shortages and disruptions. While regulatory authorities have initiated efforts to ensure availability, such as the Gas Stabilization Fund facilitating advance payments to gas suppliers before remittance by GENCOs, there remains a need for further actions.

Company Background

Business Overview

Transcorp Power Plc or "the company," was established on September 24, 2012, and operates as a subsidiary of the conglomerate Transnational Corporation Plc (TRANSCORP). Positioned in the Power Generation sector of Nigeria, the company serves as a prominent power generation entity, delivering reliable and high-quality power to residences, communities, and businesses not only in Nigeria but also across the neighboring West-African region. On September 24, 2012, Transcorp Ughelli Power Limited was incorporated as a private limited liability company for the sole purpose of acquiring 100% shareholding in Ughelli Power Plc from the Federal Government of Nigeria. Consequently, Transcorp Power Limited (TPL) became the successor company formed from the merger of Transcorp Ughelli Power Limited and Ughelli Power Plc in November 2013 when the latter had an available capacity of 160 Mega Watts (MW). Presently, TPP's Power Plant has three major sections known as Delta II, Delta III, and Delta IV. Each "Delta" is equipped with gas turbines (GTs) of varying capacities. Notably, the plant boasts eighteen gas turbines, consisting of twelve Hitachi H25 gas turbines with a capacity of 23.8MW each and six Frame 9E General Electric (GE) gas turbines with a capacity of 105MW each. The collective installed capacity for the company reached 972 MW as of December 2023, which accounts for approximately 7% of Nigeria's installed grid capacity.

Key Milestones in TPP's Journey

2012
- Transcorp Ughelli Power Ltd (TUPL) was the preferred bidder for Ughelli Power Plc (UPP)

2013
- Took control of the power plant on the 1st of November 2013.
- Doubled capacity within 6 weeks of takeover from 160MV to 324MV

2015
- TPL was formed from the merger of TUPL and UPP

2017
- Plant capacity increased from 160MV to 701MV
- Refurbished 115MV gas turbine (GT 15) was commissioned.

2018
- Joined the West African Power Pool

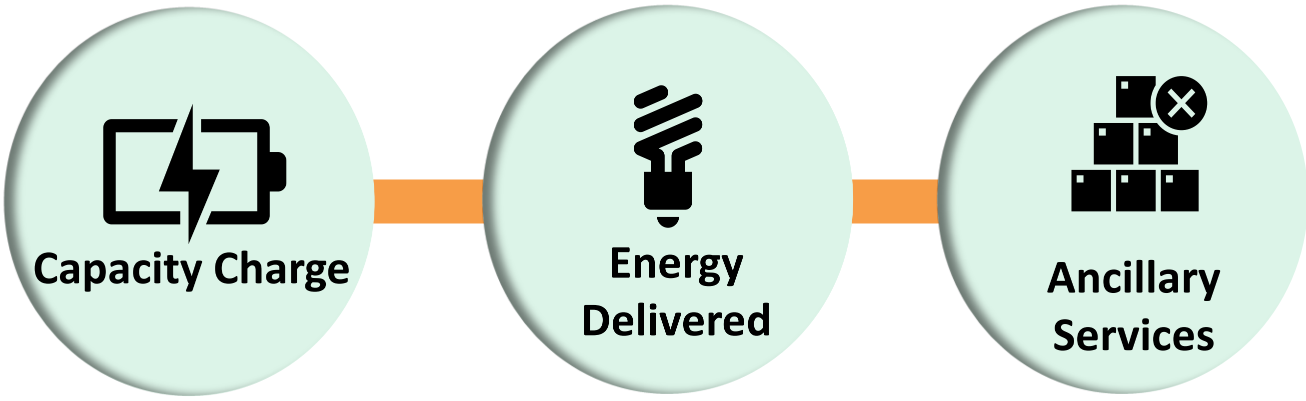
2020
- Bilateral contracts to export power to Benin republic was signed

2021/2022
- Became the first private GenCo to be awarded ISO IMS and QMS.

2023/2024
- Received post privatization discharge certificate
- Fully repaid FX denominated acquisition loan

Source: Company Financials, Meristem Research

Service Offerings: How is Revenue Generated?



From its contracts with customers, the company makes revenue from three main segments.

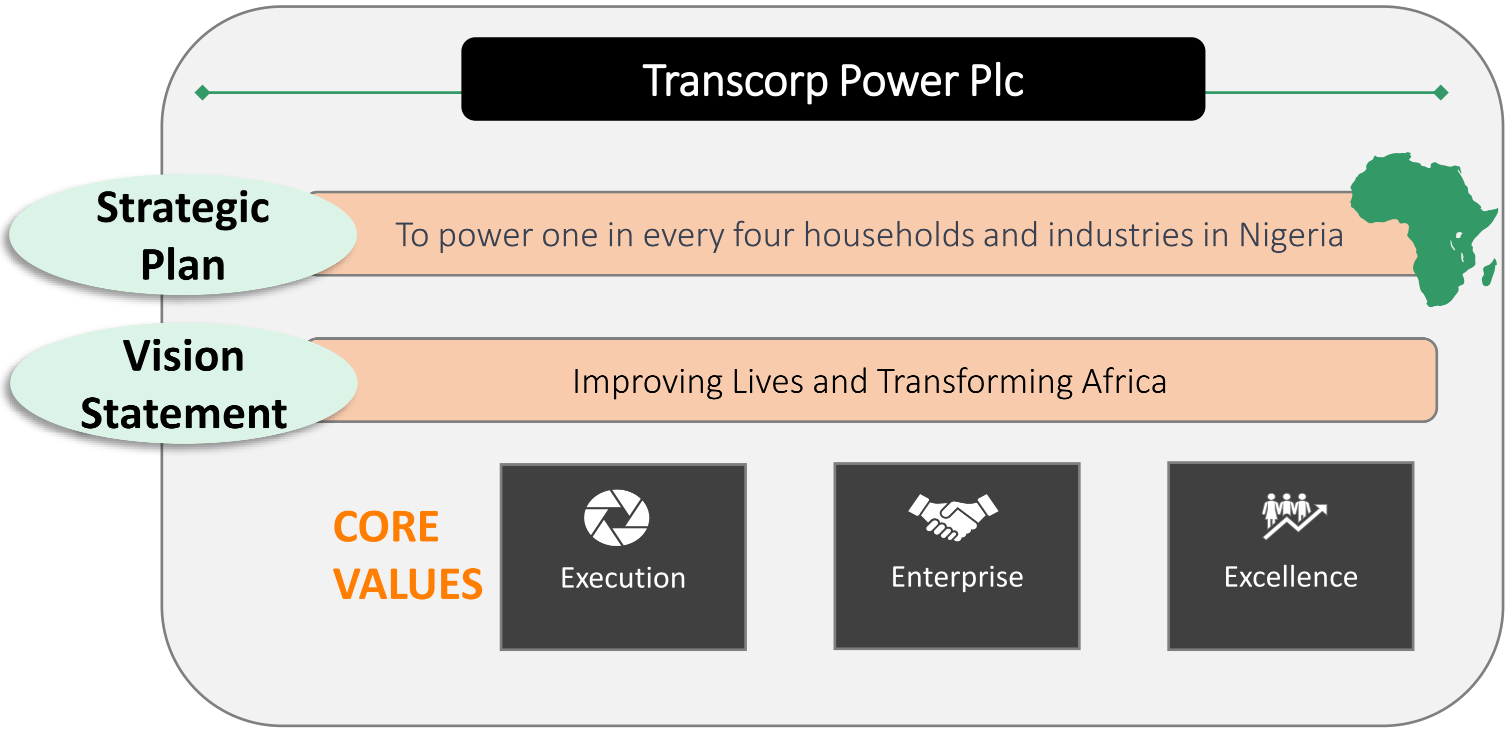
i. **Capacity Charge:** Capacity charge refers to the payment made to GENCOs based on the installed or contracted capacity of their power plants. It is a fixed fee that compensates the GENCOs for maintaining their power generation infrastructure and making it available for producing electricity.

ii. **Energy Delivered:** This refers to the actual amount of electricity supplied to consumers. Unlike capacity charges, energy charges are variable and depend on the quantity of electricity consumed.

iii. **Ancillary Services:** Ancillary services include earnings from Blackstart operations and frequency control services provided.

Vision & Core Values

Driven by a visionary commitment to improving lives and transforming Africa, the company steadfastly pursues its strategic long-term objective: to power one in every four households and industries in Nigeria. Guiding its journey toward this ambitious goal are the core values of Execution, Enterprise, and Excellence. These principles form the bedrock of the operations, underscoring the unwavering dedication to delivering tangible impact and sustainable solutions to the powering of the country.



Business Strategy: Tactical Advantages and Sustainable Initiatives

Strategically located in Ughelli, Delta State, the company's plant spans 150 hectares of land, a choice location due to its close proximity to gas input suppliers. The onsite TCN-operated evacuation infrastructure features two inter-bus transformers that adeptly manage power strength, mitigating stranded power scenarios, and seamlessly transitioning between 330KV and 132KV power levels based on grid requirements.

Having fostered a culture of loyalty and dedication among its human capital resources, a substantial portion of its workforce boasts over a decade of service to the company, translating into heightened productivity and enhanced operational efficiency.

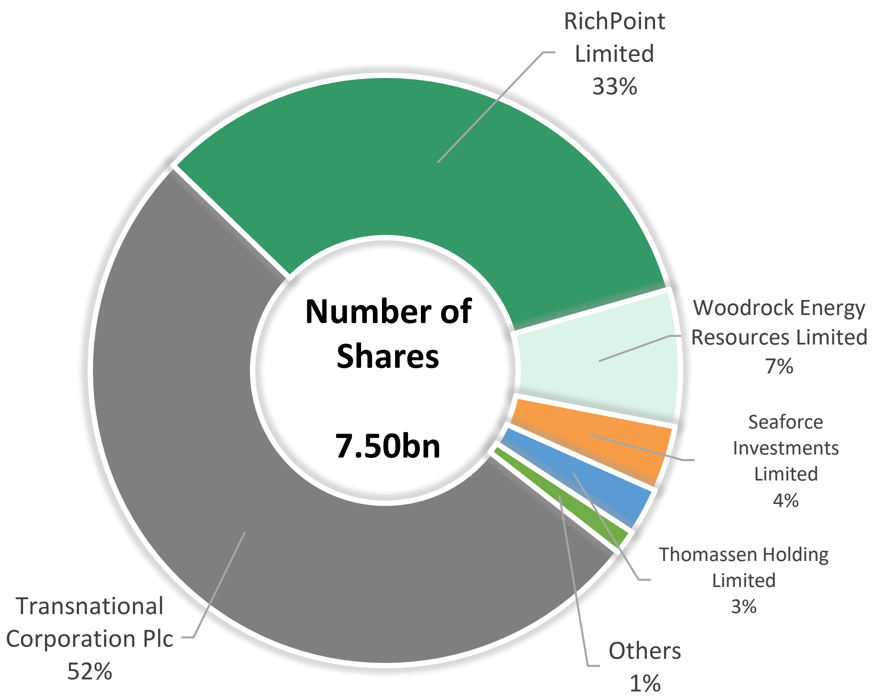
Additionally, in a shift towards self-sufficiency and operational efficiency, the company has phased out a significant portion of its outsourced repair and maintenance operations, opting for in-house repairs. This proactive initiative streamlines operational processes, reduces resolution time, and ensures greater control over infrastructure upkeep. Moreover, the company's inventory management system, the Spare Assets Portfolio Management System, facilitates swift resolutions to mechanical disruptions by housing essential equipment parts for plant infrastructure.

Looking forward, the company is committed to sustainability, with plans to harness steam generated by the plant and convert it into energy, thereby aligning with ESG standards and enhancing environmental compliance.

Shareholding Structure

As of December 31, 2023, the company's register of members reveals a total of 7,500,000,000 outstanding shares. A significant majority of these shares (51.57%) is held by the parent company, Transnational Corporation Plc (TRANSCORP), amounting to 3.87bn shares. RichPoint Limited is the second highest shareholder with 33.27% holding. Further down the line, Woodrock Energy Resources Limited, Seaforce Investments Limited and Thomassen Holding Limited have 7.46%, 3.60%, and 2.57% of the total shareholding, respectively. The residual percentage of 0.20% is distributed among 7 shareholders with less than 1% each of the total shareholding.

Chart 4: Shareholding Structure

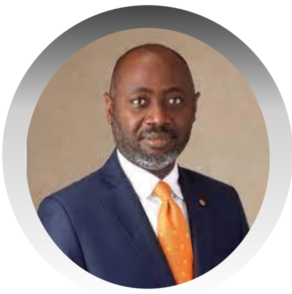


Source: Company Financials, Meristem Research

Corporate Governance Structure

Board of Directors

Emmanuel N. Nnorom
Chairman



Peter Ikenga
Managing Director/CEO

Owen Omogiafo
Non-Executive Director

Adim Jibunoh
Non-Executive Director

Peter Hertog
Non-Executive Director

Risqua Mohammed
Non-Executive Director

Prof. Sylvester O.Monye
Independent Non-Executive Director

Vincent Ozoude
Non-Executive Director

Management Team

Peter Ikenga
Managing Director/CEO

Oluwaseun Fadare
Chief Technical Officer

Evans Okpogoro
Chief Financial Officer

Sade Fagbola
Head, Supply Chain Mgt

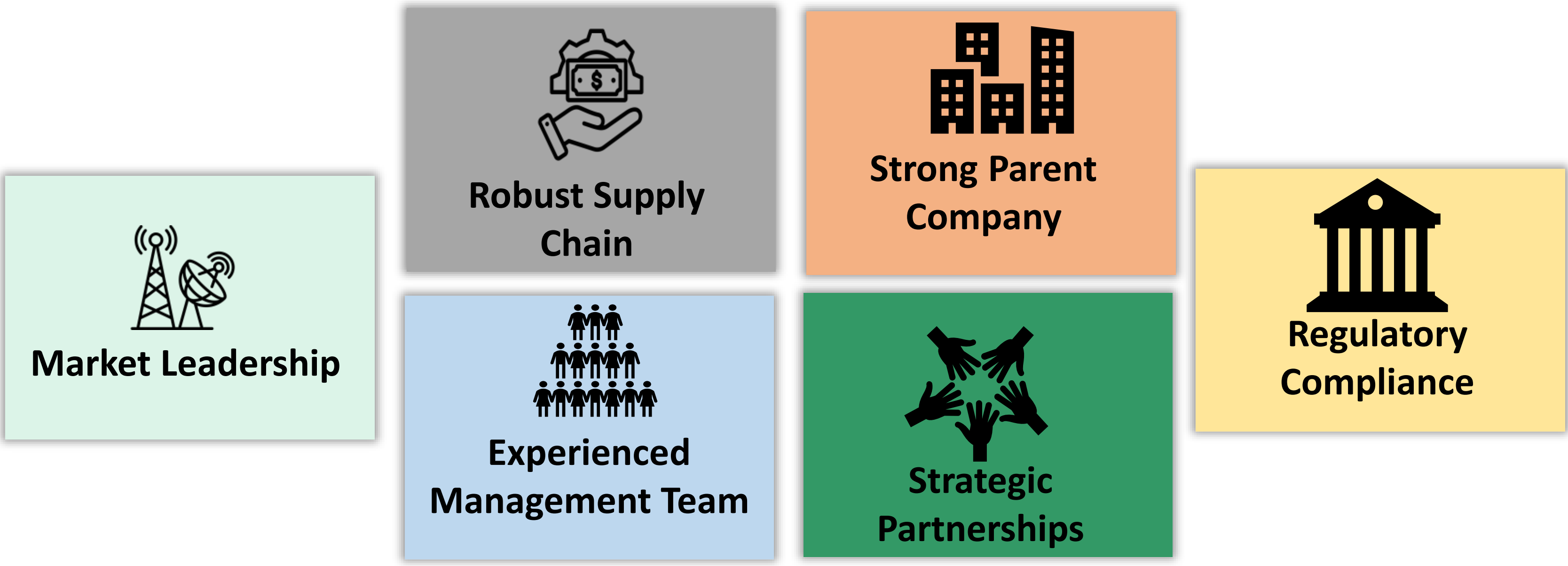
Osemonahu Ikhisemon - Oje
Head, Human Resources

Oluwafemi Sogunle
Head, Internal Audit

Joseph Ijalaye
Head, IT

Strengths and Weaknesses Analysis

Strengths – The Boosts to Race Faster



i. Market Leadership: With an installed capacity of 972MV, an available capacity of 536MV (as of Q3:2023) and a utilization rate of 70.48% with plans to enhance utilization further, the company is a prominent market leader. This positioning provides a significant advantage, allowing the company to seize and explore opportunities within the Nigerian power sector.

ii. Robust Supply Chain: The company has established a resilient supply chain, particularly in securing necessary gas inputs for sustained plant production. A noteworthy aspect is the strong supply agreement with NEPL/NDW JV OML 34, which accounts for over 80% of the plant's gas requirement. The company gets a direct gas supply from the JV through Ughelli East gas plant which eliminates transportation costs. Additional gas suppliers include Seplat, NDWestern, NEPL (formerly NPDC) and Chevron.

iii. Experienced Management Team: A key strength lies in the company's seasoned management team, boasting a collective expertise of over 250 years in technical and operational domains. This wealth of experience aligns seamlessly with the company's vision and strategic plans.

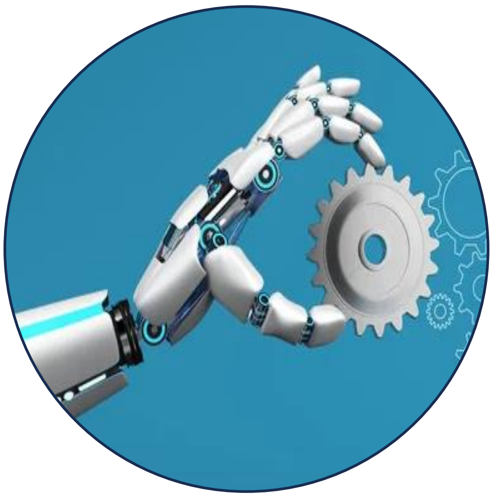
iv. Strong Parent Company Presence: The affiliation with its strong parent company - Transnational Corporation Plc, whose presence exceeds beyond the power generation sector into distribution activities, further solidifies the overall market standing.

v. Strategic Partnerships and Collaborations: The company has cultivated strategic relationships across the power sector value chain, fostering collaborations with key stakeholders. Examples include partnerships with the Transmission Company of Nigeria and bilateral agreements with Discos that have high collection rates at consumer level.

vi. Regulatory Recognition: The company became the first private power generation entity to fully meet all privatization obligations set by regulatory authorities. Consequently, **TPP** received a discharge certificate from the Federal Government of Nigeria, signalling the successful completion of its privatization commitments and exempting it from post-privatization monitoring. This reflects the company's commitment to regulatory compliance, showcasing its dedication to meeting industry standards and best practices.

vii. International Market Presence: The company's ability to supply power outside Nigeria demonstrates its strategic approach to optimizing the use of stranded power. This not only contributes to addressing energy losses but also facilitates foreign exchange inflow for the company which is instrumental in meeting dollar denominated obligations effectively.

Weakness – The Lurking Drag



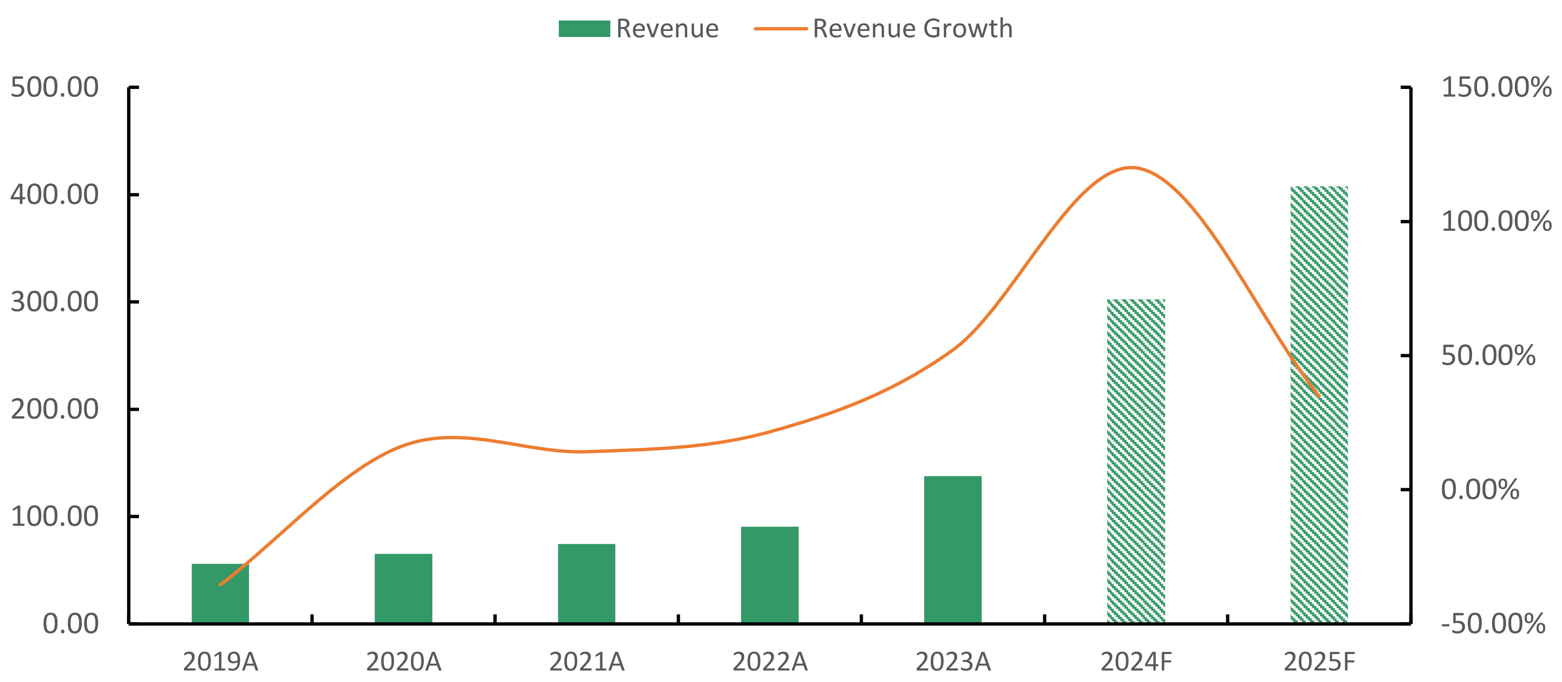
- **Manual Operation:** Manual operation of the plant remains prevalent. With evolving technology, there is a compelling need for the plant to embrace more technological innovations and automations. This shift can enhance operational efficiency and minimize the risks associated with human errors and mechanical disruptions. Despite the potential capital intensity involved in this transition, the company has the opportunity to transform its current weakness into a strength, gaining a more pronounced competitive advantage in the process.

Financial Statement Analysis

Overcoming Hurdles: A Resilient Ascent

Transcorp Power Plc (**TPP**) revenue grew at a CAGR of 32.65% from year 2019 to 2023. Throughout the years under review, the company's topline performance has consistently demonstrated annual growth, except for 2019 where revenue declined by 35.51% YoY. This decline was primarily owed to gas shortages, mandated reduction in generation from the National Control Center and revenue exposures from delayed payment of receivables during the period. In the most recent financial year-end, 2023, the company sustained its double-digit revenue expansion for the third consecutive year by 52.05%, reaching NGN 137.38bn, as compared to NGN 90.35bn in 2022FY. This impressive growth can be attributed to the upswing in capital charge(+24.68% YoY) and energy delivered (+19.92% YoY) which reflects the improvement in the company's operational activities. Additionally, the uptick was driven by reduction in both technical and commercial losses of energy, reliable gas supply and a continuous extension of the asset life of its turbines which increased production efficiency and kept the capacity utilization level elevated.

Chart 5: Revenue (NGN'bn) LHS and Revenue Growth RHS

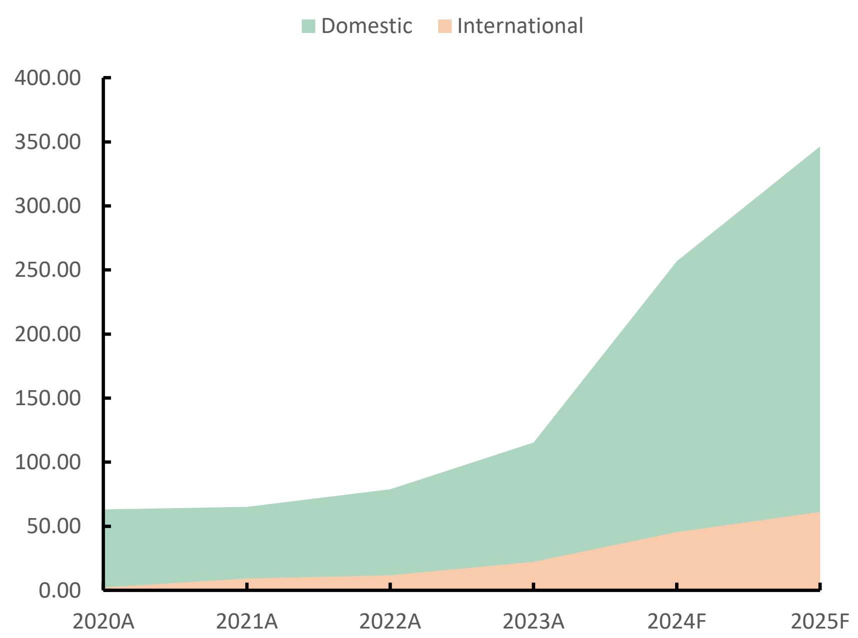


Source: *Company's Financials, Meristem Research*

Beyond Nigeria: Charting New Markets

Moreover, in 2020, Transcorp Power Plc initiated power exports beyond the borders of Nigeria, extending its reach to neighboring West African states, notably the Benin Republic. Witnessing a substantial increase, international exports accounted for 3.26% of total revenue in 2020 and surged significantly to comprise 16.14% of the company's revenue as of 2023FY. This deliberate foray into international markets has empowered the company to tap into diverse revenue streams and capitalize on opportunities beyond the confines of the domestic market. Additionally, the company has successfully mitigated power losses by exporting stranded power that could not be accommodated by the Nigerian grid system.

Chart 6: **Revenue By Region (2020A – 2024F)**



Source: *Company's Financials, Meristem Research*

Looking forward, we anticipate a sustained expansion in revenue, driven by a combination of existing capabilities and emerging opportunities that the company is well-positioned to capitalize on. The recent completion of the overhaul of one of its major turbines, which had been out of operation since 2019, is expected to significantly enhance the company's capacity utilization and power generation in the near term. Furthermore, the company's bilateral agreements with downstream distribution companies, especially those with high collection rates from users (Discos), will facilitate direct interactions without intermediaries. This is poised to result in shorter payment periods and increased transparency, thereby mitigating power losses and improving overall accountability. In summary, we reaffirm our expectation that the company is strategically positioned to maintain its robust revenue performance. Hence, we project a 2024FY revenue of NGN302.15bn, (+119.94% YoY higher than 2023's NGN137.38bn)

Gross Margins Remain Strong

Over the years under review, the company's cost of sales has increased at a slower pace than revenue. Consequently, gross margin has remained strong averaging 46.19% during the 2019 to 2023. In 2023FY, gross profit grew by 63.43% YoY to NGN 74.61bn (vs NGN45.66bn in 2022FY).

Operational Efficiency Sustains Profitability

Transcorp Power Plc showcased a trend of relatively stable operating expenses with marginal increases from 2018 to 2020. However, in 2021 to 2023, amid an inflationary environment, administrative expenses surged by 63.34% 25.44% YoY, and 47.67% respectively. The main drivers behind this surge were the upward revision of management fees and other operating expenses during the period. Despite this, in 2023FY, EBITDA expanded impressively by 67.61% YoY to NGN65.94bn, compared to NGN39.34bn in 2021FY. Similarly, EBITDA margin climbed by 448bps to its highest on record at 48.00% (vs 43.54% in 2022FY and its five-year average of 35.69%).

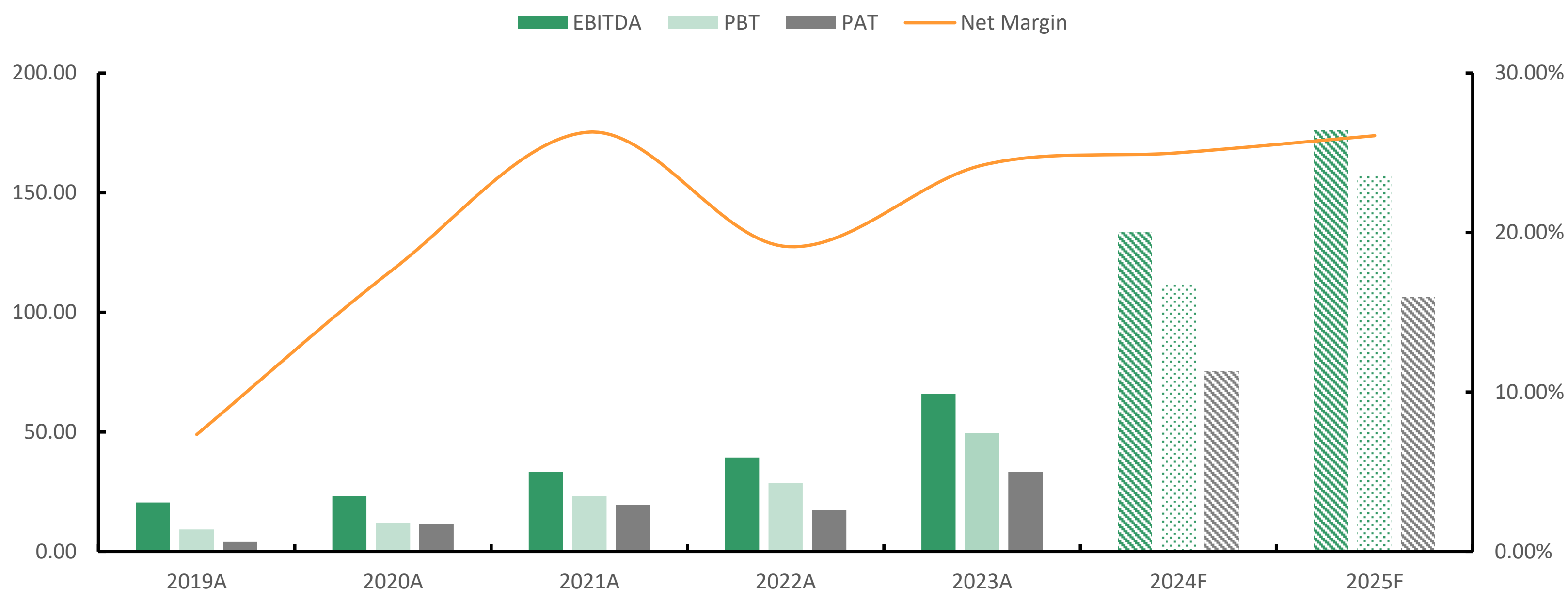
Contrary to the decline in previous years, finance costs registered a slight increase of 8.28% YoY in 2022FY, primarily attributed to foreign exchange losses from dollar-denominated debt, as the Naira continued its free fall. The impact of the Naira devaluation in 2023 was also shown in its finance cost as the firm recorded a foreign exchange loss of NGN8.42bn, leading to a finance cost of NGN15.09bn. It is noteworthy that the company has effectively managed and cushioned its interest expenses, mostly funding its capital expenditure programs through reinvestment rather than taking on significant additional debt. Thus, interest coverage remains positive at 3.13x in 9M:2023 (5-year average of 3.08x). Additionally, the settlement of foreign currency debt obligations using proceeds from international business has prevented major currency mismatches between liabilities and income. Also, the firm has made complete repayment of the USD215mn acquisition loan thus, reducing its exposure to dollar denominated debts.

Subsequently, in the seven years under assessment, TPP has consistently maintained a profitable business.

In 2023FY, profit before tax surged remarkably by 72.20% YoY to reach its highest-ever level on record at NGN 49.28bn, compared to NGN28.62bn in 2022FY. Mirroring the trend in PBT, the profit after tax grew by its fastest pace in four years by 92.47% YoY to NGN33.27bn (vs NGN17.28bn in 2022FY).

Consequently, key profitability ratios remained above the four-year averages: return on equity (43.25% vs 40.52% 4-yr avg), return on asset (15.02% vs 8.21% 4-yr avg) and Net Margin (24.21% vs 17.56% 4-yr avg). For 2024FY, we estimate a sustained expansion in net margin to 25.00%, signifying continued profitability.

Chart 7: EBITDA, Profit Before Tax, Profit After tax NGN'bn (LHS), Net Margin (RHS)



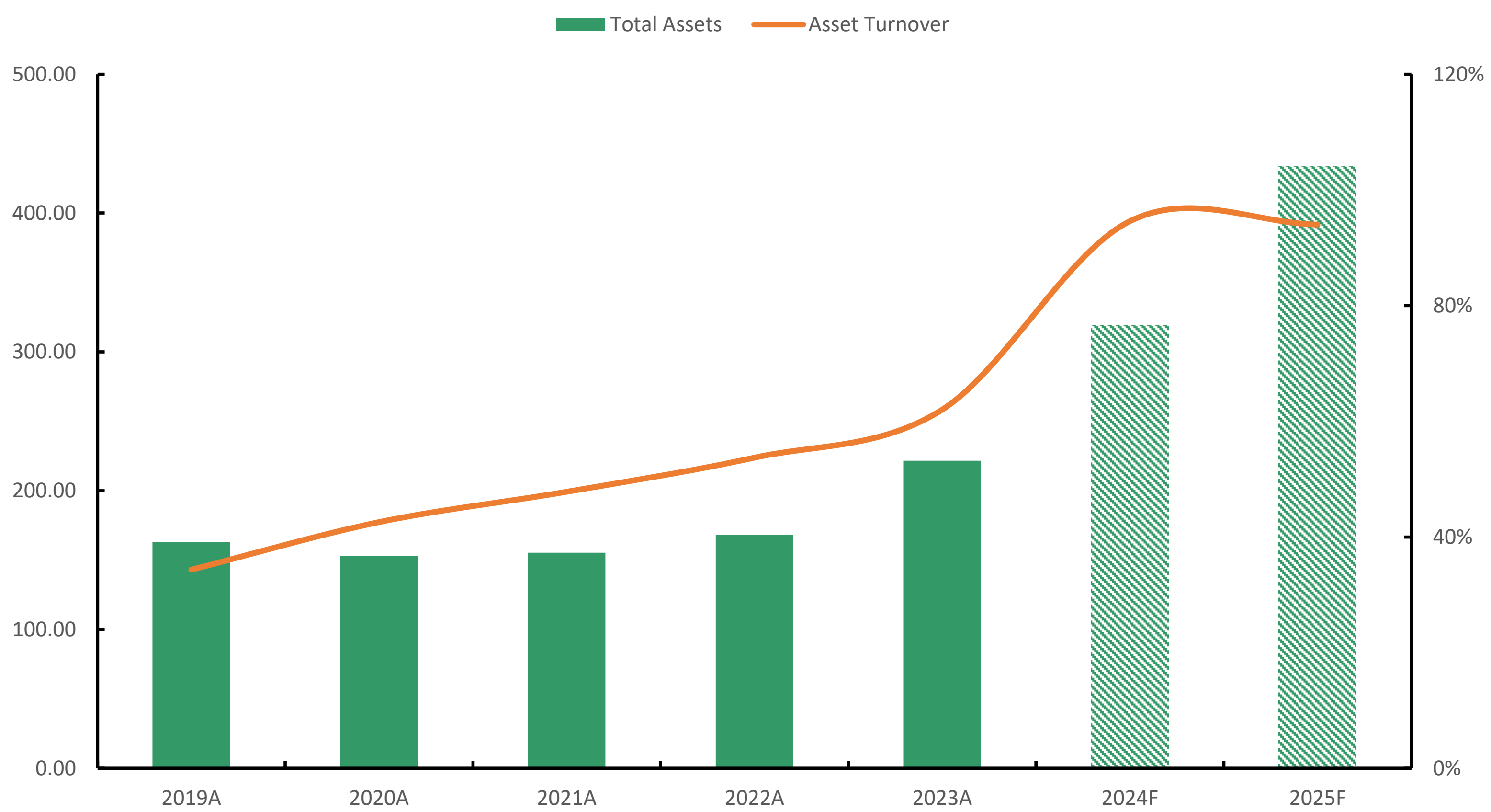
Source: *Company's Financials, Meristem Research*

Assets Optimization for Enhanced Value Creation

Due to the inherent nature of the business – *where payments from Distribution Companies (Discos) are typically received post power delivery* – trade and other receivables have consistently represented an average of 93% of current assets and 54.84% of total assets over the five years under review. This, combined with its high trade payables (83% of current liabilities has kept liquidity metrics low over the years (1.07x in 2022FY vs 5-year average of 1.13x). Also, owing to the utilization of physical immovable assets such as turbines, generators, and other plant infrastructure and equipment, Property, Plant, and Equipment (PPE) make up an average of 33.06% of the balance sheet composition. Over the past five years, the company has witnessed a moderate growth of 1.88% in its total asset base, increasing from NGN 150.38bn in 2018 to NGN 168.19bn in 2022FY. Despite this gradual expansion in total assets, the company has been able to achieve significant revenue growth. This indicates the company's adeptness at optimizing the utilization of its existing assets (particularly turbines) through its life extension plan, without necessarily increasing or adding to its asset base. As a result of this strategic approach, the company's assets turnover has maintained an upward trajectory (0.62x in 2023FY vs 5-year average of 0.47x). This underscores the efficiency with which the company leverages its assets to generate revenue, indicating a robust and effective management of its asset portfolio.

The company has consistently funded its assets with a blend of operating liabilities, equity and debt over the years. In 2023FY, the decline in debt (-9.46% YoY) which stemmed from the repayment of some short-term loan facility led to an improvement in debt ratios: debt to equity (0.49x vs 1.13x in 2022FY) and financial leverage (2.88x vs 4.43x in 2022FY).
Furthermore, the company has consistently maintained a positive operating cash flow position over the years, with net cash flow from operating activities reaching NGN24.44bn as of 2022FY. Its earnings quality ratio at 1.41x (vs 1.40x 5-year average) signals a strong earnings quality position. Moreso its cash flow-to-capital expenditure ratio improved to 5.65x (from 4.92x in 2021FY, albeit lower than its 5-year average of 7.17x) indicating the company's ability to fund its capital expenditure projects internally without having to access external financing. However, the firm's cashflow to debt coverage ratio decline to 0.57x (from 0.88x in 2021FY) despite the reduction in its debt obligations during the period.
Overall, we are comfortable with the firm's operating cash flow levels as they provide sufficient wiggle room for the firm to expand its capital structure without excessively increasing its risk profile.

Chart 8: Total Assets NGN'bn (LHS) and Asset Turnover (RHS)



***Source:** Company's Financials, Meristem Research*

Valuation and Recommendation

Summary

Methodology	Fair Value (NGN'trn)
Equity DCF [FCFE]	2.316
Economic Profit	2.540
Enterprise DCF [FCFF]	2.012
Relative Valuation	1.500
Valuation	**NGN2.290**

Metrics	NGN
Value Per Share	305.33
Current Price	264.00
Upside Potential	+15.66%
Recommendation	BUY

Basis for Valuation

In arriving at a fair value of NGN2,289,899,272,281.17 **(NGN305.33 per share)** for Transcorp Power Plc, we utilized a blended Discounted Cash Flow (DCF) valuation models (Equity Discounted Cash Flow Model, Enterprise Discounted Cash Flow Model, Dividend and Economic Profit Model) and the Relative Valuation Approach. The valuation process considered the company's growth prospects, inherent risks, and both positive and negative factors influencing its outlook.

Transcorp Power is perceived to be on a growth trajectory, marked by significant its notable operational efficiency aimed at delivering long-term value to investors. Recognizing the impact of key transformative reports in industry, **TPP** has seized the opportunities arising from the evolving dynamics of the power value chain on both domestic and global fronts (laying footprints in markets outside Nigeria). The company has consistently endeavored to enhance its capacity utilization, thus gaining increased market share in the process.

Risks

Several risks can impact our optimistic outlook of the company. One significant risk is a situation where the control cap on raw gas is removed. With the plant's heavy reliance on gas inputs for power generation (being a thermal plant). Fluctuations in gas costs can significantly affect direct cost and overall profitability. Regulatory uncertainties and policy changes, especially in the context of evolving environmental regulations, pose another threat, potentially requiring costly adjustments to adhere to new standards. Additionally, unforeseen disruptions in the power grid, theft and insecurity in regions where the company operates can lead to operational challenges and financial setbacks.

Appendix

Financial Statement Summary

*All figures are in **NGN'bn** unless otherwise stated. **A** = Actual; **E** = Estimate; **F** = Forecast;*

Profit or Loss Statement	2020A	2021A	2022A	2023A	2024F	2025F	2026F	2027F	2028F
Revenue	65.12	74.33	90.35	137.38	302.15	407.49	597.64	786.90	976.94
Cost of Sales	35.76	36.35	44.69	62.77	148.15	203.41	300.51	392.18	488.54
Gross Profit	29.36	37.98	45.66	74.61	154.01	204.08	297.13	394.72	488.40
Operating Expenses	7.01	4.90	6.52	9.27	22.10	30.09	45.55	64.19	79.41
EBITDA	23.14	33.21	39.32	65.94	133.33	175.91	253.80	333.85	412.85
Operating Profit	20.03	29.84	35.87	61.74	128.18	170.11	247.33	326.30	403.83
PBT	11.94	23.09	28.62	49.28	111.89	157.35	234.19	305.43	375.86
Profit After Tax	11.46	19.54	17.28	33.27	75.53	106.21	158.08	206.16	253.70

Statement of Financial Position	2020A	2021A	2022A	2023A	2024F	2025F	2026F	2027F	2028F
PPE	49.38	54.03	54.70	58.77	60.78	61.19	61.99	66.81	73.34
Trade and Other Receivables	88.31	77.00	94.56	142.57	232.56	336.54	474.05	571.90	632.91
Total Assets	152.93	155.41	168.19	221.55	319.43	433.41	608.84	740.45	930.86
Total Equity	24.54	34.01	37.96	76.91	105.19	137.90	184.98	257.65	355.36
Current Liabilities	72.41	100.82	95.20	104.40	175.11	248.48	368.72	416.07	477.52
Non-Current Liabilities	55.98	20.59	35.02	40.23	39.13	47.03	55.14	66.73	97.98
Total Debt	57.38	44.88	43.07	37.86	41.14	49.46	58.22	71.38	106.92
Total Liabilities	128.39	121.41	130.22	144.63	214.24	295.51	423.86	482.80	575.50
Total Equity and Liability	152.93	155.41	168.19	221.55	319.43	433.41	608.84	740.45	930.86

Ratios	2020A	2021A	2022A	2023A	2024F	2025F	2026F	2027F	2028F
Gross Margin	45.08%	51.10%	50.53%	54.31%	50.97%	50.08%	49.72%	50.16%	49.99%
EBITDA Margin	35.53%	44.67%	43.52%	48.00%	44.13%	43.17%	42.47%	42.43%	42.26%
Operating Margin	30.75%	40.15%	39.70%	44.94%	42.42%	41.75%	41.38%	41.47%	41.34%
Net Margin	17.60%	26.29%	19.13%	24.21%	25.00%	26.06%	26.45%	26.20%	25.97%
Asset Turnover	0.43x	0.48x	0.54x	0.62x	0.95x	0.94x	0.98x	1.06x	1.05x
ROE	46.72%	57.47%	45.53%	43.25%	71.80%	77.02%	85.45%	80.02%	71.39%
ROA	7.50%	12.58%	10.28%	15.02%	23.64%	24.51%	25.96%	27.84%	27.25%
Current Ratio	1.28x	0.89x	1.07x	1.44x	1.40x	1.45x	1.45x	1.59x	1.77x
Cash ratio	0.01x	0.09x	0.03x	0.06x	0.05x	0.07x	0.14x	0.19x	0.42x
Times Interest Cover	2.36x	3.80x	4.21x	4.09x	7.25x	11.33x	13.27x	12.90x	10.42x
Debt to Equity	2.34x	1.32x	1.13x	0.49x	0.39x	0.36x	0.31x	0.28x	0.30x
Financial Leverage	6.23x	4.57x	4.43x	2.88x	3.04x	3.14x	3.29x	2.87x	2.62x

CONTACT INFORMATION

Brokerage and Retail Services
topeoludimu@meristemng.com (+234 905 569 0627)
adaezeonyemachi@meristemng.com (+234 808 369 0213)
contact@meristemng.com

Investment Banking/Corporate Finance
rasakisalawu@meristemng.com (+234 806 022 9889)
davidadu@meristemng.com (+234 810 940 4836)

Wealth Management
funmilolaadekola-daramola@meristemng.com (+234 803 355 0008)
crmwealth@meristemng.com (+234 01 738 9948)

Registrars
nkechinyeluokoye@meristemng.com (+234 803 526 1801)
www.meristemregistrars.com (+234 01 280 9250)

Group Business Development
sulaimanadedokun@mersitemng.com (+234 803 301 3331)
ifeomaanyanwu@meristemng.com (+234 802 394 2967)
info@meristemng.com

Trust Services
damilolahassan@meristemng.com (+234 803 613 9123)
trustees@meristemng.com

Investment Research
praiseihansekhien@meristemng.com (+234 817 007 1512)
research@meristemng.com

Client Services
adefemitaiwo@meristemng.com (+234 809 564 6430)
brandandcomms@meristemng.com (+234 01 280 9250)

Meristem Finance Limited
olasokomubo@meristemfinance.com (+234 803 324 7996)
matthewawotundun@meristemfinance.com (+234 802 390 6249)

Corporate websites:
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