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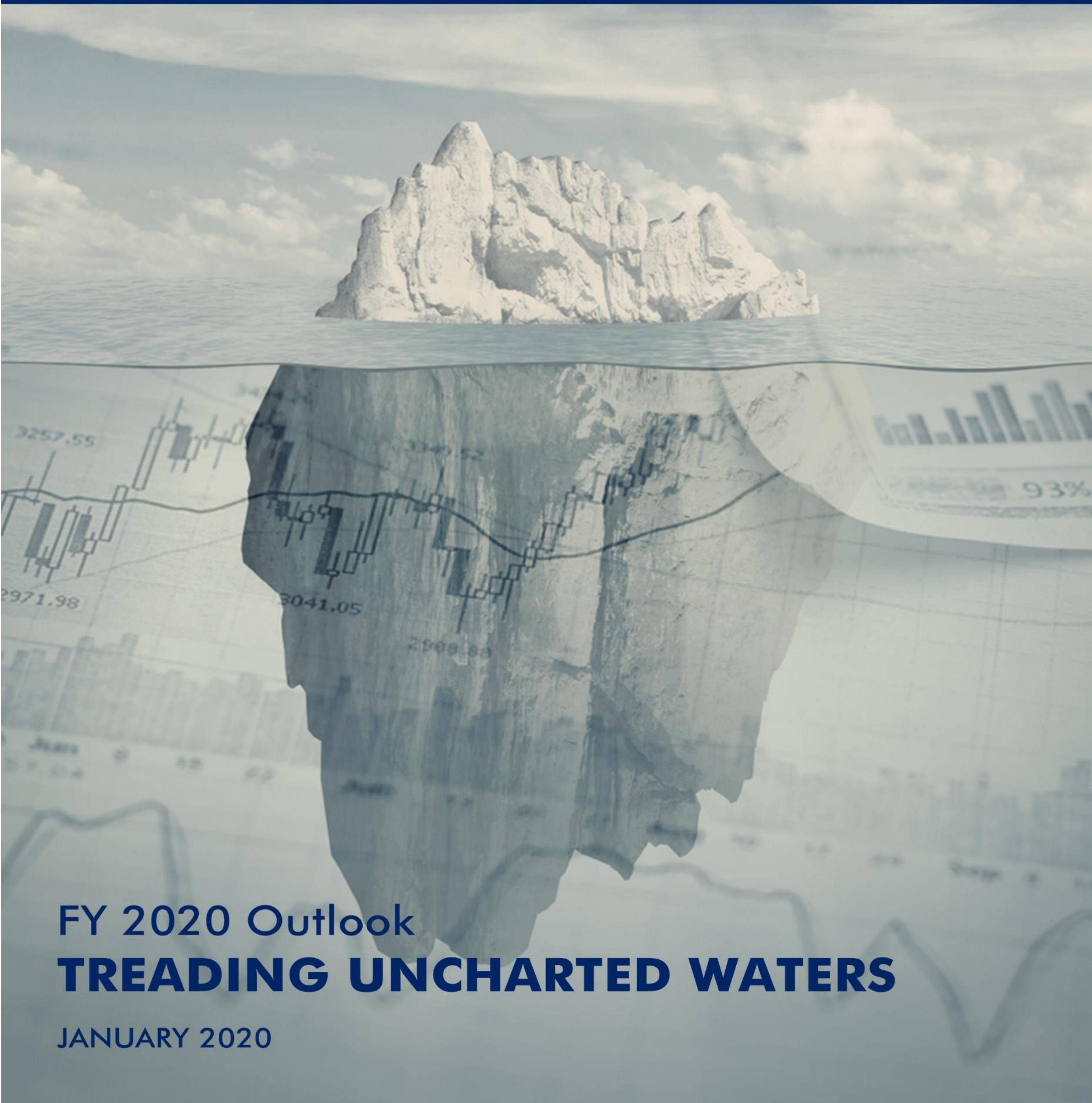

FY 2020 Outlook

TREADING UNCHARTED WATERS

JANUARY 2020

Executive Summary

We expect improvement in the domestic economy on the back of the structural changes that began in 2019. Notwithstanding, per capita income is likely to remain frail with scope for further changes in consumption patterns and, possibly, excess capacity for a few companies. Monetary bias could remain largely dovish, with administrative measures set to leave system liquidity at elevated levels and yields mostly lower in H1'20. Bold reforms would be needed to lubricate proposed implementation of Nigeria's ₦10.6 trillion budget to properly stimulate growth.

Below is a summary of our calls on Nigeria's broad macro environment.

Global economy	• GDP to recover by 10bps to 2.5% in 2020 according to World Bank • Oil prices forecasted at c.$64.83/bbl (2019: $64.14/bbl) • Global trade is likely to improve on better US-China relations
Domestic economy	• GDP predicted to improve to 2.4% in 2020 (2019E: 2.2%) • Oil production should average 2.1mbpd in 2020 (vs. 2.2mbpd in budget target; capacity of 2.5mbpd)
Monetary Policy	• Inflation forecasted to average 12.2% in 2020 • CBN to maintain administrative measures to support growth
Markets	• Liquidity deluge may sustain yield decline for most of H1'20 (1-year T-Bill yield should range between 4.0% and 5.0%; 10-year bond yield could range between 8.5% and 9.5%)
FX	• Reserves to range between ±5.0% of current levels of $38.3 billion • CBN to maintain naira defense for most of 2020

In equities, we expect investors to take advantage of bargain hunting opportunities in fundamentally strong names. We see scope for capital gains in ZENITHBANK, UBA, GUARANTY, and FBNH in the banking space. The investment case of WAPCO and UACN are also compelling following recent restructuring efforts/plans. The performance of a few other consumer names (such as FLOURMILL and NB) is likely to be buoyed by debt refinancing initiatives. We also like MTNN and DANGCEM, with reduced regulatory tension and strong market positioning set to buoy growth for the respective duo.

On fixed income, investors are more likely to stay short in view of expected recovery in interest rate in coming quarters.

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Company Ticker	Rating	TP (₦)	Ref Price (₦)[1]	Up/ Downside	Mkt Cap (₦'Bn)	2020F P/E	2020F D/ Y
Financial Services							
ACCESS	BUY	**11.97**	10.05	**19.10%**	357.3	3.2x	6.50%
ETI	BUY	**14.33**	7.70	**86.10%**	189.4	2.4x	0.00%
FBNH	BUY	**8.69**	7.50	**15.87%**	266.6	3.4x	4.70%
FCMB	HOLD	**2.04**	1.93	**5.70%**	38.2	3.1x	7.30%
FIDELITYBK	HOLD	**2.30**	2.24	**2.68%**	65.5	3.0x	6.70%
GUARANTY	BUY	**39.14**	32.20	**21.55%**	947.7	5.4x	8.70%
STANBIC	HOLD	**47.14**	42.50	**10.92%**	446.7	6.4x	0.00%
UBA	BUY	**10.06**	8.50	**18.35%**	290.7	3.0x	9.70%
ZENITHBANK	BUY	**28.46**	22.35	**27.34%**	701.8	3.9x	12.50%
Consumer Goods							
DANGSUGAR	HOLD	**15.84**	14.65	**8.12%**	174.0	8.3x	7.50%
FLOURMILL	HOLD	**25.65**	23.50	**9.15%**	96.4	9.4x	3.20%
GUINNESS	HOLD	**34.19**	30.20	**13.21%**	66.1	31.0x	2.60%
NB	BUY	**66.68**	52.00	**28.23%**	415.8	20.4x	4.90%
NESTLE	BUY	**1651.46**	1380.00	**19.67%**	1093.9	20.6x	4.90%
UACN	BUY	**13.66**	10.55	**29.48%**	30.4	4.6x	6.20%
Industrial Goods							
DANGCEM	BUY	**201.29**	173.00	**16.35%**	2944.6	13.3x	7.20%
WAPCO	BUY	**23.50**	17.35	**35.45%**	270.6	9.0x	3.90%
Agriculture							
OKOMU	BUY	**87.80**	66.00	**33.03%**	62.9	7.2x	3.03%
PRESCO	BUY	**73.70**	52.25	**41.05%**	52.3	8.3x	3.80%
Telecoms							
MTNN	BUY	**148.54**	128.50	**15.60%**	2361.1	12.2x	5.80%
Oil & Gas							
FO	SELL	**15.88**	20.60	**-22.91%**	26.8	17.1x	1.60%
MOBIL	BUY	**175.14**	147.90	**18.42%**	53.3	6.0x	5.40%
SEPLAT	BUY	**796.90**	588.00	**35.53%**	346.9	6.4x	7.80%
TOTAL	SELL	**96.55**	107.00	**-9.77%**	36.3	24.9x	2.70%

[1] Reference date is Tuesday, 21 January 2020

Contents

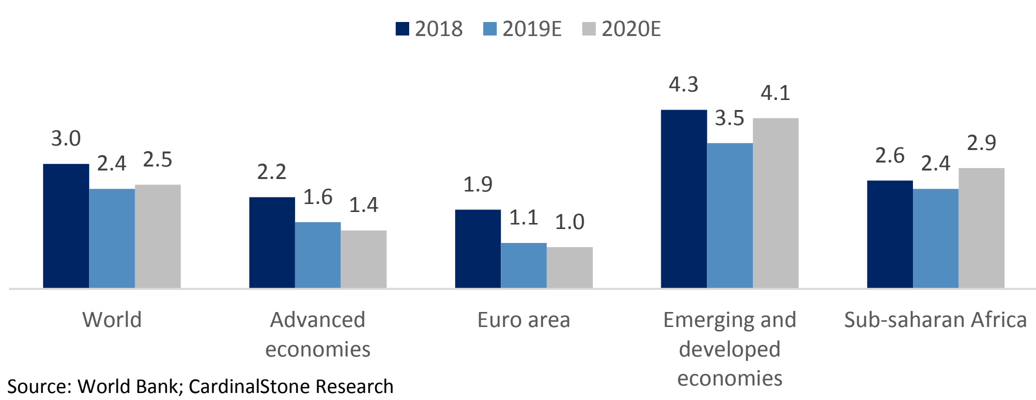
Global GDP to recover from synchronized slowdown in 2020

The global economy floundered in 2019 as growth momentum slowed and investment prospects weakened. The softer-than-expected economic upturn led to a downward revision of global growth forecasts for 2019 by the World Bank (from 2.6% to 2.4%). Trade concerns and weak economic data were among the key highlights of the year, which, consequently made monetary policy increasingly dovish as key economies shifted from interest rate normalization of the previous year.

Emerging & developing market resurgence to power global growth

The World Bank expects global economic growth to accelerate by 10bps YoY to 2.5% in 2020E, with the strongest upturn predicted to come from emerging market and developing economies. Across advanced economies, growth is projected to weaken to 1.4% (vs. 1.6% in 2019E), partly due to waning fiscal stimulus in US, Euro Area, and Japan. Slowing demand, declining manufacturing, and decelerating exports are also expected to negatively impact some advanced economies in 2020. Conversely, growth in emerging market and developing economies is forecasted to accelerate by 60bps to 4.1% in 2020E even though China's growth is expected to weaken further on slowdown in labour productivity expansion. Growth in this bloc is likely to be supported by base effect from countries that witnessed significant contraction in 2019 relative to 2018[2]. From a global trade standpoint, the new Phase 1 deal between US and China can open growth opportunities, with potential US-Japan and US-Mexico-Canada trade agreements notable upside risks to global growth. The Phase 1 deal indicates that tensions between China and US have waned, but confidence that a final resolution will be attained in 2020 remains weak due to previous stalemates. Projected softness in developed market growth suggests that key central banks are likely to remain dovish with focus on stimulating domestic credit. This is likely to cap scope for yield increases, weaken the dollar, and support oil prices. However, the outlook for oil is also contingent on the elongation (or otherwise) of the OPEC+ deal, tensions in the Middle East, trade brinkmanship, and expected output in US and countries outside OPEC+.

Figure 1: Global and regional economic growth forecasts (%)



Source: World Bank; CardinalStone Research

[2] These are countries like Brazil, Mexico, India, Russia, and Saudi Arabia

Key geopolitical themes that can define 2020

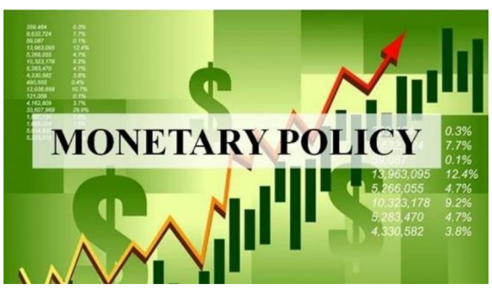
US-China trade spat

US-China trade tension could further taper due to the signing of the Phase 1 deal. Further gains on this front are likely to boost global growth and increase demand for commodities such as crude oil.

Deeper OPEC+ cuts

OPEC+ agreed to implement deeper oil production cuts from December 2019 to March 2020 on global growth fears. This could slightly offset expected impact of stronger shale output in 2020. EIA projects 2020 Brent prices at $64.83 per barrel (2019: $64.36).

Global financing conditions



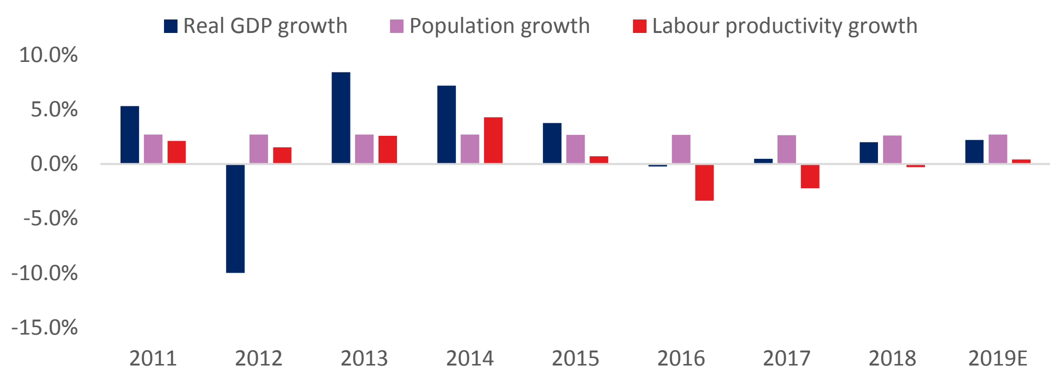
Global monetary easing will likely subsist in 2020, albeit at a slower pace. Yields are likely to remain low and/or move into negative territories as central banks react to global growth fears. Prices of riskier assets could remain volatile in early 2020 while currency performance could be mixed across markets.

Nigeria's GDP growth is likely to remain lackluster in 2020

Low labour productivity makes high population growth troubling

We expect the Nigerian economy to grow by 2.4% in 2020E (World Bank: 2.1%) on slow reform convergence, huge infrastructure gap, low private investment, and weak consumption. Relative to population growth rate of 2.7%, our growth expectation suggests that Nigeria is likely to continue facing the changing consumption patterns that have forced a few companies to operate at less than full capacity, while enduring further standard of living concerns in 2020. Although we acknowledge that a growing population could also positively impact the size of available workforce and consumers within the country, adequate investments would have to be directed at human capital development to ensure that the duo contribute to increases in the value of output in the near-to-medium term. As aptly noted in our H2'19 outlook titled "Fish or Cut Bait", infrastructure gap would also have to be plugged by private capital injection to boost growth in Nigeria in view of FG's slow fiscal consolidation. The development and quick implementation of required reforms are a sine qua non to attracting this required private capital, in our view.

Figure 2: We believe population growth became a real concern since 2016



Source: World Bank; CardinalStone Research

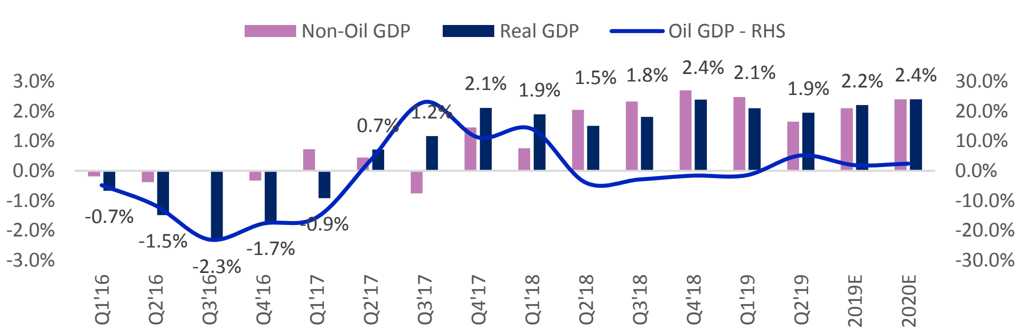
Non-oil GDP constituents to pull in different directions

The reforms and administrative efforts implemented to stir non-oil sector are likely to support slight recovery in the segment in 2020, in our view. For one, despite its anti-trade connotations, sustained border closure and/or enforcements are likely to incentivize local production of oil palm, rice, poultry, and a few other agricultural products. This, together with the notable improvement in the handling of herdsmen related conflicts, is likely to drive a 2.9% growth in agriculture GDP in 2020 (vs. c.2.6% in 2019E). Strict border enforcements could also lead to further increases in domestic prices and reduction in imported competition that has hitherto stifled manufacturing, even though weaker consumer discretionary income and poor access to export markets are restrictive. Aided by availability of cheaper funding, we project a c.1.5% YoY growth for the sector in 2020 (vs. 0.8% in 2019E). We also expect greater down trading to cheaper brands in the coming year as higher electricity tariff and value added taxes crimp disposable income. Elsewhere, growth in trade and services are likely to be subdued in 2020, with the former likely to reflect the impact of stiffer border enforcements while the latter could be pulled back by waning base effect in ICT. Our view on real estate (2020E: -0.2%; 2019E: -1.1%) is now less bearish with ongoing moderation in yields likely to cascade to better flow of funds to the sector. That said, high-end real estate growth is still likely to be pegged back by the clamp down of money laundering & terrorists financing through property transactions in 2020. While we acknowledge the recent traction in administrative and reform efforts, the noted restrictive factors are likely to cap non-oil GDP growth at 2.3% in 2020E, in our view.

Government is right to push for reduced reliance on oil output

Nigeria's oil GDP is 3.6x[3] more volatile than its non-oil counterpart, underpinning one weakness in anchoring development plans on the sector's economics. The sector is likely to be positively impacted by a ramp up of production in Egina and potential OPEC+ production cut extension and restrained by domestic disturbances. OPEC data suggests that Nigeria's crude oil production (ex-condensates) increased by 5.6% QoQ (c.12.9% YoY) in Q3'19, possibly reflecting the re-opening of previously closed infrastructure (such as Trans Forcados and Bonny Terminals) and increasing output from Egina. Despite the oil output traction seen since Q2'19, scope for growth could still be capped by slow pace of reforms and inadequate private investments. Notably, the recently signed Production Sharing Contract (PSC) amendment bill, which seeks to increase FG's share of past and future royalty and profit oils, is likely to be viewed with suspicion by International Oil Companies (IOC). This, as well as the huge probability of disturbances in oil producing areas, has informed our 2.1mbpd (+8.8% YoY) projection for oil production in 2020. Overall, we expect growth to remain frail in the current year as the country adjusts to new policy initiatives. We believe that the new reforms drummed up to improve FG's ability to provide stimulation would have to be complemented by other pro-market policies capable of attracting patient capital into the country to maintain stable growth trajectory.

Figure 3: Oil GDP is 3.6x more volatile than non-oil GDP



Source: NBS; CardinalStone Research

[3] Volatility was computed using available monthly data since 2010

Reforms: the long game could bring short term pain

The federal government introduced a raft of policies in the second half of 2019 directed at boosting productivity and long-term economic growth in line with the tenets of the ERGP. Adjustments made to profit sharing contracts with IOCs and introduction of the Finance Bill were largely targeted at improving fiscal consolidation, while proposed policies such as the implementation of cost reflective tariffs and stricter border enforcements were aimed at attracting desired investors into power and agriculture value chains, respectively. While these policies are capable of cascading into tangible medium-to-long term gains, we note that there could be associated short term ramifications in forms of higher inflation and lower consumption per capita.

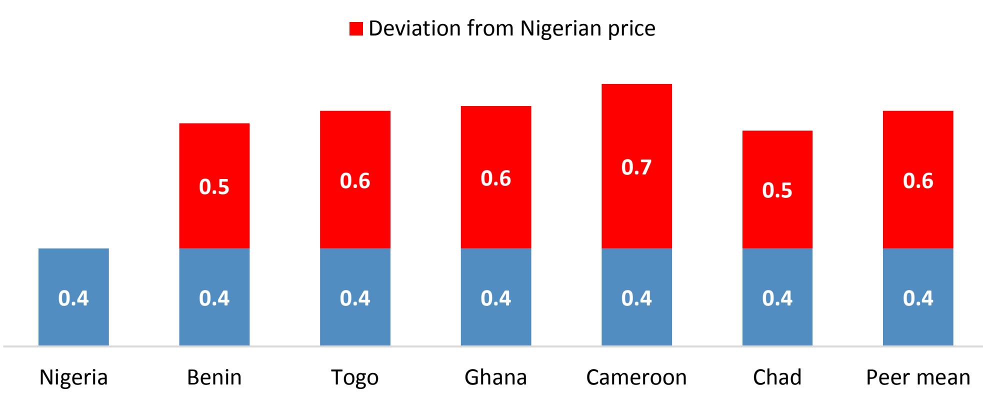
Stricter border security to bolster local productivity, steer economic growth

In a bid to encourage local production of food and reduce the cost of petrol subsidy, the Federal Government (FG) closed Nigeria's land borders (in August 2019), which had been notoriously porous and had undermined its import substitution drive. In addition to restricting unlawful food (primarily rice) importation, the border enforcement was also undertaken to restrain the illegal exports of Premium Motor Spirit (PMS). In our view, Nigeria's new protectionist tilt has had a largely mixed impact on the economy. On the positive side, Q3'19 GDP reading suggests notable improvements in agriculture (Q3'19: +2.3% YoY vs. Q2'19: +1.9% YoY) and manufacturing (Q3'19: +1.1% YoY vs. Q2'19: -0.1% YoY) since the border enforcements. In addition to this, PPPRA's data suggests that FG's quarterly subsidy cost declined by ₦9.7 billion to ₦167.5 billion in Q3'19 from ₦177.2 billion in Q2'19 as PMS smuggling moderated on closure of land borders. We, however, note that PPPRA's computation of PMS cost breakdown was done using an average official rate of ₦306/$ which is materially lower than mean market rate of c.₦364.57. This implies that a significant foreign exchange subsidy saving resulting from the border closure is not accounted for when PPPRA's PMS pricing is adopted. Elsewhere, we envisage increased customs' receipt on the sea, as previously informal trades are rerouted through the seaports, where they are subject to applicable duties.

Having highlighted some positives from the border enforcements, *we also note near-term negative fall-outs such as surge in food prices, decline in importation of essential raw materials needed in manufacturing, disruption to Pan African businesses that rely on open trade channels to transact effectively, and the negative signal it sends about Nigeria's commitment to both the West African and African integration agendas*. However, we expect Nigeria and her neighbours to put in place appropriate measures to halt the trade restrictions before the end of H1'20. To this point, Nigeria's foreign minister has already noted that Benin and Niger Republic have both agreed to set up a joint patrol team with Nigeria to curb the incidence of smuggling. The team, which comprises of the police, customs, immigration, navy and state security services of the three countries, is also expected to advise on the re-opening of the borders in coming months.

Material arbitrage opportunities could jeopardize border enforcement efforts. For us, the vast arbitrage opportunities created by distortions to price mechanism (i.e. subsidies) and variation of tariff regime & aggressiveness create significant arbitrage opportunities that continue to incentivize illicit trade. PMS, for instance, is trading at a significant discount of c58.3% in Nigeria (₦145/litre), relative to the average in neighbouring West African countries (₦347/litre). This huge discount, coupled with significantly porous border security and the opportunity to take advantage of existing free trade with border countries to make abnormal profits, had provided massive scope to illegally leverage petrol price arbitrage for many years. Since PMS became solely imported by the Nigerian National Petroleum Corporation (NNPC), smuggling has aggravated the pressure on Nigeria's finances via higher petrol importation and greater subsidy payments. Evidently, a complete subsidy removal is a viable avenue to free up funds for the growth-inducing investments needed to stimulate the economy, while making illegal PMS smuggling significantly unattractive. Presently, there are huge incentives to smuggle and the c.2,200 petrol stations (NNPC estimates) located in Nigeria's traditionally porous border towns and coastal frontiers despite their relatively small land area was suggestive of a normalization of this illicit activity before the current border closure was enforced. We do not rule out the possibility that even the current border enforcements could eventually cave in as smugglers find a way around security apparatus in chase of huge arbitrage profits.

Figure 4: <u>**Low Nigerian PMS price ($/litre) creates scope for arbitrage profits**</u>



Source: Global Petrol Prices; CardinalStone Research

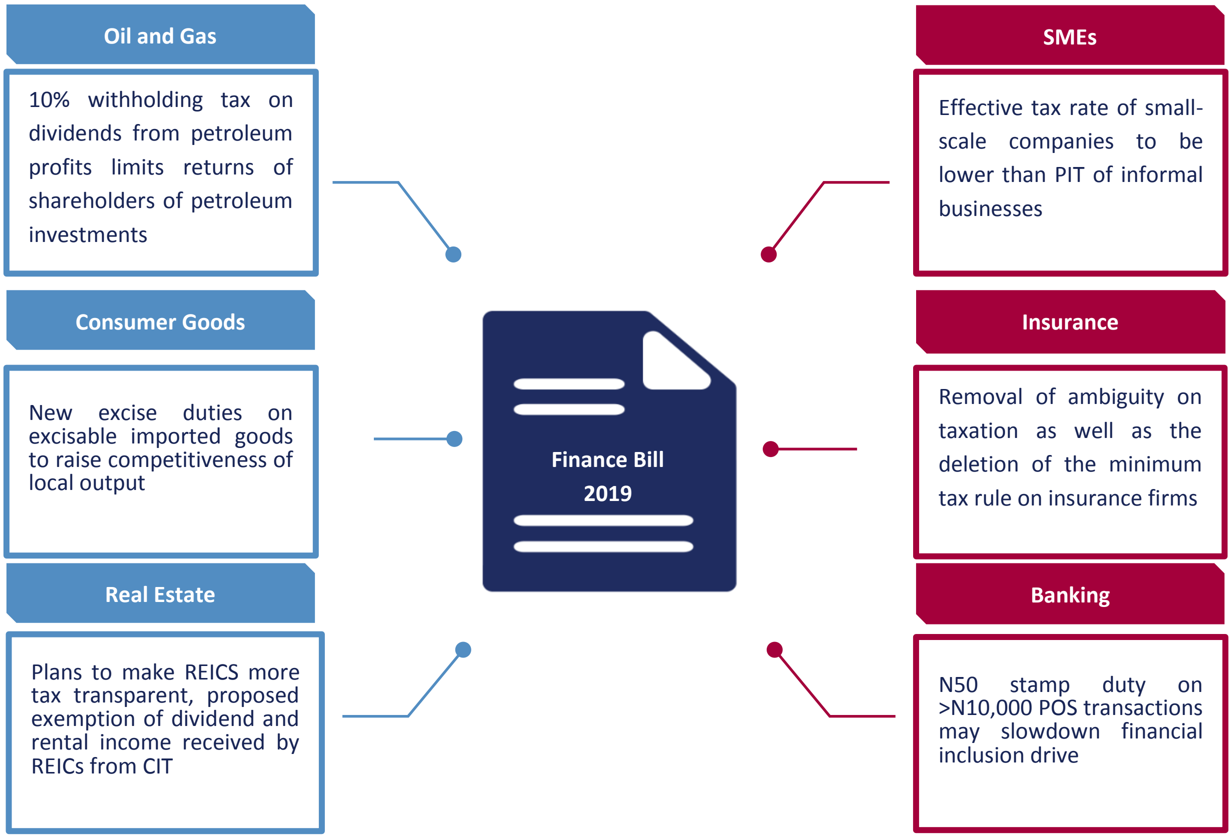
Away from PMS, neighbouring countries like Benin have served as trading hubs, importing staples (e.g. rice) and re-exporting them (often illegally) to Nigeria. Between 1995 and 2018, the Nigerian government placed varying degrees of embargo on used cars, selected food, and beverage products. As at 2018, importation of beer, poultry meat, and vegetable oils was outrightly banned while high import tariff were slammed on cigarettes (95.0%), sugar (70%), rice (70%), used cars (70%), and clothing (45% and FX ban). These trade restrictions were executed at a time when neighboring countries reduced tariffs to encourage importation of products, the bulk of which often ended up in Nigeria via illicit trade. In more ways than one, therefore, Nigeria inadvertently provides the framework upon which "arbitrage hackers" have thrived in West Africa. Thus, ongoing border enforcement can be viewed as a needed short-term response to age-long setbacks. We believe cross border agreements between affected countries, modernization of customs protocol via improved information technology and formalization of management procedures could improve accountability and transparency at the borders. Yet, these short-term panaceas would better deliver on long term expectations if they are complemented with a gradual dislodge from imperfections in the workings of price mechanism. This could entail the gradual removal of subsidies (FX and other subsidies) and better coordination of economic policies among neighboring West African countries.

Implementation of 2019 Finance Bill to support fiscal consolidation

President Muhammed Buhari signed Nigeria's 2019 Finance Bill into law on 13 January 2020, twelve days after its initially proposed effective date. The bill, which took effect after the presidential assent, is expected to promote fiscal equity, reform domestic tax laws, introduce tax incentives for investments in infrastructure and capital markets, support medium and small-scale enterprises, and raise government revenue. As per fiscal consolidation, the bill proposes an increase in value added tax (from 5.0% to 7.5%), stricter capitalization rule (not more than 30.0% of EBITDA), a rule requiring all bank accounts to have tax numbers, and taxation of dividend from petroleum profits that are likely to improve poor revenue mobilization outcomes (c. 54.1% of budget in 2018). The upward revision of VAT to 7.5% is also in line with FG's drive to ramp up non-oil receipts. However, it is pertinent to note that only 15.0% of total VAT collection accrues to FG, with the remainder allocated to states and local governments. Thus, the bulk of the added income from higher VAT is likely to provide an offset to the extra burden associated with the implementation of minimum wage and reduce the likelihood of another FG bailout for states. In addition to the mentioned proposition for fiscal consolidation (thin capitalization and dividend tax on petroleum profits), FG had previously implemented an upward revision to the exchange rate used in the computation of customs duties to ₦326/$ from ₦306/$ in June 2019 that is expected to continue to boost custom revenue.

Finance Bill seeks to provide incentives for select sectors. Tax exemption provisions for SMEs who play in the pharmaceutical space or are involved in the production of educational items, fish, meat, poultry products, staples, and other cereals complement the reforms instituted to enhance ease of doing business under the Presidential Enabling Business Environment Council (PEBEC). Pertinently, these exemptions partially isolate these businesses from the expected effect of higher inflation and harsh operating cost environment in the current year. The Bill also proposed the introduction of new excise duties on excisable imported goods to raise the competitiveness of local output and boost consumer goods industry. Similarly, the removal of tax ambiguity and deletion of minimum tax rule on insurance firms is likely to encourage investments in the sector. On the flip side though, the introduction of taxes on dividend from petroleum profits is likely to be negatively received by stakeholders in the oil and gas space.

Figure 5: New Finance Bill seeks to boost fiscal consolidation and encourage SMEs



Source: Budget Office; CardinalStone Research

To improve oil revenues, the President assented to the amended Deep Offshore and Inland Basin Production Sharing Contract Act of 2004 in November 2019. Under the amended Act, royalty payable on a field basis was revised from erstwhile graduated rates to a uniform scale for deep offshore PSCs. The new policy effectively reduces royalty payment for offshore players with 200m-500m depth, while increasing that of players exploring greater depths. IOCs such as Shell[4] are known to play in the latter space and could be potentially negatively impacted. However, royalties payable by inland basin PSCs (a natural habitat for indigenous companies) were revised downwards to 7.5% from 10.0%, a move aimed at fostering conducive environment for local oil E&P players. The new bill also introduced defined royalty rates based on crude oil prices, eradicating the obscurity before the adjustment. In addition to royalty revisions, federal revenue is likely to be bolstered by the renewal of oil bloc licenses in mid-2020 according to the NNPC.

[4] Shell has a 200,000 bopd Bonga deep-water infrastructure while Chevron boasts a 108,000 bopd Agbami Fields facility

This is estimated to contribute N939.0 billion (11.2% of projected revenue for 2020) to 2020 fiscal revenue.

Figure 6: Changes in Production Sharing Contract Act

Royalty on field depth basis	For deep offshore PSCs: • 0% for > 1000m • 4% for 800 – 1000m • 8% for 501 – 800m • 12% for 201 – 500m	10 % for deep offshore PSCs greater than 200 m water depth
	10% for inland basin PSCs	7.5% for inland basin PSCs
Royalty on crude oil price basis	Provided for review of royalty rates where crude oil price exceeds $20 per barrel	• 0%: $0 - $20 • 2.5%: $21 - $60 • 4%: $61 - $100 • 8%: $101 - $150 • 10%: > $150

Source: Budget Office; CardinalStone Research

Electricity tariff review set to arrest liquidity crunch

The Nigerian Electricity Regulatory Commission (NERC) revised its Multi Year Tariff Order (MYTO) in August 2019, with a view to achieving full cost-reflective tariffs by July 2020. In the interim, the review of end user allowed tariffs suggests a c.30% increase in electricity charges by April 2020, per our estimates. Accordingly, the FG is also expected to remit outstanding tariff shortfalls (from 2015 – 2018) totaling ₦1.15 trillion to the Discos.

- We expect cost reflective tariff to provide support for the power sector, which is largely characterized by substantial debt and weak operational performance. While we expect higher tariffs and shortfall reimbursements to reduce the existing debt burden and render the sector more economically viable, we note that the pervasive issue of low collection rates still plagues revenue in the sector

- We see scope for renewed inflationary pressures from 2020, emanating from pass-through effects on the core inflationary components of the consumer price index. Potentially affected core components could include energy and housing water, gas, and other fuels.

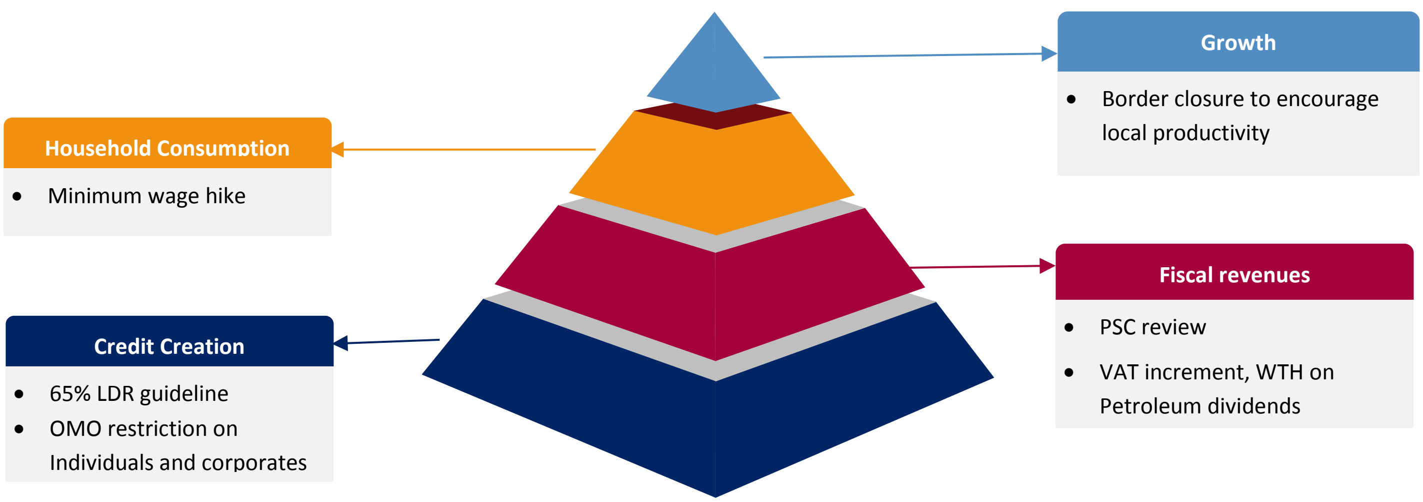
- Furthermore, higher energy prices could erode consumer discretionary income, counterbalancing the impact of higher minimum wage.

We downplay the expansionary impact of minimum wage implementation

In Q4'19, FG eventually reached an agreement with the Labour Union on the implementation of the minimum wage bill, following a long stalemate in negotiations surrounding the consequential adjustments across all civil service levels. The wage hike across all staff levels is largely expected to translate to higher spending because those at the lower end of the income spectrum theoretically have a higher marginal propensity to consume. The adjustment was, therefore, expected to fuel inflationary pressures. However, we believe that the potential knock on effect on inflation may not be material, guided by the last minimum wage hike that saw minimum wage surge to N18,000 from N7,500 with inflation remaining unchanged.

Level band	Increment (%)
1 - 6	66.7
7	23.2
8	20.0
9	19.0

Figure 7: Policy concoctions to support medium-to-long term growth



Source: Budget Office; CardinalStone Research

Monetary focus remains growth despite inflation trajectory

The monetary policy committee disclosed at the start of 2019 that Nigeria's lower aggregate output (relative to potential) leaves scope for non-inflationary GDP and monetary growth. The constraints imposed on fiscal policies and overall implementation of the ERGP was also believed to have made it imperative for monetary policy to provide the much-needed leverage to support output growth and employment generation— Summary from March 2019 MPC meeting

In line with the discussion above, the CBN cut the monetary policy rate once in 2019 to signal a shift in focus towards bolstering economic growth. While we do not expect the monetary authority to explicitly signal another dovish tilt in its next policy meeting in view of projections for higher inflation, we expect the apex bank to sustain its OMO ban and use of growth-targeted administrative measures to increase money supply and credit creation in the near term. Specifically, for administrative measures, we expect sustained direct interventions in the real sector and use of loan-to-deposit ratio requirements to encourage lending. In addition, the CBN is likely to remain steadfast in its bid to maintain exchange rate stability through 2020, with the recent restriction of OMO bill transactions to foreign investors and banks making it cheaper to target foreign funds at lower cost.

Improved CBN targeting allows for dovish monetary stance

In our view, the CBN has done a better job at targeting foreign portfolio investors (FPIs) by essentially decoupling the OMO market from the treasury bills market through the introduction of the OMO ban instituted in October 2019. The ban, which restricts participation of local players from buying OMO instruments is set to reduce interest costs for the CBN, while allowing for the unrestricted access of foreign investors to its high yield money market paper. Prior to the OMO ban, OMOs and NTBs were largely viewed as interchangeable, with the former usually trading at a slight premium to the latter. However, the yield on both instruments have diverged materially by 936bps since the restriction, with the one-year OMO trading at a yield of 15.20% compared to a yield of 5.84% on the corresponding T-Bill, as at 17 January 2020. The wide spread seeks to simultaneously keep the carry-trade attractive enough in the OMO space to motivate FPIs to remain in the country, while supporting domestic credit creation/growth through administrative measures. Indeed, the apex bank has sought to do the latter by redirecting liquidity to the private sector through its institution of a Loan-to-Deposit (LDR) ratio requirement of 65% by December 2019 and the creation of liquidity through the elimination of OMO roll over for domestic non-bank investors. These measures have, so far, delivered the desired outcomes as credit creation has improved (+11.5% YoY to ₦27.8 trillion as at October 2019) and borrowing cost has significantly reduced. Most importantly, these objectives were achieved while simultaneously ensuring a relatively decent spread for FPIs. Although there are arguments that credit creation through increased liquidity could drive inflation significantly above CBN's single digit target, we retain our view that Nigeria's inflation is largely supply side driven. For context, Nigeria's inflation has been largely driven by disruptions to food supply stoked by insecurity and border closures in the last two years. In 2020, we believe the key driver of inflation would be the upward revision to energy tariffs (again a cost push factor) barring any shock naira devaluation. Hence, the CBN may view an immediate liquidity reduction in response to potentially higher inflation as a rather ineffective remedy.

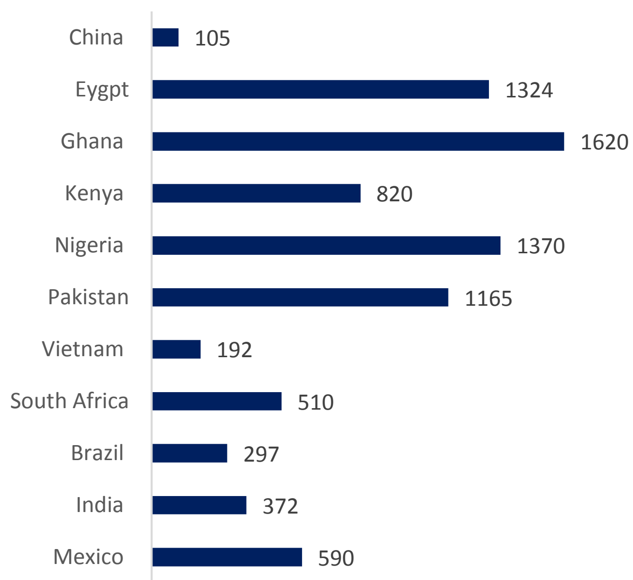
We see near term NGN stability, but reserves remain susceptible to large outflows

To our minds, CBN's decision to make OMO bills (which has been the mainstay of many domestic institutional investors) exclusive to foreign investors and banks, to better target FPI's at lower cost is a sign of the bank's commitment to maintain the current exchange rate level. We believe this resolve is further buttressed by the apex bank's decision to follow up the OMO ban with a commitment to offer two-way quotes for OMO bills to address the liquidity concerns of FPIs. However, we highlight with concern that the strategy of defending the currency by attracting foreign portfolio flows has left Nigeria's reserves significantly vulnerable to external shocks. For context, NBS reports reveal that foreign portfolio investments in money market securities have grown from $557.0 million in 2016 to a cumulative of $11.9 billion as at September 2019. In view of this, FPIs now account for c.44.4% of Nigeria's foreign reserves. Nevertheless, in September 2019, the CBN Governor, Godwin Emefiele, was quoted as saying that the monetary authority will not devalue the naira until reserves falls below $30.0 billion. The determinant of naira stability would rest on the CBN's ability to retain most of the foreign portfolio flows amidst pervasive macroeconomic weakness and the possibility of a ratings downgrade from international ratings agencies.

OMO rates vital to FPI retention

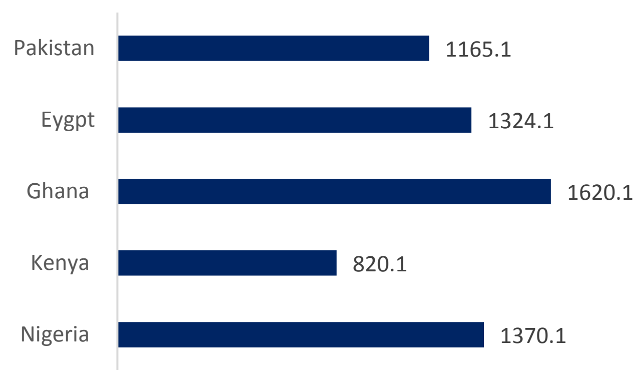
While T-Bill and Bond rates may be pressured by liquidity concerns, OMO rates are likely to be driven by the attractiveness to foreign investors, external financing conditions, and changes in Nigeria's risk profile. In our view, reserves could fall below the threshold $30 billion, which, according to the CBN, could trigger a devaluation, if all or some of the drivers of OMO rates move unfavorably. However, the CBN's body language suggests that it is likely to do all within its powers to hold currency at near current levels. This could entail leaving OMO carry trade largely unchanged amidst sustained dovish orientation across foreign markets. Expectations for relatively stable oil price in 2020, aided by the recently announced deeper oil production cut by OPEC+ and sustained global easing, suggest that the apex bank may not have to significantly raise OMO rates to keep FPIs. On this wise, we expect the CBN to maintain rates at current levels with moderate fluctuations of around +/- 50bps from current yield level of 15.3% in H1'20. Our outlook is further supported by an already higher interest rate compared to frontier market peers and countries of similar credit ratings. For context, Nigeria's yield spread versus the US benchmark is the widest among selected peers of countries with equal risk profiles (i.e. +138bps higher than the spread of B rated peers).

Figure 8: Nigeria's spread over US yields vs frontier/emerging market peers (bps)



Source: World Government Bonds; CardinalStone

Figure 9: Nigeria's spread over US yields vs frontier/emerging market peers (bps)



Source: World Government Bonds; CardinalStone

Egypt has one of the most attractive carry in Sub Sahara Africa. The country's investment case is also strengthened by its strong growth, floated currency, and low inflation. In Nigeria, guaranteed liquidity and availability of hedge instruments could similarly help to retain some FPI interest.

Currency outlook

Devaluation: a question of when, not if

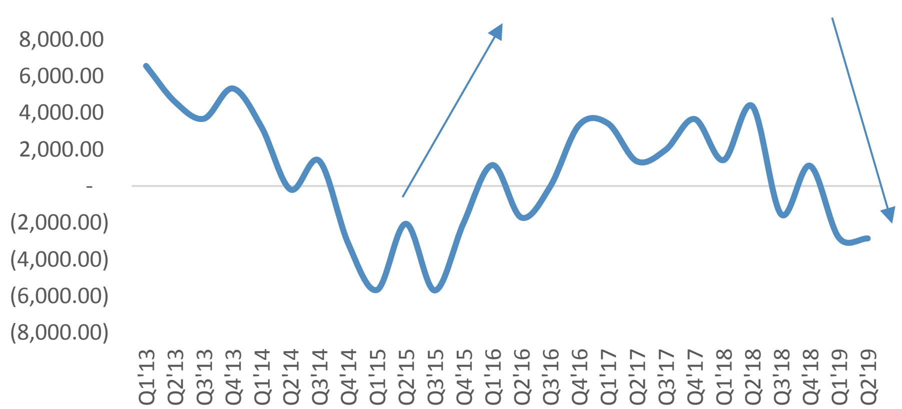
Concerns over the probability of *imminent* naira devaluation appear to have waned after the CBN hinted that it *will not* devalue the currency unless Brent crude oil price and the country's external reserves fall below $45.0/bbl and $30.0 billion, respectively. This also follows the apex bank's introduction of measures that point to the continued utilization of FX stabilization and intervention frameworks to support the exchange rate and retain the allure of the domestic market for foreign portfolio investors. Notable of these recent measures were:

- A ban on domestic non-bank institutions and individuals from participating in primary and secondary market OMO operations
- CBN's participation in the secondary market for OMO bills to enhance liquidity
- Sustained FX restriction for certain imports

While on the one hand these measures appear to be supportive of exchange rate stability in the near-to-medium term, we believe, on the other hand, that there emerges a conspicuity of concerns that suggest that the CBN's stance could continue to expose the economy to increased vulnerabilities. Some obvious risks to currency outlook are: 1) Persisting weakness in current account balance; 2) Increasing dependence on foreign portfolio flows; 3) oil price volatility; 4) unfavourable changes in external financing conditions 5) weak macroeconomic environment. 6) High capex implementation could put pressure on FX

- **Persisting weakness in current account balance.** Nigeria has recorded current account deficits in 4 of the last 5 quarters, with the provisional Q3'19 reading coming in at a deficit of $2.80 billion. In our view, this is redolent of the trend during the economic crisis of 2014 – 2016, which partly led to the forced devaluation of the currency.

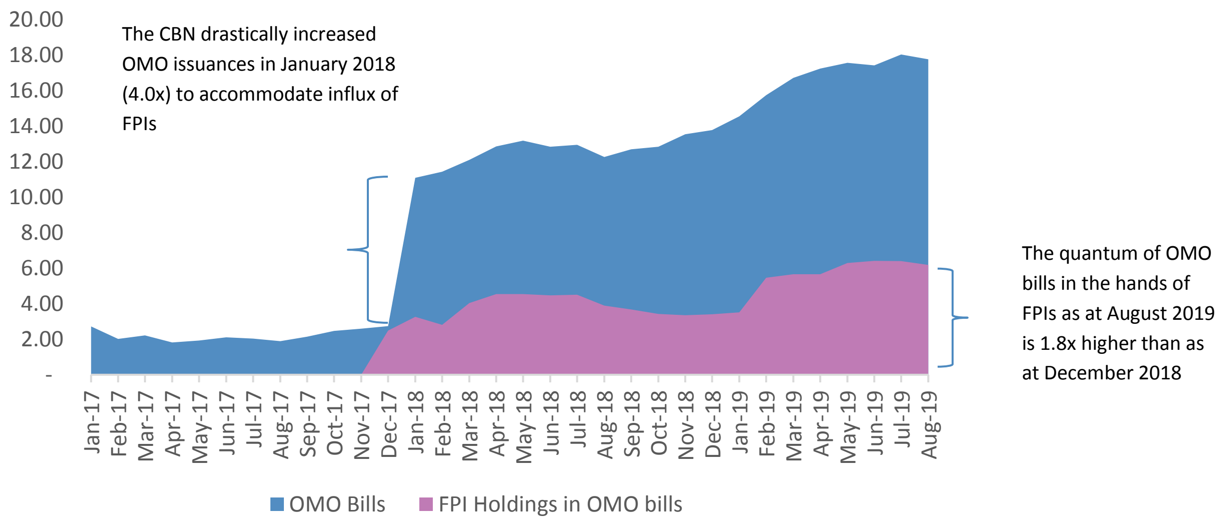
Figure: 10: Nigeria is facing current account pressures



Source: *CBN; CardinalStone Research*

- **Increasing dependence on foreign portfolio flows heightens vulnerability.** At $17.2 billion, foreign portfolio holdings of OMO bills account for roughly 44.4% of gross reserves. This increases the susceptibility of the nation's foreign reserves to external shocks such as interest rate normalization in developed markets and oil price volatility. More so, the recent restriction of the nation's OMO market to just banks and foreign investors raises concern that the CBN is unlikely to ease up on its approach of prioritizing hot money inflows as a key reserve component. This supports our view that the CBN will likely keep OMO rates attractive in the near term.

Figure 11: Uncertainty over FPI changes is now the key risk to NGN outlook

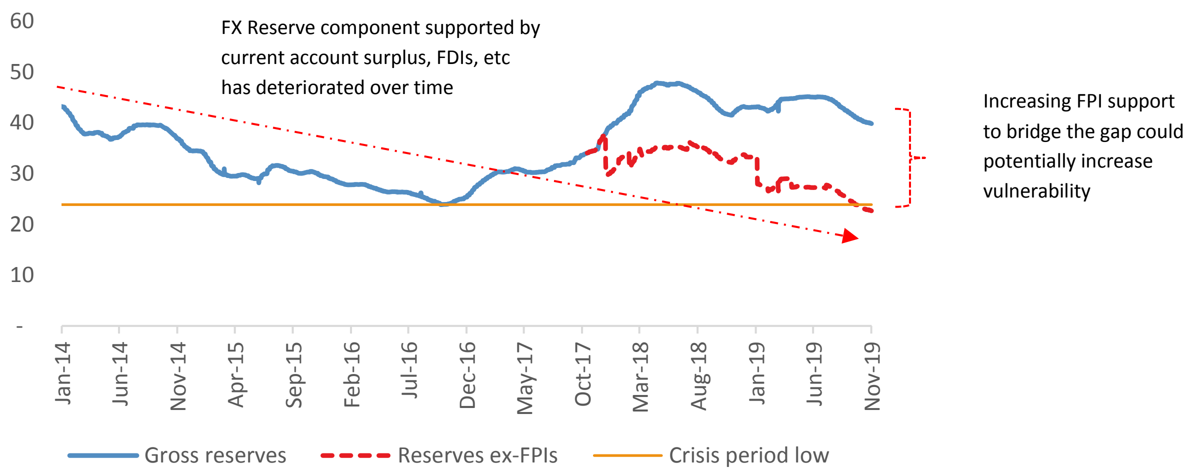


Source: CBN; CardinalStone Research

- **Oil price volatility and reserves adequacy concerns could drive negative sentiments.** Clearly, foreign investors' interests—across fixed income and equity markets—have largely tracked oil price performance, given that oil remains the most notable export commodity and FX earner in Nigeria. The outlook for oil price is largely dependent on the pace of global growth; changes in US oil inventory buildup; and the sustainability of OPEC's deeper production cuts. The US Energy Information Agency (EIA) forecasts that the Brent oil price will average $63.93 in 2019 (10.7% lower than 2018's average price) but increase marginally to $64.83/bbl in 2020. In our view, foreign investors' fixation on movements in oil prices makes it likely that a significant dip in Brent price could drive outflows that could hurt the domestic economy.

- **High capex implementation could put pressure on FX.** We expect the FG to take advantage of lower yield environment in 2020 by raising more debt to fund capital investments. However, with capital expenditure comes greater demand for forex needed to import required inputs. Thus, while higher capex spending may be positive for long term economic growth, it may have short term negative impact on the naira.

Figure 12: Breakdown of reserves



Source: CBN; CardinalStone Research

We expect naira volatility in 2020

Overall, prevailing macro weaknesses suggest the inevitability of a devaluation in our view. What is unclear is when the monetary authorities will budge on their current FX policy stance, either willingly or, as observed during the 2016 financial crises, involuntarily. Clearly, the CBN's dogged conditions for devaluation (external reserves below $30 billion and Brent crude oil price below $45/bbl.) suggest that currency re-pricing would only be sought as a last resort in 2020. We also highlight that a recourse to desperate ad-hoc FX measures, akin to those in 2016, could be the clearest pointer and *precursor* of an imminent devaluation in the coming year. We are also of the view that the key risks to currency outlook are a significantly high OMO FPI component of reserves (c.44.4%) and low crude oil reserves contribution of less than 35.0%. The former leaves the country vulnerable to capital flow reversals that could be driven by sudden changes in global financing conditions, fundamental shift in the investment case of the country, and a significantly negative credit rating downgrade. Of the three potential drivers, credit rating downgrade looks the more imminent with both Moody's and Fitch recently placing the country on negative watch. While we note the CBN could "postpone the evil day" by adjusting rates to compensate for the country's worsening risk profile once again, potential impact on government borrowing cost and its own interest expense are likely to place the monetary authorities largely in check. All in, we believe there is a good chance of a slight naira devaluation towards the end of the second half of 2020 and as foreign currency concern intensifies.

Nigerian Fixed Income: A tale of two markets

We expect liquidity injections from OMO maturities that cannot be rolled over to drive a mean 350bps YoY moderation in government bond yield by end of 2020. For bills, we envisage yields bottoming out between 4-5% in H1’20 (vs. 5.8% currently) before a potential reversal. The aforementioned yield moderation is likely to slightly taper in H2’20 on lower maturity inflows and possible change in capital allocation in favour of non-fixed income instruments as negative real yield widens. Elsewhere, the interest rate on OMO, which could remain exclusive to FPIs and banks, is likely to be dictated by external financing conditions, attractiveness of carry trade, and Nigeria’s economic risk profile. Our base case expectation is for yields in the OMO space to remain within +/-50bps of current level, aiding FPI participation as CBN extends liquidity support and ensures the availability of hedge instruments for FPI’s.

Huge system liquidity to paper over “macro cracks”

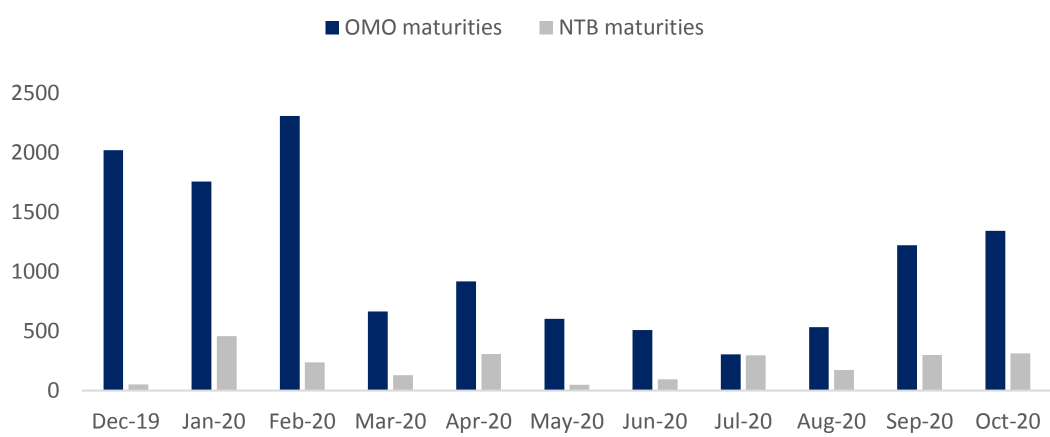
In our view, yields moderation is likely to subsist in the near term despite sustained macro weakness, high inflation, and inadequate fiscal consolidation. Precisely, although higher inflation and wider-than expected fiscal deficit (c.4.0% of GDP in 2020E) should ordinarily have necessitated an upward repricing of government yields, bloated system liquidity level is likely to sustain the current yield moderation. Since the OMO ban, yields on Nigerian T-Bills and bonds have plummeted by 850bps and 313bps respectively compared to an average monthly change of 41 bps and 36 bps in the prior 6 months. The liquidity impact has been pivotal in determining borrowing costs and we expect this effect to continue into the first quarter of 2020 with an additional ₦4.0 trillion worth of OMO bills due to domestic and non-bank corporates maturing. The scheduled size of OMO maturities in 2020 alone is c.2x the projected fiscal deficit for the year, with a potential N1.2 trillion in new pension contribution likely to further magnify the liquidity glut. We believe the liquidity deluge from maturing OMOs and fresh funds (i.e. FAAC allocations, SMIS refunds etc.) would continue to compete for limited FG debt offering and drive yields down for most of Q1’20. However, we may see this downward trajectory in yields reverse in H2’20 as OMO maturities dry up significantly and domestic fund managers adapt to other high yielding investment options.

How much lower can yields go in 2020?

Nigeria has endured spells of negative real yields on government instruments in the past, with the three-year spell between 2008 and 2010 particularly notable. Within the referenced period, average negative real yield widened to -6.5% from -1.2% as the CBN embraced dovish orientation in response to international monetary easing aimed at combating the global financial crisis. The implied liquidity injection in the domestic market pressured nominal yields lower by as much as 600 bps (to nominal levels of c.3.0% on some tenors) between 2009-2010, before a reversal in 2011 following pressures on *inflation, foreign reserves, and the exchange rate*.

Given that the negative real yield environment is expected to coincide with economic frailties such as rising inflation and weak fiscal position, a few market participants are projecting a reversal in yield trajectory in the coming year. To this point, we note that the downward yield trajectory is primarily liquidity driven as market players continue to price their bids higher in a market where traders are reluctant to sell. While we expect further inflows into government treasuries as investors continue to rotate out of OMO instruments in the more immediate term, we expect to see a reversal of downward yield pressures between Q2’20 and Q3’20 as the intensity of OMO maturities tapers and the effect of higher demand for domestic borrowing and inflationary concerns comes to the fore. For context, average maturities over Q2’20 and Q3’20 (₦618 billion) pales in comparison to average OMO inflows of ₦1.5trillion since the OMO ban in October 2019. Specifically, maturities in Q4’19 and Q1’20 were elevated at ₦5.4 trillion and ₦4.7 trillion respectively.

Figure 13: Expected OMO and NTB maturities scheduled till Oct 2020



Source: FMDQ, CardinalStone Research

In addition to expected OMO maturities, our argument in favour of a reversal in yield trajectory is also hinged on expectations that institutional investors would eventually become averse to sustained negative real yield and get more acclimatized to other alternative investments by mid-2020. Indeed, there is precedence showing that Pension Fund Administrators (PFAs) had been comfortable with high equity allocations in prior years (e.g. 14.0% in 2009 and 17.6% in 2010) for example. In addition, the provisions of the multi-fund structure allow PFAs to have maximum exposure to variable income securities (such as ordinary shares and collective investment schemes) of 75.0%, 55.0%, and 20.0% for Fund I, Fund II, and Fund III respectively. We appreciate that PFAs’ allocation to other investments is dependent on factors such as economic growth, company performances, and market outlook, but note that the provisions of multi-fund structure and historical precedence of higher allocations to some variable income investments suggest that another asset allocation rejig in favour of alternative investments could be in the offing.

FG is likely to miss its 2020 revenue target and maintain reliance on CBN's backdoor deficit funding. According to the proposed 2020 budget, FG is projecting overall revenue and fiscal deficit at ₦8.4 and ₦2.2 trillion, respectively. In our view, the government is likely to once again miss its revenue target in 2020 largely on overambitious expectations on the non-tax non-oil revenue segment which was forecasted at ₦1.9 trillion (vs. cumulative of ₦1.4 trillion over the last five years[5]). Even though the renegotiated PSC is expected to unlock $1.4 billion (₦428.0 billion), oil license renewals and upward VAT adjustment also likely to contribute to fiscal revenue, we hold the view that the government's overambitious stance on non-tax non-oil revenue is likely to result in revenue underperformance in 2020. We, therefore, project a base case fiscal revenue of ₦5.4 trillion. This, in addition to FG's plan to plug power value chain backlog of ₦1.2 trillion (if undertaken), is likely to drive fiscal deficit to ₦5.1 trillion assuming full budget implementation. Assuming only 80.0% budget implementation in 2020 (consistent with c.82.0% in 2018)—comprising 90.0%, 100.0%, and 75.0% implementation across recurrent, debt service, capital expenditure—fiscal deficit is likely to approximate N3.2 trillion in 2020E. *While this should ordinarily translate to upward pressure on domestic yields, FG's reliance on CBN's backdoor deficit funding is likely to restrict pass-through to market rates.* Potential pass-through to inflation is also largely checked by significantly high effective cash reserve ratio of between 30-40% for most banks as at Dec 2019.

All in, we expect yield moderation of c.350bps from 2019-year end levels in 2020 aided by expected yield reversal in mid-2020.

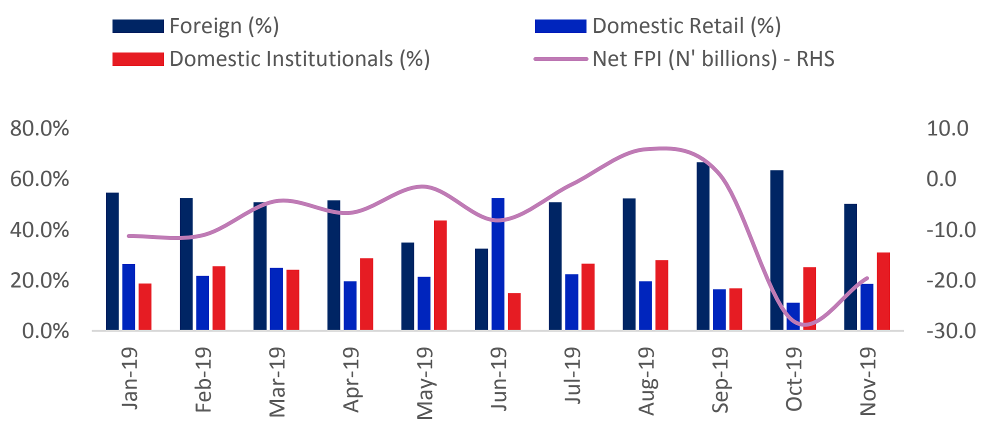
[5] For context, these non-oil non tax items refer to line items such as FGN balances in special levies accounts, FGN share of actual balance in special accounts, signature bonuses/renewals and domestic recoveries) account for 38.6% of non-oil revenue and 25.7% (₦1.8 trillion) of total projected revenue in FY'2020. Prior to Q3'19, these items had only cumulatively generated ₦89 billion, however actual balance in Special Accounts as at 9M'19 jumped to ₦1.3 trillion. This may be a signal of better future performance on these items, but the driver remains unclear.

Rising liquidity levels could drive more flows into equities

Equities market may be set for a first gain in three years in 2020

Monthly data spanning January 2014 to January 2020 suggests that Nigeria's equity market had a 73.4% correlation (R square of 53.9%) with global crude oil price. The market is also impacted by flow of capital, policy changes, corporate restructurings and the pace of liquidity build up, in our view. Aided by improved oil price outlook, we believe changes in the last three drivers could lead the ASI to a second positive return in six years in 2020. Notably, the U.S. Energy Information Administration expects global Brent price to slightly improve to $64.83 per barrel in 2020 (vs. $64.36 in 2019) on expected increase in refinery runs and slight improvement in oil demand outlook. The mild improvement in oil price expectation is, however, unlikely to persuade foreign providers of capital to significantly come into Nigerian equities in 2020 (YTD net foreign portfolio outflow stood at ₦84.5 billion as at November 2019). However, domestic investors are more likely to take advantage of equity opportunities due to the second order effect of the exclusion of domestic non-bank institutions and individuals from OMO activities. Specifically, the policy tweak could continue to result in the re-allocation of some maturing OMO bills to other investment options such as equities, as real yield on fixed income investments become increasingly negative. Thus, although the fundamentals may not be compelling enough to attract FPIs, a bourgeoning system liquidity could provide support for equities in the coming year.

Figure 14: Foreigners are likely to remain net sellers of Nigerian equities



Source: NSE; CardinalStone Research

There could be selected opportunities in some equity names

We believe 2020 could be characterized by major transactions such as acquisitions, recapitalization, and potential listings. We also see legroom for significant balance sheet optimization and policy-induced uplifts from cost reflective tariff and stricter border enforcements. On acquisitions, Seplat may have set the tone with the completion of the acquisition of Eland Oil & Gas Plc (Eland), via cash and new borrowings, in December

2019, with Transcorp also expected to finalise the acquisition of Afam in H1'20. In addition to these, 2020 is also likely to be characterized by business consolidation in the insurance industry as companies race to meet the 31st December 2020 recapitalisation deadline. The new CBN policy restricting domestic non-bank institutions and individuals from participating in OMO market activities is also likely to cascade to some redirection of liquidity to some of these names. Considering expected weighty maturities and the negative real yield environment in the money market (and some bond tenors), investors may seek out opportunities in alternative asset classes, including equities. This view is supported by the inability of the shallow treasury bills market (₦2.7 trillion outstanding as at H1'19, according to Debt Management Office) to absorb the impending liquidity injections. Indeed, the. We highlight that a conservative increase in allocation to equities of 100 - 150bps by PFAs could amount to c. ₦84.6 billion – ₦126.9 billion flows, which represents a potential 2.0% to 2.9% of the free float market capitalization of stocks in the Pension Index (or c. 1.1% to 1.7% of the free float market capitalization of the entire market). Although our assumed allocation increases constitute only small fractions of free float market capitalization, a concentration of demand activities in a few counters may drive rallies in select names.

In line with the largely cautious stance of Nigeria's PFAs, our recent engagements reveal that a few of them have been placing funds in money markets (i.e. fixed deposits) in the hope that the apex bank would reverse the OMO ban rather than go into equities. We believe that this tactic may break if the CBN fails to upturn its decision, while banks re-price interest rates on deposits lower as liquidity builds up. Elsewhere, the apex bank and the FG look likely achieve reduced interest expense pressure and lower cost of borrowing with this OMO policy. In addition, given that it is also an anomaly for non-bank institutions to participate in OMO transactions, the CBN is likely to retain its new policy in the near term and liquidity build up could have some positive pass-through to select equity names in coming months.

Nigerian Banks: Meandering through dark alleys

We posit 2020 will be a reality check for Nigerian banks reflecting CBN's regulatory changes that has raised uncertainties around possibly weaker earnings and asset quality deterioration. Although our view is that Nigerian banks are still in a position of strength from a standpoint of profitability and valuation when compared to their African counterparts, we do believe that the recent fears over the potential impact of CBN's measures, amidst sustained macro weaknesses, remain largely justified. In this section, we assess some of the key themes that will shape the banking sphere in 2020.

Regulatory concerns at the forefront of conversations

In H2'19, the CBN introduced a raft of regulatory changes aimed at spurring the sector. Even though the new measures will positively impact the broader economy, we believe the frequency and unpredictable nature of the policies could be negative for investors' sentiments. Some of the recently introduced measures include:

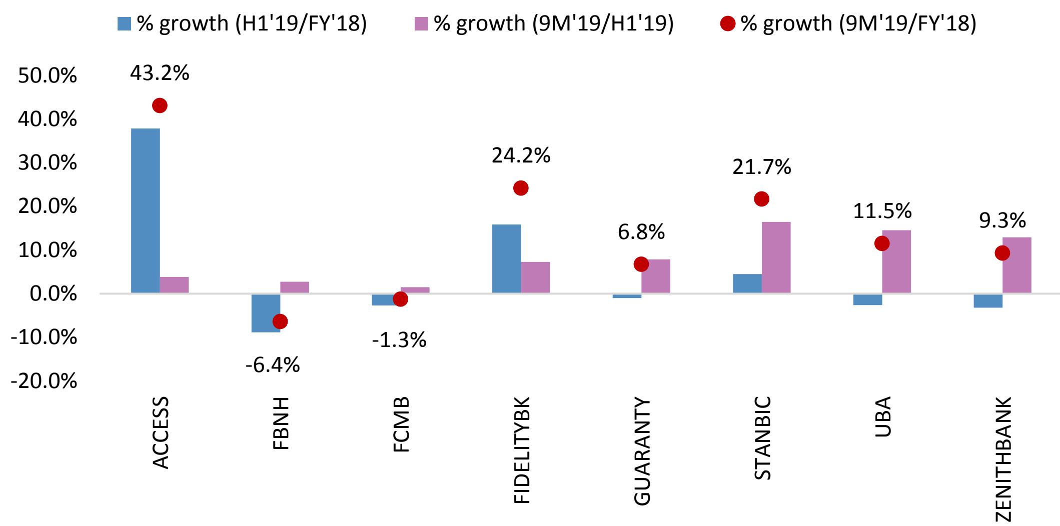
- Introduction of minimum loan to deposit ratio for banks in order to stimulate lending to the real economy (initially at 60.0%, then raised to 65.0%)
- Downward review of the maximum remunerable standing deposit facility (SDF) placement for banks to ₦2 billion from ₦7.5 billion previously
- Restriction of primary and secondary market participation in OMO securities to only banks and Foreign Portfolio Investors (FPIs)
- Review of cashless policy
- Broad review of charges by bank

By FY'20, there is the likelihood of further regulatory announcements with measures such as recapitalization of the banking sector and Basel III implementation already in the works.

Banks will grow loans but at their own pace

Credit to the real economy has dominated banking sector conversations since H2'19 and this discussion is expected to persist through 2020. Clearly, the CBN has conveyed its intent to influence bank lending, imposing a 65.0% minimum loan to deposit ratio (LDR) on banks in the country. While the potential implication of higher LDR on loan growth should ordinarily spur excitement on expected asset yields, a dearth of quality obligors, amidst moderating yields, informs our largely cautious stance. To be clear, therefore, we do not anticipate a significant lending rush by banks to meet the stipulated LDR requirement. In fact, our recent engagements with some banks revealed that a few players would prefer to walk at pace with the framework of their defined risk appetites even though they applaud the motive of CBN's initiative.

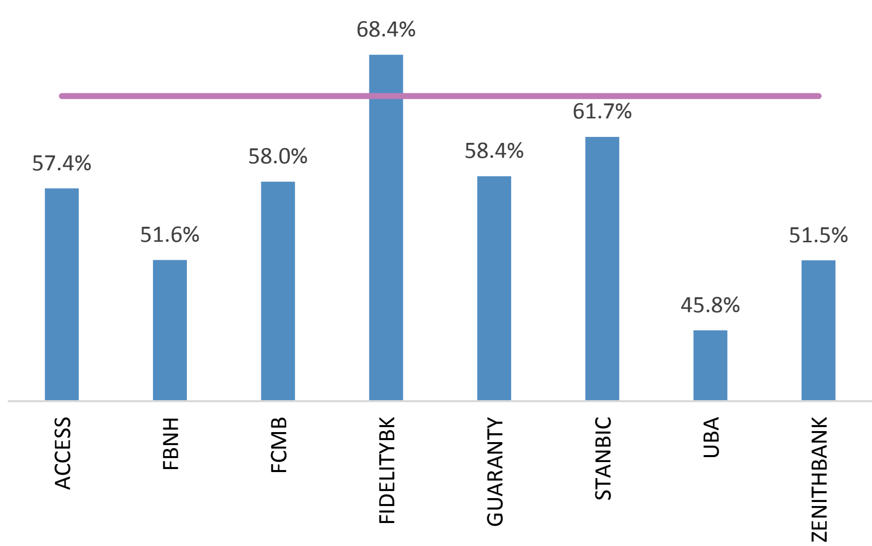
Figure 15: Banks' lending increased following CBN's measures



Source: Corporate filings; CardinalStone Research

Despite banks' communicated intention to remain cautious, we have seen commendable growth in loans since the introduction of the lending measure. Within our banking coverage, STANBIC (+16.4%) was the standout performer from a loan growth perspective between Q2'19 and Q3'19. In absolute terms, UBA (₦256.1 billion) and ZENITHBANK (₦252.8 billion) created the most loans on a group basis. On the flipside, FBNH (-6.4%) and FCMB (-1.3%) still reported contractions in loan that could slightly buttress our view that despite the minimum LDR requirements, banks may still have to play within their risk appetite and available CAR legroom while pursuing asset creation opportunities.

Figure 16: Banks are likely to remain off the LDR mark in the early quarters of FY'20

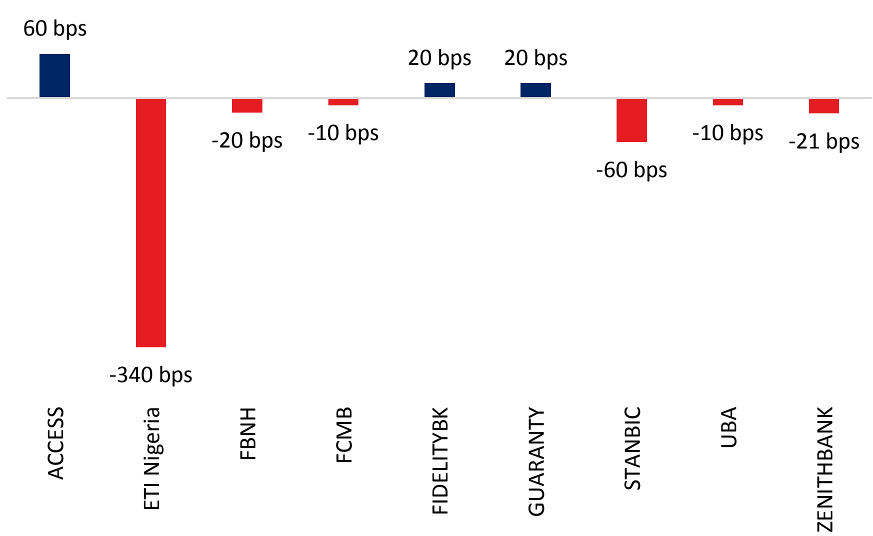


Source: Corporate filings; CardinalStone Research

Moderating yield environment could exact its toll on NIMs

Ex-ETI Nigeria (-340bps), net interest margins (NIMs) moderated by an average of 3bps in 9M'19 (relative to FY'18 levels) across our coverage. Sustained moderation in overall yield environment suggests that NIMs could come under further pressure in FY'20E. Specifically, we anticipate weaker asset yields arising from moderating interest rate on government securities and a fall in lending rates. While banks can continue to invest in higher yielding OMO bills, they could also be forced to reduce asset allocation to treasuries given CBN's latest pronouncement, revealing that banks' LDR compliance would now be assessed on the basis of average daily figures as opposed to the quarter end balances previously applied. This could mean that banks would have to intentionally seek out credit creation opportunities or risk forfeiture of funds to the CBN as additional CRR. Although there appears to be prospect for lower funding cost—from plunging term deposit rates—which could possibly ease the pressure on NIMs, we expect the pull from asset yields to be weightier and more consequential.

Figure 17: Changes in total cost of funds (9M'19 vs. FY'18)

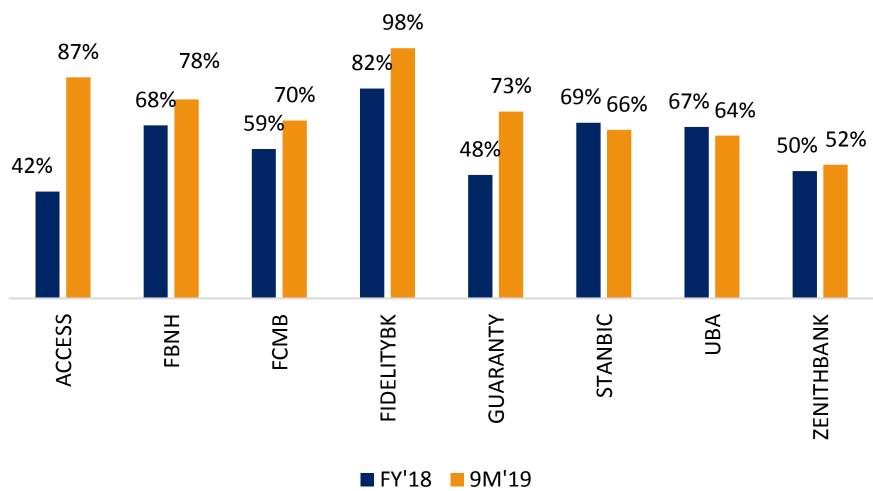


Source: Corporate filings; CardinalStone Research

NIR challenge accentuates banks' worries

Owing to growing concerns over moderating asset yields in 2020, we had expected banks to boost fee-based income in order to cushion the impact on bottom line. However, that expectation is dampened by the recent broad review of banks' fees by the CBN, which holds downward implications for earnings in our view. We note the improvements in fee-based income generation, which as at 9M'19 accounted for an average of 58.9% of total non-interest revenue (NIR) across our coverage (vs. 52.8% in FY'18 and 49.0% in FY'17). Adjustments for non-recurring gains is likely to increase the contribution of fee-based income to about 73.7% (vs 60.8% in FY'18 and 56.9% as at FY'17) on average. Clearly, this strong reliance on fee-based income suggests that banks are likely to be worried about the potential impact of the recent downward review of fees by the CBN. We, however, expect banks to find creative means of offsetting weaknesses in asset yields which may include: 1) Attempting to significantly expand retail footprint in order to propel transaction volumes and potentially offset the impact of lower fees; 2) Banks with strong NIR support from other sources (e.g. Zenith and Stanbic) such as asset trading and wealth management could increase reliance on those sources to ease the pressure on overall NIR; 3) ETI and UBA's strong regional presence offers a diversification advantage that could help offset the impact of the regulatory change. That said, we believe that these possible remedies could take time to bud and, consequently, expect a slowdown in banks' NIR in FY'20E.

Figure 18: Fees contribute significantly to core NIR as suggested by 9M'19 fee to NIR ratio



Source: Corporate filings; CardinalStone Research

Access Bank Plc

NIR slowdown could contrain earnings momentum

We project a 29.2% YoY growth in earnings to ₦122.0 billion in FY'19E (previous: ₦102.8 billion). Our revised earnings expectation reflects stronger asset yields and lower cost of risk than previously anticipated. In FY'20E, however, we project a 7.3% YoY decline in earnings to ₦113.7 billion. Our FY'20E earnings forecast assumes a 6.8% decline in non-interest revenue amid elevated operating costs.

Despite the broad moderation in asset yields, we expect NIM support from declining cost of funds as most of Access's expensive deposits (46.0% of total deposits) are likely to be repriced downward as they mature. Elsewhere, we note that the impact of the bank's retail expansion on fees and commission has not been as momentous as initially thought. In addition, the recent downward review of fees chargeable by banks is likely to compound fee-based income concerns going forward. Consequently, we project a 6.8% YoY decline in non-interest income in FY'20E. This projection also takes into consideration a possible slowdown in loan recoveries and the volatile nature of the bank's derivative trading. We also expect cost to income ratio to remain elevated at 62.0%, despite the unlikelihood of some integration-related one-off costs in FY'20E.

All-in, our ROE forecast for FY'19E comes in at 22.1%, though this could moderate to 16.9% in FY'20E. Post FY'20E, we anticipate full realization of integration synergies and, hence, forecast ROE at 18.6% in FY'22E. Upside risks to ROE expectations are stronger than expected trading income and lower cost to income.

Valuation

Adjustments to our estimates translate to an increase in our 12-month Target Price (TP) to ₦11.97. Our TP implies a potential upside of 19.1% relative to our reference price of ₦10.05. We retain our **BUY** recommendation on the stock.

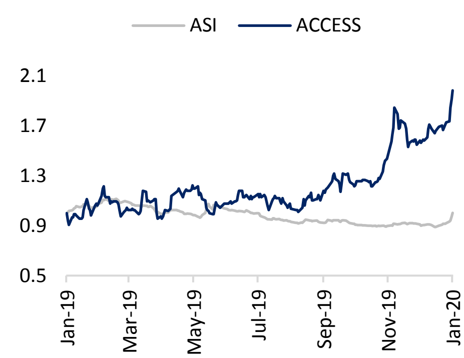
BUY	**TP: ₦11.97**

Stock Data	
Bloomberg Ticker:	ACCESS:NL
Market Price* (₦)	10.05
Shares Outs (Bn)	35.55
Market cap (₦'bn)	357.28

Price Performance	**ACCESS**	**NSE**
12-month (%)	79.5	-4.2
3-month (%)	36.7	11.7
YTD (%)	0.5	9.7

Valuation	**2018A**	**2019F**	**2020F**
P/E (x)	3.1	2.9	3.2
P/B (x)	0.6	0.6	0.5
Div. Yield (%)	7.5	6.0	6.5

1-year price performance (rebased)



Financial Summary	**2018A**	**2019E**	**2020F**	**2018A**	**2019E**	**2020F**
		N'Mn			**$'Mn**	
Net interest income	173,578	283,151	293,830	482	787	816
Non-interest revenue	138,229	135,313	126,112	384	376	350
Loan loss provisions	(14,657)	(18,111)	(25,839)	(41)	(50)	(72)
Profit after tax	94,981	122,588	113,678	264	341	316
Gross loans to customers	2,081,771	3,018,568	3,229,868	5,783	8,385	8,972
Total assets	4,954,157	6,489,946	6,684,644	13,762	18,028	18,568
Total liabilities	4,463,645	5,859,362	5,964,047	12,399	16,276	16,567
Shareholders' funds	490,512	630,584	720,597	1,363	1,752	2,002
ROE	19.1%	22.1%	16.9%	19.1%	22.1%	16.9%
ROA	2.1%	2.1%	1.7%	2.1%	2.1%	1.7%

CARDINALSTONE

Ecobank Transnational Incorporated

Broader business propostion is still supportive of ROE

UEMOA: We think that interest earnings could be bolstered by growth in asset base in FY'20E. However, NIR growth is likely to be muted due to central bank induced restrictions on FX. We also project a slowdown in the pace of loan recoveries, which could potentially weigh on ROE for the region.

Nigeria: We expect the weakness in the Nigerian business to persist in FY'20E on concerns over resolution of lingering issues. It is also unclear if ETI will be able to attract required funding to drive asset growth, and we do not anticipate similar level of loan recoveries as recorded in FY'19.

AWA: We see better asset growth prospects which could bode well for bottom line for the region. We also expect sustained NIR growth across trading, cash management, and FX. We are wary, however, of higher cost of risk due to higher loan growth prospects.

CESA: We anticipate moderation in earnings from the region on account of slowdown in NIR growth on easing FX revaluation gains and reduced activities following the BEAC's FX rules. We also see scope for higher cost of risk due to loan growth prospects and a likely slowdown in recoveries. On the flip side, improved credit growth is likely to cushion the impact of any further moderation in NIMs.

All in, while we expect the African businesses to continue to provide support for ETI's ROE, weaker NIR, amidst a likely slow-down in recoveries and client FX trading activities (34.0% of total NIR), could cap scope for earnings growth. Thus, we project a 4.6% YoY decline in earnings in FY'20E (FY'19E: -14.3% YoY).

Valuation

Our estimates suggest a 12-month TP of ₦14.33. Our TP represents a potential upside of 79.1% to our ref price of ₦7.70 (**BUY**).

Financial Summary	2018A	2019E	2020F	2018A	2019E	2020F
		N'Mn			$'Mn	
Net interest income	334,714	262,887	282,249	930	730	784
Non-interest revenue	322,348	293,145	292,233	895	814	812
Loan loss provisions	(95,009)	(43,603)	(50,814)	(264)	(121)	(141)
Profit after tax	118,025	101,181	96,503	328	281	268
Gross loans to customers	3,530,595	3,354,065	3,387,606	9,807	9,317	9,410
Total assets	8,129,591	8,170,239	8,578,750	22,582	22,695	23,830
Total liabilities	7,477,094	7,438,003	7,766,760	20,770	20,661	21,574
Shareholders' funds	652,497	732,235	811,990	1,812	2,034	2,256
ROE	19.2%	17.1%	14.3%	19.2%	17.1%	14.3%
ROA	1.5%	1.2%	1.2%	1.5%	1.2%	1.2%

BUY	TP: ₦14.33
Stock Data	
Bloomberg Ticker:	ETI:NL
Market Price* (₦)	7.70
Shares Outs (Bn)	24.59
Market cap (₦'bn)	189.34

Price Performance	ETI	NSE
12-month (%)	-45.0%	-4.2
3-month (%)	8.5%	11.7
YTD (%)	18.5%	9.7

Valuation	2018A	2019F	2020F
P/E (x)	1.5	2.4	2.4
P/B (x)	0.3	0.3	0.3
Div. Yield (%)	0.0	0.0	0.0

1-year price performance (rebased)

Notes: UEMOA: *Francophone West Africa*. **AWA:** *Anglophone West Africa*. **CESA:** *Central, Eastern and Southern Africa*

FBN Holdings Plc

Heralding a new era

We project a 15.5% YoY growth in PAT to ₦69.0 billion in FY'19E, with legroom for a further 15.0% growth to ₦79.4 billion in FY'20E. Over FY'20 –23E, we forecast a PAT CAGR of 24.2%. The bank's performance is likely to be driven by improvements in cost of risk and cost to income ratios.

We believe that FBNH, constrained by ongoing efforts to ensure a cleaner loan book, will pursue a more cautious approach to lending. Thus, we project a 5.0% YoY loan growth in FY'20E. We also believe FBNH's strong retail franchise could drive funding cost improvement, amidst a general moderation in the yields. More so, we see scope for improvement in efficiency and cost of risk. In our view, it is unlikely that significant expenses incurred in FY'19E, relating to the Group's transformational projects, will re-occur in FY'20E. We, therefore, project FY'20E cost to income at 66.5% compared to 70.0% in FY'19E. This, alongside projected moderation in cost of risk to 2.0% and 1.5% in FY'19E and FY'20E respectively (from 3.5% in FY'18), portends strong earnings upside.

All-in, our ROE forecast for FY'20E comes in at 13.0%, and likely to average 16.5% over our forecast period. We expect NPLs to decline to single digit from FY'19 in line with management's expectation. We also expect CAR to be above 18.0% by FY'20E on the back of earnings capitalization, expected release of c.₦33.8 billion in regulatory risk reserve, and a possible tier II capital raise.

Valuation

We raise our 12-month TP to ₦8.69 (previous: ₦7.74) per share. Our TP reflects an exit P/B multiple of 0.54x. FBNH is currently trading at FY'20E P/B of 0.34x, which is lower than its 5-year average of 0.40x. Our TP represents a potential upside of 15.9% to our ref price of ₦7.50. We retain our **BUY** rating on the counter.

Financial Summary	2018A	2019E	2020E	2018A	2019E	2020E
		N'Mn			$'Mn	
Net interest income	284,168	289,986	271,528	789	806	754
Non-interest revenue	131,714	131,237	116,551	366	365	324
Loan loss provisions	(86,911)	(42,213)	(33,243)	(241)	(117)	(92)
Profit after tax	59,744	69,025	79,365	166	192	220
Gross loans to customers	2,069,286	2,110,672	2,216,205	5,748	5,863	6,156
Total assets	5,568,316	5,735,365	6,022,134	15,468	15,932	16,728
Total liabilities	5,037,669	5,146,048	5,369,324	13,994	14,295	14,915
Shareholders' funds	530,647	589,317	652,809	1,474	1,637	1,813
ROE	9.9%	12.6%	13.0%	9.9%	12.6%	13.0%
ROA	1.1%	1.2%	1.4%	1.1%	1.2%	1.4%

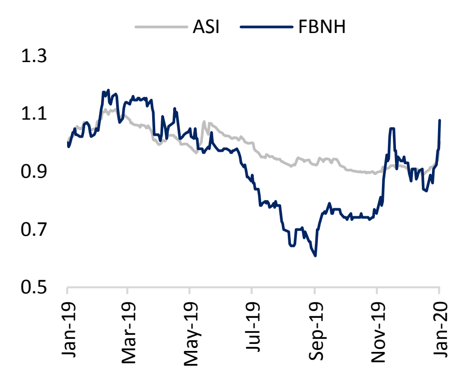
BUY	**TP: ₦8.69**

Stock Data	
Bloomberg Ticker:	FBNH:NL
Market Price* (₦)	7.50
Shares Outs (Bn)	35.55
Market cap (₦'bn)	266.63

Price Performance	**FBNH**	**NSE**
12-month (%)	2.7	-4.2
3-month (%)	41.5	11.7
YTD (%)	22.0	9.7

Valuation	**2018A**	**2019F**	**2020F**
P/E (x)	4.5	3.9	3.4
P/B (x)	0.5	0.5	0.4
Div. Yield (%)	3.5	3.3	4.7

1-year price performance (rebased)



CardinalStone

FCMB Group Plc

Aggressive loan growth could ease earnings pressure

We cut our FY'19E PAT forecast to ₦14.2 billion (-10.6%) reflecting higher cost to income ratio (75.0% in FY'19E vs 70.9% in FY'18) and weaker operating income (-1.8% YoY).

In FY'20E, we forecast a further 13.1% YoY decline in PAT to ₦12.4 billion, weighed by lower net interest income and weaker non-interest revenues. Amidst falling asset yields, we believe an increase in risk asset base could ease the pressure on overall earnings. Given that FCMB has historically leveraged on lending to boost interest income (on average c.70.0% of total interest income are attributable to lending), we see scope for an intentional asset creation drive. Indeed, management has hinted at a more aggressive approach for FY'20 with focus on opportunities in agriculture, renewable energy, consumer finance, as well as digitizing its SME lending products. However, while we assume a 15.0% loan growth, it is our view that falling asset yields could potentially weigh on overall net interest income (-3.8% YoY).

On the non-interest revenue (NIR) front, management has disclosed that it plans to offset the impact of lower e-business related fees through 1) Accelerated digitalization in pursuit of scale; 2) Growth in other NIR sources such as trade services and credit-related fees; 3) Strategic focus in Corporate and Investment Banking (CIB) business, which follows the recent appointment of a new ED for the CIB business. While we view these as positive, we note the non-recurrence of one-off gains like litigation reversals (as at 9M'19) and hence, project a 5.5% decline in NIR. Downside risks are elevated cost to income and cost of risk. All-in, we project FY'20 ROE at 6.3% (FY'19E: 7.6%).

Valuation

Adjustments to our estimates over FY'20-22 reflect a 12-month TP of ₦2.04 (previous: ₦1.80) reflecting an exit PB of 0.20x. We retain our **HOLD** rating on the counter.

Financial Summary	2018A	2019E	2020F	2018A	2019E	2020F
		N'Mn			$'Mn	
Net interest income	72,573	75,654	72,774	202	210	202
Non-interest revenue	39,207	35,974	33,992	109	100	94
Loan loss provisions	(14,113)	(10,526)	(13,720)	(39)	(29)	(38)
Profit after tax	15,141	14,269	12,403	42	40	34
Gross loans to customers	681,326	701,766	807,031	1,893	1,949	2,242
Total assets	1,431,298	1,574,428	1,731,871	3,976	4,373	4,811
Total liabilities	1,247,871	1,382,440	1,532,441	3,466	3,840	4,257
Shareholders' funds	183,427	191,988	199,430	510	533	554
ROE	8.1%	7.6%	6.3%	8.1%	7.6%	6.3%
ROA	1.2%	0.9%	0.8%	1.2%	0.9%	0.8%

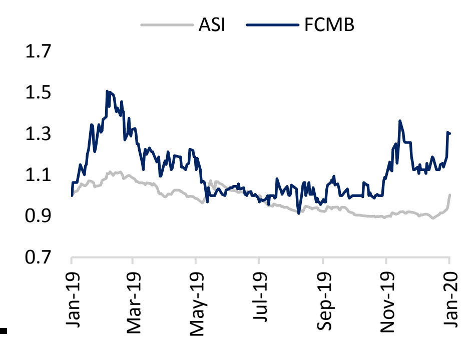
HOLD **TP: ₦2.04**

Stock Data	
Bloomberg Ticker:	FCMB:NL
Market Price* (₦)	1.93
Shares Outs (Bn)	19.80
Market cap (₦'bn)	38.21

Price Performance	FCMB	NSE
12-month (%)	4.9%	-4.2
3-month (%)	20.6%	11.7
YTD (%)	4.3%	9.7

Valuation	2018A	2019F	2020F
P/E (x)	2.5	2.7	3.1
P/B (x)	0.2	0.2	0.2
Div. Yield (%)	7.3	7.3	7.3

1-year price performance (rebased)



Fidelity Bank Plc

Cost pressures could hurdle growth opportunities

We raise our FY'19 PAT projection to N25.1 billion (previous: ₦23.1 billion). Our revised estimates are likely to be driven by stronger asset yields and loan recoveries. In FY'20E, however, we foresee a 13.8% YoY decline in PAT to ₦21.6 billion weighed mostly by higher cost of risk (vs writebacks in FY'19E) and sustained operating expense pressures.

Over the last five years, FIDELITYBK grew loans at a CAGR of 15.4% and, per our estimates, is only one of few banks likely to comply with the CBN's LDR measure. Hence, we do not foresee an aggressive loan growth strategy in FY'20. Instead, it is our view that the bank is more likely to increase asset allocation to OMO bills to offset the impact of lower asset yields partly caused by a fall in lending rates. Hence, we project only a softer fall in interest income (-4.4% YoY) vs our expectation for domestic peers. We also see scope for improvement in the bank's funding cost which, at 6.8%, is the highest among our coverage banks.

On the downside, however, our FY'20E estimates reflect the impact of higher cost of risk and sustained operating cost pressures on earnings. We model a 0.5% cost of risk for FY'20E, in contrast to expected credit writebacks for FY'19E. We also note the challenge posed by higher operating expenses. Over the last 5 years, cost to income has averaged 73.5% and this is forecast to rise to 75.0% in FY'19E before reverting to 73.0% in FY'20E. More so, we expect the downward review of e-business fees and non-recurrence of one-off gains to put some strain on earnings in FY'20E.

All-in, ROE is likely to come in at 12.3% in FY'19E and moderate to 9.7% in FY'20E.

Valuation

Adjustments to our estimates over FY'20-22E reflect a 12-month TP of ₦2.30 (previous: ₦2.16) per share, reflecting an exit PB multiple of 0.29x. Our TP reflects a 2.7% upside to ref price of ₦2.24, hence we rate the counter a **HOLD** (vs. BUY previously).

HOLD	**TP: ₦2.30**

Stock Data	
Bloomberg Ticker:	FIDELITYBK:NL
Market Price* (₦)	2.24
Shares Outs (Bn)	28.96
Market cap (₦'bn)	65.48

Price Performance	FIDELITYBK	NSE
12-month (%)	7.2%	-4.2
3-month (%)	31.8%	11.7
YTD (%)	9.3%	9.7

Valuation	2018A	2019F	2020F
P/E (x)	2.8	2.6	3.0
P/B (x)	0.3	0.3	0.3
Div. Yield (%)	4.9	7.7	6.7

1-year price performance (rebased)

Financial Summary	2018A	2019E	2020F	2018A	2019E	2020F
		N'Mn			$'Mn	
Net interest income	69,587	77,292	76,802	193	215	213
Non-interest revenue	31,845	23,300	21,423	88	65	60
Loan loss provisions	(4,215)	2,267	(2,975)	(12)	6	(8)
Profit after tax	22,926	25,084	21,633	64	70	60
Gross loans to customers	906,623	1,133,279	1,189,943	2,518	3,148	3,305
Total assets	1,719,883	1,805,877	1,896,171	4,777	5,016	5,267
Total liabilities	1,525,467	1,591,394	1,664,381	4,237	4,421	4,623
Shareholders' funds	194,416	214,483	231,790	540	596	644
ROE	11.5%	12.3%	9.7%	11.5%	12.3%	9.7%
ROA	1.5%	1.4%	1.2%	1.5%	1.4%	1.2%

Guaranty Trust Bank Plc

Still primed to deliver value

We revise our FY'19 PAT estimate upwards to ₦192.8 billion (previous: ₦180.5 billion). Our earnings revision reflects impact of stronger loan growth and lower funding cost on overall net interest margin. We also note sustained improvements in operational efficiency and project FY'19E cost to income at 36.5%.

We, however, cautiously forecast a moderation in PAT to ₦175.9 billion (-8.8% YoY) in FY'20E. Despite the potentials for further loan growth and sustained funding cost moderation, NIM is likely to be lower on weaker asset yields. We also assume slight increase in cost of risk to 0.40% (FY'18: 0.36%; FY'19E: 0.25%) on account of stronger lending push, and model cost to income at 38.0% (vs. 36.0% in FY'19E) considering higher inflation expectations for the year. Furthermore, we are wary of the impact of the recent downward revision of fees on overall non-interest revenue (NIR); given that trading gains only account for 14.0% of total NIR. We model a 9.8% YoY decline in NIR in FY'20E. Though, we note that an aggressive retail push and increased transactions volume portends upside risk to our NIR expectations.

All-in, ROE is likely to come in at 32.9% in FY'19E (FY'18: 30.8%) and weaken to 28.4% in FY'20E.

Valuation

Adjustments to our model result in a new 12-month TP of ₦39.14 (previous: ₦41.96). Our TP implies an exit PB multiple of 1.80x. GUARANTY is currently trading at FY'20E PB of 1.50x, which is lower than its 5-year average of 1.72x. Our TP suggests a potential upside of 21.6% relative to our reference price of ₦32.20. We retain a **BUY** rating on the counter.

Financial Summary	2018A	2019E	2020E	2018A	2019E	2020E
		N'Mn			$'Mn	
Net interest income	222,434	228,911	227,375	618	636	632
Non-interest revenue	125,188	134,138	120,927	348	373	336
Loan loss provisions	(4,906)	(3,737)	(6,578)	(14)	(10)	(18)
Profit after tax	184,640	192,779	175,871	513	535	489
Gross loans to customers	1,359,076	1,494,983	1,644,482	3,775	4,153	4,568
Total assets	3,287,343	3,484,583	3,763,350	9,132	9,679	10,454
Total liabilities	2,711,776	2,892,204	3,123,580	7,533	8,034	8,677
Shareholders' funds	575,567	592,379	639,769	1,599	1,645	1,777
ROE	30.8%	32.9%	28.4%	30.8%	32.9%	28.4%
ROA	5.6%	5.7%	4.9%	5.6%	5.7%	4.9%

BUY **TP: ₦39.14**

Stock Data	
Bloomberg Ticker:	GUARANTY:NL
Market Price* (₦)	32.20
Shares Outs (Bn)	29.43
Market cap (₦'bn)	947.65

Price Performance	GUARANTY	NSE
12-month (%)	0.3	-4.2
3-month (%)	22.4	11.7
YTD (%)	8.4	9.7

Valuation	2018A	2019F	2020F
P/E (x)	4.9	4.9	5.4
P/B (x)	1.7	1.6	1.5
Div. Yield (%)	8.4	8.7	8.7

1-year price performance (rebased)

Stanbic IBTC Holdings Plc

Headwinds could restrain earnings growth

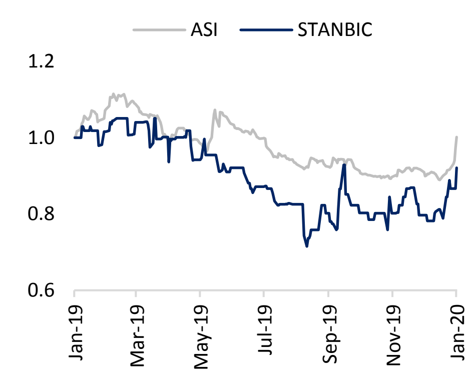
HOLD	TP: ₦47.14

Stock Data	
Bloomberg Ticker:	STANBIC:NL
Market Price* (₦)	42.50
Shares Outs (Bn)	10.51
Market cap (₦'bn)	446.68

Price Performance	STANBIC	NSE
12-month (%)	-9.6%	-4.2
3-month (%)	14.9%	11.7
YTD (%)	3.7%	9.7

Valuation	2018A	2019F	2020F
P/E (x)	6.0	5.9	6.4
P/B (x)	1.8	1.5	1.3

1-year price performance (rebased)



Earnings before tax is likely to grow by 5.5% YoY in FY'19E on improvement in cost to income ratio (-200bps) and growth in non-interest revenue (+7.5% YoY). We, however, see legroom for higher effective tax rate of c.20.0% in FY'19E (vs FY'18 15.6%). According to management, the higher effective tax rate is likely to be driven by the assessment of the banking subsidiary using excess dividend tax basis. Hence, we forecast a flat growth in FY'19E after tax earnings (-0.1% YoY).

We expect earnings to decline by 6.7% YoY in FY'20E, partly weighed by high assumed cost of risk of 0.5%. Specifically, we believe that STANBIC's earnings is unlikely to be supported by credit writebacks, which provided support for earnings in previous quarters. We also anticipate the adverse impact of high inflation on overall expense, notably in the PBB business. More so, while we note the recent improvements in the bank's digital businesses, we believe that its relatively weak market reach could potentially limit volume-induced growth opportunities considering the downward review of fees.

On the upside, however, there could be earnings support from loan growth and lower funding costs as the bank replaces its more expensive deposits with cheaper funding. Stronger AUM growth could also offset the impact of reduced fees while favorable capital market conditions would be positive CIB business.

Valuation

We arrive at a 12-month TP of ₦47.14, which suggests an exit PB of 1.46x which is at a discount to the bank's 5-year average of 1.92x and MEA peer average of 1.87x. Our lower target PB reflects potential ROE reversion over our forecast period on account of muted earnings growth. Our TP represents a potential upside of 10.9% to our reference price of ₦42.50, hence we rate the counter a **HOLD**.

Financial Summary	2018A	2019E	2020F	2018A	2019E	2020F
		N'Mn			$'Mn	
Net interest income	78,209	77,720	77,722	217	216	216
Non-interest revenue	102,604	110,330	104,868	285	306	291
Loan loss provisions	2,940	(1,056)	(2,903)	8	(3)	(8)
Profit after tax	74,440	74,375	69,416	207	207	193
Gross loans to customers	458,946	527,788	580,567	1,275	1,466	1,613
Total assets	1,663,661	1,863,300	2,049,630	4,621	5,176	5,693
Total liabilities	1,423,994	1,563,135	1,704,345	3,956	4,342	4,734
Shareholders' funds	239,667	300,165	345,285	666	834	959
ROE	34.5%	27.6%	21.5%	34.5%	27.6%	21.5%
ROA	4.9%	4.2%	3.5%	4.9%	4.2%	3.5%

United Bank for Africa Plc

Africa-wide strategy yielding gains

We increase our FY'19E after tax earnings forecast to ₦107.7 billion (+37.0% YoY) on projected surge in NIR (+40.7% YoY). Our forecast is likely to be supported by growth in credit, e-products, and transaction related fees and commissions. We also expect earnings to be driven by increased trading income performance, notably on bills and bonds. That said, we project an 11.8% YoY decline in earnings to ₦95.0 billion, which is likely to be driven by higher cost of risk, lower NIM and weaker NIR.

In FY'20, earnings could likely to be supported by moderation in funding costs. We believe the bank's aggressive retail push on the cheap deposit front, in addition to moderating yield environment for its Nigerian operations, could potentially ease funding cost pressures. We expect UBA to continue to expand its risk assets, with significant growth expected in the Nigerian operations. We model a 10.0% YoY growth in loans.

On the downside, however, we see the likelihood of higher cost of risk and cost to income and posit that the duo could potentially weigh on overall earnings. We also project a moderate decline in NIR (-4.7%) for the bank, though we think that the impact of lower revised fees in Nigeria could slightly offset by stronger transaction volumes and e-business growth in other African markets.

All-in, ROE is likely to come in at 20.5% in FY'19E (FY'18: 15.6%) and moderate to 15.9% in FY'20E.

Valuation

Upward revisions to our earnings estimates over FY'20-22E result in a 12-month TP of ₦10.06 (previous: ₦8.68). Our TP reflects an exit PB multiple of 0.53x and a potential upside of 18.4% relative to our reference price of ₦8.50. We retain our **BUY** rating.

Financial Summary	2018A	2019E	2020F	2018A	2019E	2020F
		N'Mn			$'Mn	
Net interest income	205,646	208,966	206,051	571	580	572
Non-interest revenue	102,572	144,312	137,562	285	401	382
Loan loss provisions	(4,529)	(9,941)	(15,309)	(13)	(28)	(43)
Profit after tax	78,607	107,724	94,961	218	299	264
Gross loans to customers	1,807,393	1,988,132	2,186,946	5,021	5,523	6,075
Total assets	4,869,738	5,346,419	5,482,935	13,527	14,851	15,230
Total liabilities	4,367,130	4,769,024	4,839,689	12,131	13,247	13,444
Shareholders' funds	502,608	577,394	643,247	1,396	1,604	1,787
ROE	15.6%	20.5%	15.9%	15.6%	20.5%	15.9%
ROA	1.8%	2.1%	1.8%	1.8%	2.1%	1.8%

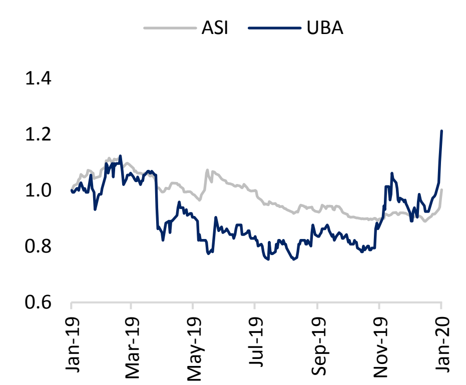
BUY	**TP: ₦10.06**

Stock Data	
Bloomberg Ticker:	UBA:NL
Market Price* (₦)	8.50
Shares Outs (Bn)	34.2
Market cap (₦'bn)	290.7

Price Performance	**UBA**	**NSE**
12-month (%)	17.2%	-4.2
3-month (%)	49.1%	11.7
YTD (%)	18.9%	9.7

Valuation	**2018A**	**2019F**	**2020F**
P/E (x)	3.7	2.7	3.0
P/B (x)	0.6	0.5	0.5
Div. Yield (%)	10.0	11.0	9.7

1-year price performance (rebased)



Zenith Bank Plc

Strong retail push to support earnings

We project a modest 1.5% YoY growth in after tax earnings to ₦196.1 billion in FY'19E, 3.5% higher than our previous forecast. The improved earnings expectation is mostly driven by projected growth in non-interest income (+15.1% YoY). Notably, we expect e-business fees to double to ₦42.4 billion in FY'19E from ₦20.4 billion in FY'18. This is likely to be driven by expected strong growth (+16.4%) in the bank's electronic channel offerings (across cards, POS terminals and ATMs), alongside a forecast 15.8% growth in customer base that is consistent with the bank's recently announced retail push.

We project an 8.0% YoY decrease in earnings to ₦180.5 billion in FY'20E, dragged by expected weakness in NIMs and fall in NIR. We also see scope for higher cost of risk, amidst potential loan growth, and raise our cost to income expectations on higher inflation forecasts. On the one hand, while we expect loan growth and lower funding costs to support net interest income, we believe that the expected fall in asset yields could lead to further depression in NIM. We also believe that the recent downward fee revision by the CBN could restrain the bank's recent strides in fees and commission, following its retail expansion strategies. While we believe that ZENITHBANK's strong trading income prospects could ease the pressure, we maintain a cautious view and project NIR to decline by 11.1%.

All-in, ROE is likely to come in at 23.8% in FY'19E and moderate to 21.2% in FY'20E.

Valuation

We cut our 12-month TP to ₦28.46 (previous: ₦29.13) per share. Our TP reflects an exit PB multiple of 1.02x. ZENITHBANK is currently trading at FY'20E PB of 0.79x, which is lower than its 5-year average of 0.90x. Our TP implies a potential upside of 27.3% relative to our ref price of ₦22.35. We retain our **BUY** rating on the counter.

Financial Summary	2018A	2019E	2020F	2018A	2019E	2020F
		N'Mn			$'Mn	
Net interest income	295,594	287,757	301,681	821	799	838
Non-interest revenue	179,963	207,080	184,042	500	575	511
Loan loss provisions	(18,372)	(26,618)	(32,940)	(51)	(74)	(91)
Profit after tax	193,424	196,092	180,498	537	545	501
Gross loans to customers	2,016,520	2,218,172	2,439,989	5,601	6,162	6,778
Total assets	5,955,710	6,074,824	6,378,565	16,544	16,875	17,718
Total liabilities	5,139,959	5,242,573	5,504,702	14,278	14,563	15,291
Shareholders' funds	815,751	832,251	873,863	2,266	2,312	2,427
ROE	23.8%	23.8%	21.2%	23.8%	23.8%	21.2%
ROA	3.3%	3.3%	2.9%	3.3%	3.3%	2.9%

BUY **TP: ₦28.46**

Stock Data	
Bloomberg Ticker:	ZENITHBANK:NL
Market Price* (₦)	22.35
Shares Outs (Bn)	31.4
Market cap (₦'bn)	701.8

Price Performance	ZENITHBANK	NSE
12-month (%)	2.5	-4.2
3-month (%)	29.6	11.7
YTD (%)	20.2	9.7

Valuation	2018A	2019F	2020F
P/E (x)	3.6	3.6	3.9
P/B (x)	0.9	0.9	0.8
Div. Yield (%)	12.5	12.6	12.5

1-year price performance (rebased)

CardinalStone

Scope for restructuring gains within Consumer Goods

Near-term impact of policy changes to weigh on earnings again

In line with the trend in recent years, Nigeria's consumer goods industry was bedeviled by high unemployment, **consumer down trading**[6], lagged impact of prior devaluations, material cost inflation, and promotional intensity that combined to drag earnings lower in 9M'19. In our view, sustained down trading is driven by the fall in consumer discretionary income, which has increased price sensitivity amongst consumers. Similarly, pressures on the cost front and promotional intensity speak to sustained double-digit inflation in the last four years and cut-throat competition from known and relatively unknown brands, respectively. These drags could largely subsist in 2020 on primary and secondary impacts of proposed increases in electricity tariff, VAT, and excise duties on consumers. We, however, note that a potential offset could come from the ongoing *border enforcement* and its attendant reduction in competition from illegally imported brands. In addition to this, *availability of cheap credit* (particularly to the urban working-class segment) and implementation of *new minimum wage* are upside risks to consumer spending that could slightly ease earnings pressure in 2020.

In the ***brewery sub-segment***, producers were held by the difficulty of transferring the burden of a graduating excise duty to final consumers in 9M'19. *Perhaps encapsulating this brewery market dilemma is the recent admission by producers that beer unit prices have not materially changed in Nigeria since 2013 despite years of double-digit inflation and regulatory-induced charges*. So far, brewers have responded to earnings set-back by expanding product lines, boosting presence in high margin segments, and refinancing expensive debt. In addition, industry leader (NB) has also talked up the option of raising prices to offset pressures from excise duty. Irrespective, we largely expect our coverage names in the brewery space to face a difficult 2020 on weaker consumer income and harsh regulatory environment but note emerging opportunities for further balance sheet restructuring and optimization as interest rate moderates.

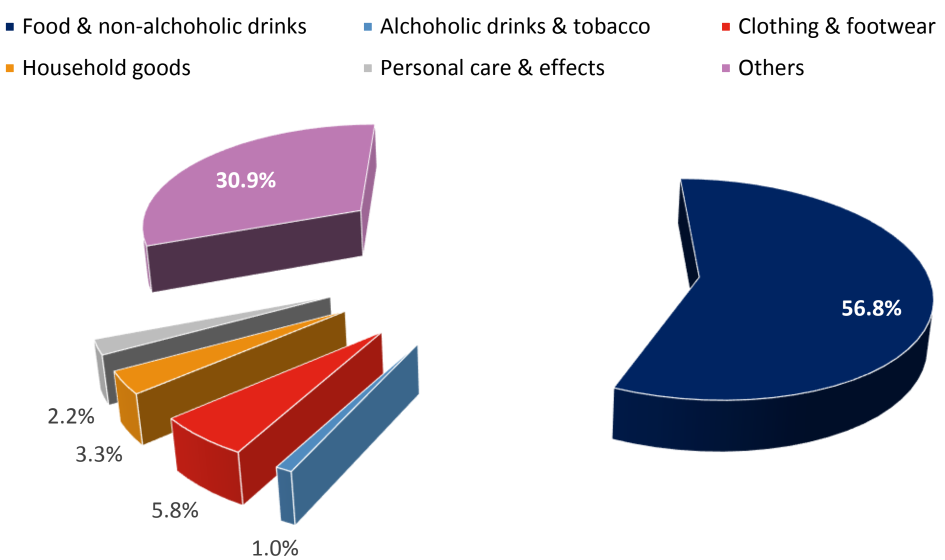
Fast-moving consumer goods companies such as Dangote Sugar and Flour Mills are likely to benefit from stricter border enforcements, in our view. Arguably feeding from the closure, the former has already managed to reverse its H1'19 4.0% YoY contraction in revenue in 9M'19 (+0.5% YoY), though the Apapa traffic situation is yet to be resolved. Similarly, Flour Mills reported a 6.0% YoY growth in H1'19 volumes, with gains noted in the sugar, pasta, and noodles segments. Although management largely pinned these gains on continued focus on quality, B2C channels, and product offerings at the right price points, we believe that the second order effect of the border closure had a hand in the performance as well. Away from the impact of border enforcements, a few companies (Nestle) within the fast-moving consumer goods space could continue to

[6] Even though household consumption could slightly increase in 2020, the benefit is likely to accrue to producers of relatively cheaper and unknown brands due to pressured consumer income

leverage diversity of product lines and price points to bolster topline. Although organic and inorganic top-line growth drivers remain crucial in a market haunted by sustained deterioration in consumers purchasing power, we believe that cost efficiency and proactive balance sheet restructuring will be critical to sector earnings growth in 2020. Given our projection for strong double-digit inflation in the coming year, companies would, therefore, do well to front-load the purchase of storable or non-perishable raw materials in the current year. Similarly, balance sheet restructuring in the mold of debt refinancing, tenor elongation, and a revisit of working capital management strategies could make sense amidst ongoing decline in borrowing costs.

All in, household spending is likely to remain concentrated on essential sub-sectors such as food and non-alcoholic drinks in 2020 as per capita income declines. We also expect pricing, health, and comfort to be critical drivers of consumption allocation in the coming year. Having buttressed our view on the impact of pricing in our analysis of down trading, we now note, in passing, that health and comfort also play key roles in consumption allocation discourse in Nigeria. Clearly, companies like Unilever could continue to contend with health-induced demand for competing products such as Oral B and Sensodyne that could lead to further market share erosion for Close Up. The case for comfort is more relevant in the feminine care space, wherein ultra-pads are considered more comfortable than the relatively economical thick pads.

Figure 19: Breakdown of total household spending (2017 to 2019)



Source: Fitch; CardinalStone Research

Guinness Nigeria Plc

Navigating through competitive waters

We model a 61.1% YoY decline in EPS to ₦0.97 for FY'19/20E. Firstly, we expect sales to moderate by 2.4% to ₦128.3 billion, driven by sustained competition in the local brewery segment. Specifically, harsh economic and competitive environment could continue to depress Satzenbrau sales in the lager segment and offset net sales growth in Malta Guinness, Guinness, and the spirits. Furthermore, we expect the penultimate round of the graduated increase in excise duties to stoke further pressures on bottom-line following management's indication that these additional costs will likely not be transferred to consumers. This suggest further margin erosion in the current year (gross margin – FY'19/20E: 30.0%; FY'18/19: 30.5%). Even though moderating yield environment should ordinarily create legroom for interest expense moderation, negative passthrough from foreign currency exposure is likely to dampen the interest rate impact, especially in the event of devaluation. To this point, we note that the company has already reported a loss on remeasurement of foreign currency balances of ₦527.5 million (+169.5% YoY) that combined with huge reliance on expensive overdraft to drive interest expense to ₦1.3 billion in Q1'19/20 (vs. ₦593.1 million in Q1'18/19).

In addition to a likely contraction in consumer's discretionary income with the 50.0% VAT increase and electricity tariff hike still on the cards. Heightened industry competition and naira devaluation are also key downside risks to our forecast. The current yield moderation leaves legroom for refinancing at lower rates, potentially reducing interest expense pressures going forward.

Valuation

Despite the company's weak operating performance, we believe investors have inordinately sold down on the stock in the last twelve months (Guinness: -57.5%; ASI: -4.2%). Our 12-month TP of N34.19 implies a 13.2% upside to reference market price and HOLD recommendation.

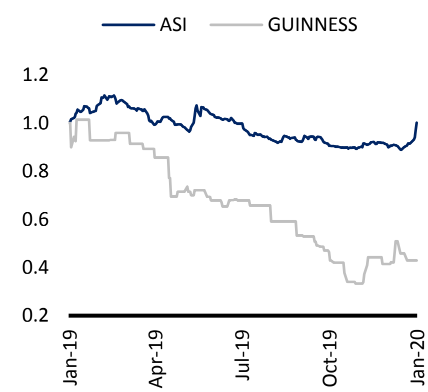
Financial Summary	2019E	2020F	2021F	2019E	2020F	2021F
		(₦'Mn)			(US$'Mn)	
Revenue	131,498	128,348	133,267	365.3	356.5	370.2
EBITDA	17,145	13,764	16,168	47.6	38.2	44.9
EBT	8,966	5,919	8,119	24.9	16.4	22.6
PAT	5,484	2,132	3,539	15.2	5.9	9.8
EBITDA Margin	13.0%	10.7%	12.1%	13.0%	10.7%	12.1%
EBT Margin	6.8%	4.6%	6.1%	6.8%	4.6%	6.1%
Net Profit Margin	4.2%	1.7%	2.7%	4.2%	1.7%	2.7%
Return on Average Assets	3.5%	1.4%	2.4%	3.5%	1.4%	2.4%
Return on Average Equity	8.0%	3.2%	5.6%	8.0%	3.2%	5.6%

HOLD	TP: ₦34.19
Stock Data	
Bloomberg Ticker:	GUINNESS:NL
Market Price* (₦)	30.20
Shares Outs (Mn)	2,190.4
Market cap (₦'Bn)	66.1

Price Performance	GUINNESS	NSE
12-month (%)	-57.5	-4.2
3-month (%)	2.9	11.7
YTD (%)	0.5	9.7

Valuation	2019A	2020F	2021F
P/E (x)	12.1	31.0	18.7
EV/EBITDA (x)	4.7	5.2	4.2
Div. Yield (%)	5.0	2.6	4.3

1-year price performance (rebased)



Dangote Sugar Refinery Plc

Broad macro improvements could support earnings

We project a decline in DANGSUGAR's FY'19E earnings to ₦20.4 billion (-7.4% YoY), largely reflects weaker sugar prices despite expected increase in volume sales. In FY'20E, however, we forecast moderate growth in earnings to ₦21.3 billion (+4.5%), supported by improved top-line growth (12.1% YoY) on higher volume sales and prices.

We forecast a 10.0% rise in sales volume to 720,000MT supported by the recent closure of the country's land borders which we believe could stem the previously unabated flow of cheaper smuggled sugar that had constrained DANGSUGAR's market share. We also expect some improvement in distribution logistics as the government continues efforts to resolve issues surrounding the Apapa gridlock. These, in addition to a likely increase in sugar prices, make case for our top line growth expectations. Notwithstanding, our bottom-line growth expectation is muted owing to concerns about rising global sugar prices. Recent output concerns in big producers like Brazil (about 52% of global production) India and Thailand have raised fears of a global production deficit, causing sugar futures to spike to a two-year high. Our estimates suggest that DANGSUGAR imports c.98.0% of its raw sugar, given slow progress in backward integration projects. Hence, higher import costs could constrain margins—we see limited scope for transmission to selling prices with the company keener on capturing market share, especially in niches where it has long been in the fringes. We also see margin pressures from the recent the 100% increase in import duty rate for raw sugar (from 5% to 10%).

Valuation

We raise our 12-month TP to ₦15.84 (previous: ₦8.68) per share reflecting an exit PE of 8.97x and a potential upside of 8.1% to our ref price of ₦14.65. We retain our HOLD rating on the counter.

FINANCIAL SUMMARY	2019E	2020F	2021F	2019E	2020F	2021F
		(N'Mn)			(US$'Mn)	
Revenue	156,867	175,829	172,172	435.7	488.4	478.3
EBITDA	39,480	43,127	48,048	109.7	119.8	133.5
EBT	31,304	32,700	35,817	87.0	90.8	99.5
PAT	20,348	21,255	23,281	56.5	59.0	64.7
EBITDA Margin	25.2%	24.5%	27.9%	25.2%	24.5%	27.9%
EBT Margin	20.0%	18.6%	20.8%	20.0%	18.6%	20.8%
Net Profit Margin	13.0%	12.1%	13.5%	13.0%	12.1%	13.5%
Return on Average Assets	11.8%	11.6%	12.2%	11.8%	11.6%	12.2%
Return on Average Equity	19.8%	19.0%	18.9%	19.8%	19.0%	18.9%

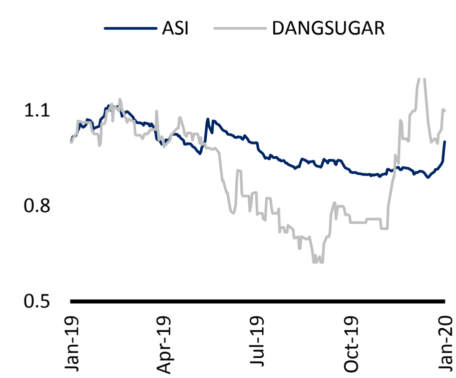
HOLD	TP: ₦15.84

Stock Data	
Bloomberg Ticker:	DANGSUGAR:NL
Market Price* (₦)	14.65
Shares Outs (Bn)	12.0
Market cap (₦'bn)	174.0

Price Performance	DANGSUGAR	NSE
12-month (%)	1.0%	-4.2
3-month (%)	43.6%	11.7
YTD (%)	7.7%	9.7

Valuation	2019E	2020F	2021F
P/E (x)	8.6	8.3	7.6
EV/EBITDA (x)	4.3	3.9	3.5
Div. Yield (%)	7.5	7.5	7.5

1-year price performance (rebased)



UAC of Nigeria Plc

Repositioning for onward growth

UACN is on course to sustain profitability from continuing operations (FY'20E PAT: ₦6.6 billion; 9M'19 PAT: ₦4.7 billion) with strong prospects for a rebound in free cash flow. This follows the reclassifying of UPDC as discontinued operation in preparation for the unbundling of its 64.0% interest in same. Notably, UPDC is also on course to carry out a N15.96 billion capital raises (via rights issue) to pay down its ₦15.84 billion bridge funding from UACN—a material upside risk to UACN from an investing cash inflow standpoint.

Largely aided by sustained gains in Animal Feeds & Other Edibles and Packaged Food & Beverages, we expect post-unbundled UACN to grow gross revenue to N98.0 billion in FY'20E with strong passthrough to operating margins (FY'19E: 7.5%; FY'20E: 8.1%; and operating loss in FY'18). Management has linked ongoing recovery in Animal Feeds & Other Edibles to a rebound in poultry and fish feeds sub segment aided by direct engagement with farmers and second order effect of border closures. Similarly, traction in the Packaged Food & Beverages could also be supported by a ramp up in investments in branding, selling and distribution in Q4'19. Interestingly, both sectors could be key to growing operating margins for the group, with management highlighting plans to improve raw material procurement efficiency in Animal Feeds and overall operational efficiency in Packaged Food & Beverages. Broadly, the transfer of UPDC-associated debt off the books of UACN is also likely to reduce finance expense pressure in FY'20E (-54.7% YoY to 218.9 million) with potentials for little or no impairment charge also in the offing in coming years. We view volatility in wheat, maize, and soya beans prices due to seasonal trends and production concerns as key risks that could impact margins. Given the absence of a commodity exchange in the country, the Group does not hedge these risks.

Valuation: We arrive at our TP of ₦13.66 adopting a blended valuation methodology that assigned a 40.0% weight to discounted cash flow and 30.0% to PE and EV/EBITDA relative valuation approaches apiece. UACN is trading at FY'20E PE of 4.8x compared to 5.8x for selected Bloomberg peers. We re-initiate with a **BUY** rating.

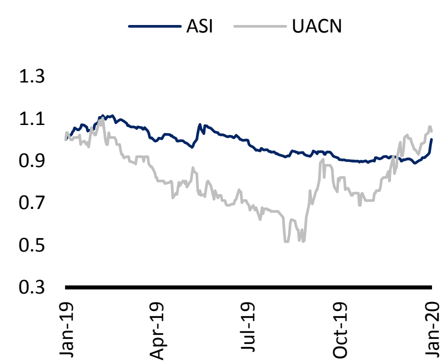
BUY	TP: 13.66

Stock Data	
Bloomberg Ticker:	UACN:NL
Market Price* (₦)	10.55
Shares Outs (Mn)	2,190.4
Market cap (₦'Bn)	30.4

Price Performance	UACN	NSE
12-month (%)	18.5	- 4.2
3-month (%)	62.3	11.7
YTD (%)	22.7	9.7

Valuation	2019E	2020F	2021F
P/E (x)	4.9	4.6	4.5
EV/EBITDA (x)	5.5	4.7	4.4
Div. Yield (%)	5.9	6.2	6.4

1-year price performance (rebased)



FINANCIAL SUMMARY	2019E	2020F	2021F	2019E	2020F	2021F
		(N'Mn)			(US$'Mn)	
Revenue	88,220	97,982	102,905	245.1	272.2	285.8
EBITDA	8,668	9,986	10,690	24.1	27.7	29.7
EBT	9,205	9,701	10,038	25.6	26.9	27.9
PAT	6,259	6,596	6,826	17.4	18.3	19.0
EBITDA Margin	9.8%	10.2%	10.4%	9.8%	10.2%	10.4%
EBT Margin	7.5%	8.1%	8.2%	7.5%	8.1%	8.2%
Net Profit Margin	7.1%	6.7%	6.6%	7.1%	6.7%	6.6%
Return on Average Assets	-7.9%	4.4%	4.3%	-7.9%	4.4%	4.3%
Return on Average Equity	-15.6%	7.3%	7.3%	-15.6%	7.3%	7.3%

CARDINALSTONE

Flour Mills Nigeria Plc

Refinancing could support earnings resurgence

We believe the recent border closure/strict enforcement is likely to have a positive impact on FMN's Food business (62.8%% of revenue). According to stakeholders, the negative impact of border closures on rice importation appears to have shifted some demand to alternatives such as pasta (Spaghetti, Macaroni etc.). This slight demand resurgence, and FMN's ongoing effort to drive retail presence for its B-to-C ready to eat products may have partly accounted for the moderation in Food revenue declines to -1.5% YoY in Q2'19/20 (vs. -2.6% YoY in Q1'19/20). We also believe that the border closures could encourage the production of domestic poultry with positive implications for FMN's Animal Feeds business. However, the second order effect of border closures is unlikely to be as material in Sugar (16.6% of revenue), with FMN mostly focused on B-to-B sales. Irrespective, sugar revenue still came in at a decent N20.9 billion in Q2'19/20 (+9.7% YoY) on strong corporate demand. Within the Agro Allied business, strategic procurement of raw materials such as maize and soya (for feeds production), during main harvest periods of November through February, is now being pursued to boost margins (FY'19/20E EBIT margin: +20bps to 6.3%).

Elsewhere, FMN looks set to take advantage of the moderating rate environment, with c.N20 billion bond borrowing already been considered for early 2020. Management is looking to issue at c.100bps premium to government bond yields and could deploy the proceeds to the refinancing of short-term borrowings and plugging of working capital gaps. Notably, the company's previous N20 billion bond programme was executed via three- and five-year securities with coupons at 15.5% and 16.0% respectively. All in, passthrough from debt refinancing efforts and better operating efficiency is likely to cascade to an over two-fold YoY surge in PAT to N10.1 billion in FY'19/20E.

Valuation: We have a ₦25.65 target price that implies a HOLD recommendation on the stock, given our reference price of ₦23.50 per share. FMN is trading at FY'19/20E EV/EBITDA of 4.0x which is largely at par with its 4-year historical average of 4.8x.

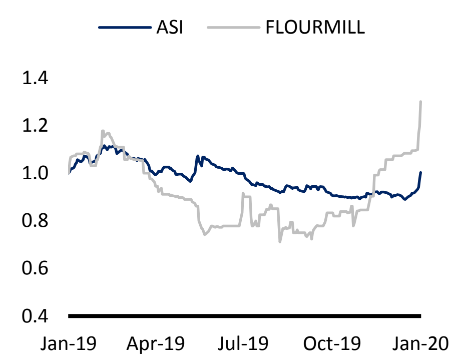
Financial Summary	2019A	2020E	2021F	2019A	2020E	2021F
		(N'Mn)			(US$'Mn)	
Revenue	527,405	532,679	538,005	1,465.0	1,479.7	1,494.5
EBITDA	44,963	50,424	51,785	124.9	140.1	143.8
EBT	9,846	13,420	18,357	27.4	37.3	51.0
PAT	4,000	10,065	12,851	11.1	28.0	35.7
EBITDA Margin	8.53%	9.47%	9.63%	8.53%	9.47%	9.63%
EBT Margin	6.06%	6.27%	6.33%	6.06%	6.27%	6.33%
Net Profit Margin	0.76%	1.89%	2.39%	0.76%	1.89%	2.39%
Return on Average Assets	0.97%	2.38%	2.87%	0.97%	2.38%	2.87%
Return on Average Equity	2.65%	7.03%	9.18%	2.65%	7.03%	9.18%

HOLD	TP: 25.65
Stock Data	
Bloomberg Ticker:	FLOURMILL:NL
Market Price* (₦)	23.5
Shares Outs (Mn)	4,100.4
Market cap (₦'Bn)	96.4

Price Performance	FLOURMILL	NSE
12-month (%)	20.8	-4.2
3-month (%)	55.6	11.7
YTD (%)	19.3	9.7

Valuation	2019E	2020F	2021F
P/E (x)	23.5	9.4	8.1
EV/EBITDA (x)	4.8	4.3	4.2
Div. Yield (%)	5.1	3.2	4.0

1-year price performance (rebased)



Nestle Nigeria Plc

Strongly positioned to sustain growth

We project a 12.0% YoY growth in earnings, supported by improving operating efficiency (EBIT margin: FY'18 22.5%; FY'19E 25.4%) and lower cost to sales (FY'18 57.2%; FY'19E 55.0%). In FY'20E, we see further scope for earnings growth to N56.7 billion, on the back of improved top line growth.

In FY'20E, we anticipate broad support for NESTLE's products as a fallout of the recent closure of the country's land borders. While we expect the borders to be reopened at some point in the year, we believe that tighter controls will remain. The disruption of inflow of cheaper substitutes partly makes NESTLE—with its large diversified portfolio of non-discretionary products—a potential winner in the emerging circumstance. We also like the company's strong brand presence and highly developed route-to-market strategies which have, over the years, kept the business afloat amidst macro turbulence, positioning NESTLE as the leader in Nigeria's food space. We expect production efficiency to persist given the company's increasing recourse to local materials. Over 80.0% and 90.0% of raw and packaging materials respectively are sourced locally, according to management. In our view, this limits NESTLE's vulnerability to global commodity price fluctuations, higher food import tariffs and FX risks and supports management's quest for margin expansion. We, however, note higher inflation expectations and consequently forecast flat operating margin at 25.6% for FY'20 (FY'19E: 25.4%).

We expect NESTLE to maintain its consistent improvement in ROE to 97.7% (FY'18 90.4%; FY'19E 95.4%) and strong dividend payouts (c.90% on average in last 5 years).

Valuation

On account of the adjustments to our FY'20 forecasts, we raise our 12-month (TP) to N1651.46 (previous: N1423.81). Our TP reflects an exit P/E of 23.1x and a potential 19.7% upside to ref price of N1380.00. We upgrade the counter to a **BUY**.

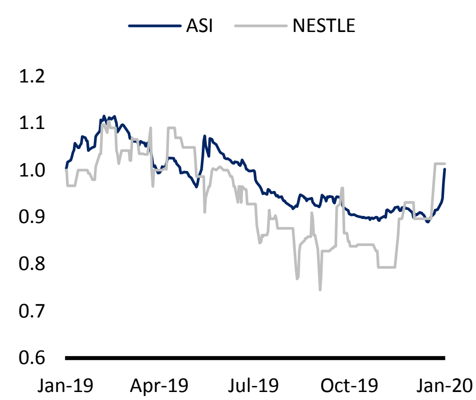
	2019E	2020F	2021F	2019E	2020F	2021F
		(N'Mn)			(US$'Mn)	
Revenue	284,914	319,104	351,014	791.43	886.40	975.04
EBITDA	80,556	91,180	99,464	223.77	253.28	276.29
EBT	71,865	81,038	88,164	199.62	225.11	244.90
PAT	50,305	56,727	61,715	139.74	157.57	171.43
EBITDA Margin	28.27%	28.57%	28.34%	28.27%	28.57%	28.34%
EBT Margin	25.22%	25.40%	25.12%	25.22%	25.40%	25.12%
Net Profit Margin	17.66%	17.78%	17.58%	17.66%	17.78%	17.58%
Return on Average Assets	27.99%	28.56%	28.34%	27.99%	28.56%	28.34%
Return on Average Equity	95.39%	97.66%	96.41%	95.39%	97.66%	96.41%

BUY	TP: ₦1651.46
Stock Data	
Bloomberg Ticker:	NESTLE:NL
Market Price* (₦)	1,380.0
Shares Outs (Mn)	792.7
Market cap (₦'bn)	1,093.9

Price Performance	NESTLE	NSE
12-month (%)	-4.8	-4.2
3-month (%)	13.1	11.7
YTD (%)	-6.1	9.7

Valuation	2019E	2020F	2021F
P/E (x)	21.4	20.6	19.2
EV/EBITDA (x)	14.4	12.8	11.7
Div. Yield (%)	4.7	4.9	5.2

1-year price performance (rebased)



Nigerian Breweries Plc

Moderating finance costs to support earnings

We expect the tough operating environment in the brewery sector to extend into 2020 as consumer discretionary income face further headwinds. As such we forecast modest revenue growth of 2.7%, driven by volume growth and possible price increase to compensate for higher inflationary pressure and the impact of excise duties. We highlight however, that excise duties will not increase in 2020 which should give reprieve to net revenue (-0.2 ppts moderation in COGS margin to 59.0% in 2020F) and provide a competitive edge over GUINESS which produces spirits (excise duty on spirits set for 14% increase in 2020).

NB increased its marketing spend by 11.7% in 9M'19 amid heightened competition and we expect that increase to be sustained in 2020 especially as it seeks to strives to retain its overall market share. Hence, we forecast an increase in SG&A growth of 2.7% to N101.6 billion as NB through increased marketing and advertising to influence consumption patterns. This increase should raise SG&A margin to c.29.4% (vs 27.6% 9M'19), higher than its 5-year average 27.4%. While its marketing spend still lags behind that of INTBEW (c.37% of sales), we expect NB to cap its spend at around 30% due to differing strategies.

We forecast a 5.8% moderation in finance cost to ₦10.9 billion as NB may access lower cost borrowing through its launched ₦100 billion commercial paper program as well as through traditional sources to meet its working capital needs. The moderation should support earnings from 2.0 EPS in FY'19E to 2.6 in FY'20F.

Valuation

We adjust our 12-month target price to ₦66.68, which translates to capital appreciation of 28.3 % and a **BUY** recommendation. Our target price implies an exit P/E multiple of 26.2x, which is a premium to our selected peer average of 21.5x but at a discount to its 5-year average 29.6x.

	2019E	2020F	2021F	2019E	2020F	2021F
		(N'Mn)			(US$'Mn)	
Revenue	329,790	338,541	359,177	909	933	989
EBITDA	69,947	76,037	90,699	193	209	250
EBT	22,086	29,088	44,537	61	80	123
PAT	15,460	20,362	31,176	43	56	86
EBITDA Margin	21.21%	52.40%	60.10%	43.40%	52.40%	60.10%
EBT Margin	6.70%	8.82%	13.50%	31.60%	42.20%	49.30%
Net Profit Margin	4.69%	6.17%	9.45%	25.90%	34.50%	40.40%
Return on Average Assets	4.34%	6.11%	9.45%	16.80%	26.00%	35.10%
Return on Average Equity	9.18%	11.84%	17.60%	23.70%	36.50%	48.60%

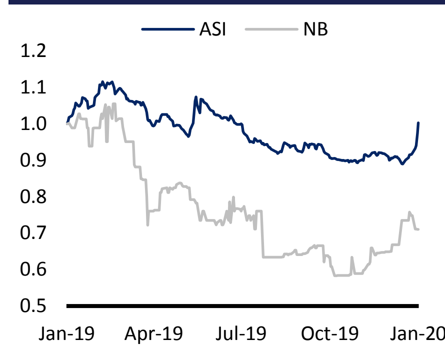
BUY | **TP: 66.68**

Stock Data	
Bloomberg Ticker:	NB:NL
Market Price* (₦)	52.0
Shares Outs (Mn)	7,996.9
Market cap (₦'Bn)	415.8

Price Performance	NB	NSE
12-month (%)	-35.0	-4.16
3-month (%)	12.9	11.7
YTD (%)	-11.9	9.7

Valuation	2019E	2020F	2021F
P/E (x)	26.9	20.4	13.3
EV/EBITDA (x)	6.3	5.9	4.8
Div. Yield (%)	3.7%	4.9%	7.5%

1-year price performance (rebased)

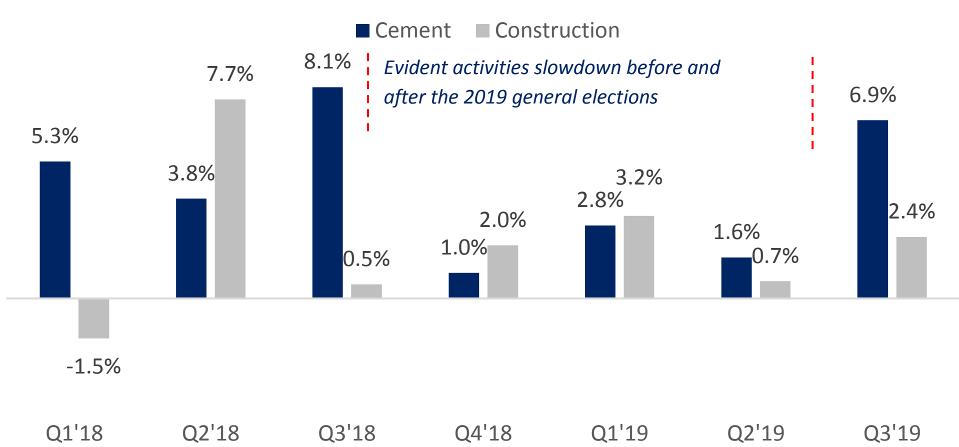


Cement: Interest savings and write backs may define FY'20

Private cement consumption may require greater stimulation

The Nigerian cement market is likely to slightly recover from the flat volume growth reported in FY'19E (c.0.6% YoY) on impact of the low base stoked by election distractions in 2019 with FG likely to match its prior year's monthly CAPEX in 2020. Although consumer discretionary income per capita is projected to remain weak in 2020, the return of private stakeholders to construction after the election-related jitters is likely to support cement output. Elsewhere, FG's proposed CAPEX is likely to be dedicated to projects such as the ₦43.6 billion federal government & social housing schemes, the ₦210 billion construction & rehabilitation of roads, and the ₦67.2 billion counterparty funding allocated to major railway projects. Even though proposed CAPEX is 15.8% lower YoY, we believe FG's decision to go slightly lower on CAPEX speaks to a desire to be more realistic on budget and planning. For evidence, the move makes proposed 2020 CAPEX largely consistent with the annualized May 2019 through December 2019 CAPEX of ₦2.4 trillion. It is pertinent to note that government has only achieved over 70.0% CAPEX implementation in the last six years. This record CAPEX implementation (108.0%), which occurred in 2015, was only achieved because the country adopted a proposed CAPEX that was 70.3% below the last six-year average (2014 – 2019). We believe the swifter passage of 2020 budget is likely to translate to better accuracy, frequency and timeliness of disbursements to earmarked capital projects.

Figure 20: NBS data supports argument of election-related slowdown in cement output

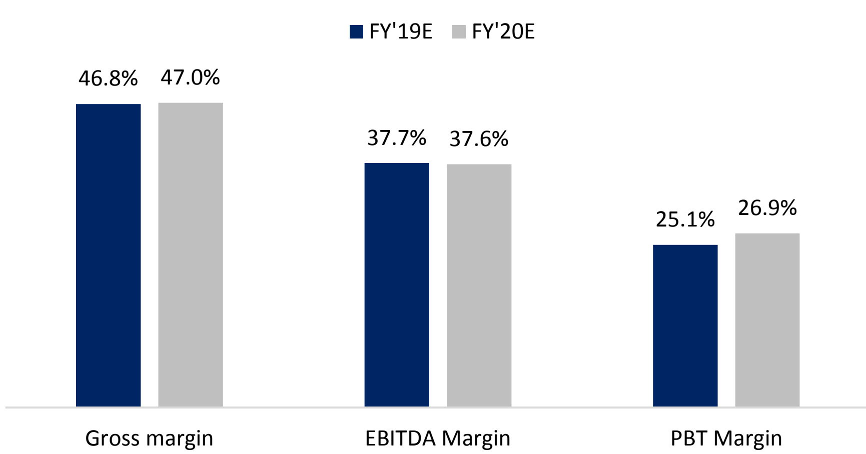


Source: NBS; CardinalStone Research

Cement sector margins are likely to contract slightly in FY'20E. Major cement marketers attributed the tame 9M'19 cement sector growth to abnormal levels of torrential rainfall, which affected private cement consumption (c.75.0% to 80.0% of sector consumption). We, therefore, believe that a tilt to normal rainfall patterns in Southern (March through October) and Northern (May through November) Nigeria could slightly support sector cement consumption in FY'20E (+5.0% YoY). However, we believe a changing competitive landscape, headlined by the merger of all BUA Group's cement concerns and the listing of same under the name "BUA Cement", could sustain the scamper for market share in a thinly growing cement sector in the current year. We also expect prices to remain weak in 2020 as players look to protect market share via promotional efforts such as DANGCEM's "Bag of Goodies" and Lafarge's "Ember Buy and Win" promo of 2019. Elsewhere, rising operating cost could be further spooked by double digit inflation and currency volatility. In our view, these factors suggest that operating margins are likely to be weaker across board in 2020. As highlighted in the macro section of this document, Nigeria faces a significant risk of devaluation in the current year and this is likely to do more harm than good to cement companies, in our view. On this front, we note that cement companies are heavily exposed to FX volatility as gas contracts are invoiced in naira but priced in dollars. In addition to potential pressures from gas pricing, partial reliance on imported coal (BUA's Kalambaina and DANGCEM's Ibese and Obajana) and complete dependence on foreign sourced gypsum are potential drags to operating performance.

We see refinancing opportunities in current declining interest rate environment. With the newly listed BUA Cement having an insignificant proportion of debt in its capital structure, we believe DANGCEM and Lafarge could emerge as the winners on the interest savings in 2020. To this point, we note that Lafarge currently has ₦33.6 billion outstanding bond balance running at a fixed coupon rate of 14.75% and maturing in June 2021. Similarly, DANGCEM has also raised funds via commercial papers at rates between 12.4% and 12.7% and holds ₦89.5 billion outstanding parent company loan running at c.13.0% and maturing in 2020. On balance, we believe interest savings via debt refinancing and tax writebacks can help paper over some cracks created by the increasing difficulty of transferring cost burden to final consumers, occasioned by intensifying competition.

Figure 21: Gross, EBITDA, and PBT margin forecasts of Nigerian Cement Sector



Source: Company financials; CardinalStone Research

Dangote Cement Plc

Tax credits & interest savings to paper over cracks

DANGCEM may be unable to fully transfer cost burden to final consumers on intensifying competition in Nigeria in FY'20E (volume: +4.9% YoY; EBITDA margin: -60bps to 44.0%). However, margins may be supported by interest savings and tax writebacks in FY20E. Away from the domestic operation, we expect Pan African volumes to sustain its growth charge in FY'20E (4.0% YoY), aided by rising demand in Congo, Senegal, and Zambia. This segment is also likely to be supported by the proposed completion of the 1.5MTPA plant construction in Lomé in Q4'20. The Lomé plant is expected to use local clinker and imports from Nigeria to serve its immediate markets (Togo and neighboring countries). Added to this, management has indicated that the company is on the verge of completing the construction of export terminals in Ibese, Lagos, and Onne. These terminals are expected to facilitate clinker exports to grinding plants in Cameroun and other grinding facilities across the group. However, we expect overall volume resurgence to come at the expense of significant operating cost increase stoked by sustained marketing drive, possible devaluation, and rising inflation. Irrespective, the combination of Nigerian interest savings (-24.3% YoY) and tax writebacks is likely to reverse EBT contraction in FY'20E (7.1% YoY to ₦277.5 billion). On potential for interest savings, we note that the company has already embarked on a commercial paper series 13 & 14 issuance in December 2019 at 7.46% discount rate compared to the 12.83% discount rate offered in series 11 & 12 in July 2019.

In our view, a shift away from government's regulatory support (FX proscription and overall ban on cement imports) is the single and most potent risk to medium to long term cement sector outlook. In the immediate term, naira devaluation, surge in inflation, and incessant rainfalls are downside risks to 2020 outlook. We also highlight that some cash flow pressures can be stoked by the company's plan to buy back up to 10.0% of its issued shares – up to c.₦297.5 billion or 4.2x net cash balance as at 9M'19.

Valuation: We retain a **BUY** rating on DANGCEM with a 12-month Target Price (TP) of **₦201.29**. Our TP implies a total return of 24.9%, comprising dividend yield of 8.2% and capital appreciation of 16.7%.

FINANCIAL SUMMARY	2018A	2019E	2020F	2018A	2019E	2020F
		(₦'Mn)			(US$'Mn)	
Revenue	901,213	885,755	927,050	2,503.4	2,460.4	2,575.1
EBITDA	435,261	395,045	408,066	1,209.1	1,097.3	1,133.5
EBT	300,806	259,145	277,479	835.6	719.8	770.8
PAT	390,325	257,850	221,983	1,084.2	716.2	616.6
EBITDA Margin	48.3%	44.6%	44.0%	48.3%	44.6%	44.0%
EBT Margin	33.4%	29.3%	29.9%	33.4%	29.3%	29.9%
Net Profit Margin	43.3%	29.1%	23.9%	43.3%	29.1%	23.9%
Return on Average Assets	23.2%	15.1%	13.1%	23.2%	15.1%	13.1%
Return on Average Equity	44.2%	26.2%	22.9%	44.2%	26.2%	22.9%

BUY	TP: ₦201.29

Stock Data	
Bloomberg Ticker:	DANGCEM:NL
Market Price* (₦)	173.00
Shares Outs (Mn)	17,040.5
Market cap (₦'Bn)	2,944.6

Price Performance	DANGCEM	NSE
12-month (%)	-9.1	-4.2
3-month (%)	20.1	11.7
YTD (%)	21.7	9.7

Valuation	2019E	2020F	2021F
P/E (x)	11.4	13.3	12.3
EV/EBITDA (x)	8.2	7.9	7.4
Div. Yield (%)	8.3	7.2	7.7

1-year price performance (rebased)

Lafarge Africa Plc

Reaping benefits of LSAH sales

Investment consideration: In our view, the sale of Lafarge South Africa Holding (LSAH) was a masterstroke that put Lafarge on track to record a ₦24.5[7] billion net profit in FY'19E—a first profit in three years. As at 9M'19, Lafarge reported a net profit of ₦20.6 billion, bolstered by operating efficiency and lower finance expense. Notably, LSAH was old and expensive to run, contributing c.29.3% to group revenue and accounting for 38.1% of operating cost (ex-depreciation). Thus, its sale, and the mothballing of Sagamu plant (which was also not cost efficient), resulted in a 37.3% YoY contraction in cost of sales and surge in gross margin to 31.4% in 9M'19 (vs. 23.9% in 9M'18). In FY'20E, we project PAT at ₦31.2 billion on sustained gains from the sale of LSAH and mothballing of Sagamu. Cost efficiency is likely to be improved by ongoing $20.0 million investment in coal-utilising captive power plant in Ashaka, which currently has a relatively high cost per tonne. The company is also aiming to reduce variable cost associated with trip turnaround time via extensive engagements with stakeholders across its transport value chain. These initiatives are likely to drive Lafarge's EBITDA margin to 28.5% by FY'20E and 30.2% by FY'23E (vs. 28.4% in FY'19E). Lafarge's net profit (and associated margin) could be supported by lower finance expense and tax credits from UNICEM line 2 in FY'20E.

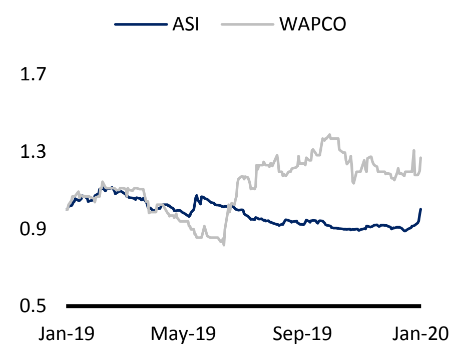
Risk: In our view, a shift away from government's regulatory support (FX proscription and overall ban on cement imports) is the single and most potent risk to medium to long term cement sector outlook. In the immediate term, wider than expected naira devaluation, surge in inflation, and incessant rainfalls are downside risks to FY'20E outlook. We also view price volatility and gas availability as a key earnings risk for Lafarge.

Valuation: Adjustments to our model result in a 12-month Target Price (TP) of ₦23.50 for Lafarge. The stock is trading on FY'20E PE and EV/EBITDA of 9.0x and 4.2x, compared to 19.9x and 11.1x for EMEA peers. Our TP implies an upside of 35.4% to our reference price of N17.35.

BUY	**TP: ₦23.50**
Stock Data	
Bloomberg Ticker:	WAPCO:NL
Market Price* (₦)	17.35
Shares Outs (Mn)	16,107.79
Market cap (₦'Bn)	270.6

Price Performance		**WAPCO**	**NSE**
12-month (%)		33.3	-4.2
3-month (%)		10.9	11.7
YTD (%)		9.8	9.7
Valuation	**2019E**	**2020F**	**2021F**
P/E (x)	2.3	9.0	7.8
EV/EBITDA (x)	4.4	4.2	4.0
Div. Yield (%)	3.1	3.9	4.5

1-year price performance (rebased)



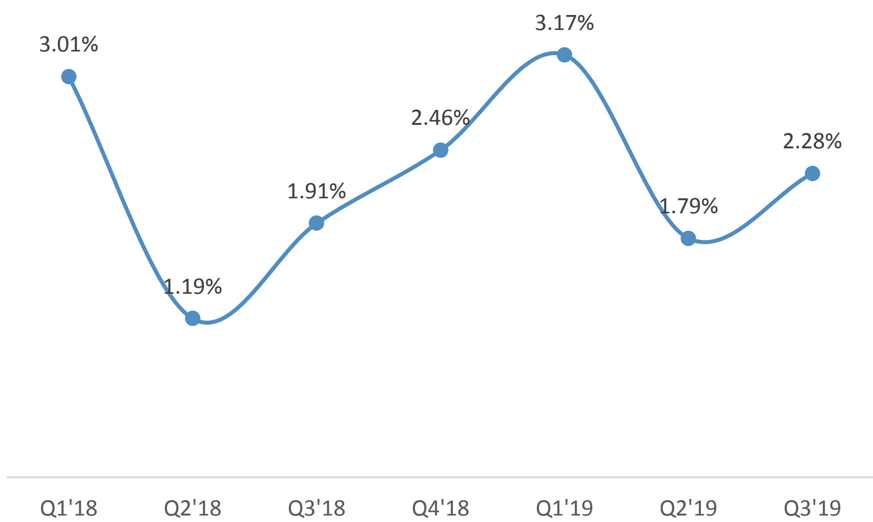
FINANCIAL SUMMARY	2018A	2019E	2020F	2018A	2019E	2020F
		(₦'Mn)			(US$'Mn)	
Revenue	308,425	221,155	228,921	856.7	614.3	635.9
EBITDA	47,594	62,737	65,195	132.2	174.3	181.1
EBT	(19,443)	22,306	34,620	(54.0)	62.0	96.2
PAT	(8,737)	24,537	31,158	(24.3)	68.2	86.5
EBITDA Margin	15.4%	28.4%	28.5%	15.4%	28.4%	28.5%
EBT Margin	-6.3%	10.1%	15.1%	-6.3%	10.1%	15.1%
Net Profit Margin	-2.8%	11.1%	13.6%	-2.8%	11.1%	13.6%
Return on Average Assets	-1.6%	24.1%	6.3%	-1.6%	24.1%	6.3%
Return on Average Equity	-6.0%	52.2%	8.8%	-6.0%	52.2%	8.8%

[7] Excluding profit from discontinued operations

Agriculture sector: Consolidating growth momentum

The agriculture sector remained sluggish in 2019 as the impact of FG interventions through initiatives such as the Anchor Borrowers Program (ABP) were intermittently stifled by incidences of conflict and banditry in food producing regions. Although agriculture GDP grew by 2.28% YoY in Q3:2019, the sector's growth remained well below its 5-year average of 3.5% YoY growth. Notably, the slight recovery in agriculture GDP has coincided with a considerable drop in the number of herders-farmer clashes reported by Armed Conflict Location and Event Data Project (ACLED). Specifically, the agency reported a 67.6% decline in the number of violent attacks involving Fulani militias to 110 in 2019 from 339 in 2018.

Figure 22: Agriculture GDP growth 2018-2019



Source: NBS, CardinalStone Research

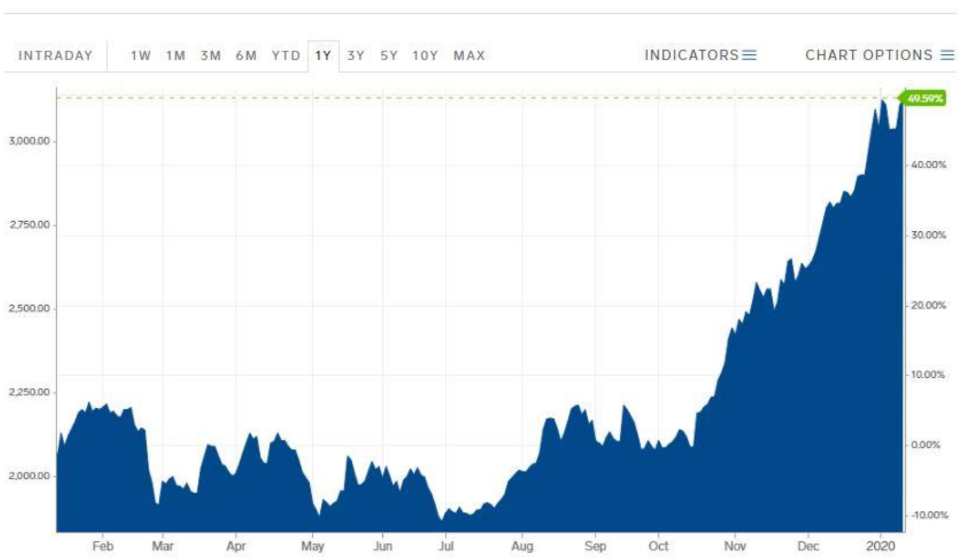
Recent border closure positive for agricultural output – Nigeria completely shut all its land borders with its neighbours in August 2019 in a bid curb the incessant smuggling of goods (such as rice, sugar, vegetable oil etc.) to encourage domestic production. We believe the closure is likely to force neighboring countries to step up border control measures. Indeed, Nigeria has set up a joint border control force with its neighbors (Benin and Niger) to tackle smuggling between the countries. Improved border controls will inevitably favour agricultural producers, however, consumers and manufacturers who procure their inputs through the border may suffer short term price shocks. Following the closure of the borders, food inflation reversed its downward trend, advancing from 13.17% YoY in August to 14.67% YoY in December. Although the CBN expects the inflationary impact to be short lived, we forecast inflation to remain elevated in H1'20. All in, we expect the impact of border closures in combination with existing FG initiatives (such as ABP, Commercial Agricultural Lending Scheme, Agricultural Credit Guarantee Scheme, etc), further reduction in herdsmen clashes, and the recent initiative by the Ministry of Agriculture to offer farming equipment procured by the Ministry to farmers at a 50% discount to drive agriculture growth to 2.9% YoY in 2020 (versus 2019E: 2.6%).

Oil Palm Sector – Ushering in the next growth phase

Reversal of fortunes for CPO prices

The price of crude palm oil (CPO) had been on a steep decline since 2017, averaging c. $638.6 per ton and $586.3 per ton in 2018 and 2019, from $810 per ton at the beginning of 2017. The steep decline in prices was as a result of a supply glut emanating from the two biggest oil palm producers globally and the effect of the price dip was manifest in the performance of the two largest oil palm producers in Nigeria. While PRESCO Plc witnessed a 4.5% YoY decline in CPO turnover in FY'18 (and we forecast another 3.8% dip in FY19E), OKOMU recorded marginal growth of (FY'18: +1.6%YoY; FY19E: +0.5%YoY) despite pushing greater volumes over the periods. However, in recent months, CPO prices have witnessed a complete reversal as the edible oil appreciated by 46.7%, from $522.0 per ton in January 2019 to $777.0 per ton in October 2019. The improvement was driven by expectations of a jump in consumption of biodiesel amid supply concerns. The catalyst has been the Indonesian government's push for program 'B30', a program that requires biofuels to be made using at least 30% of palm oil from 2020.

<u>Figure 23: 1Y CPO price movement (in Malaysian Ringgit)</u>



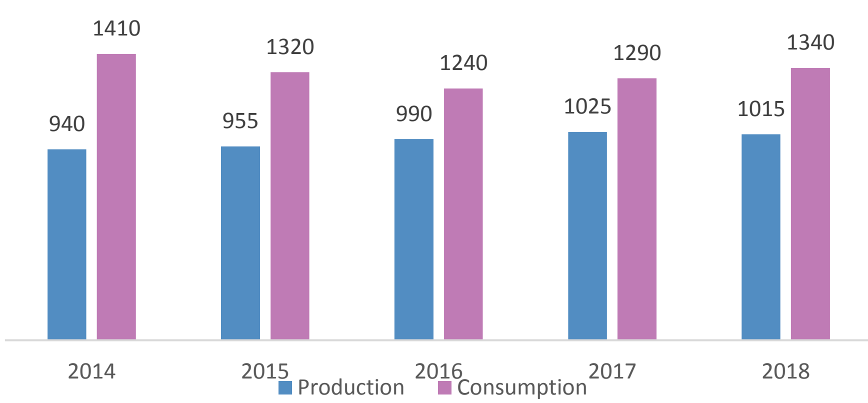
Source: Business Insider, CardinalStone Research

Palm oil mandates have also increased in Malaysia from 7% to 10%, with the possibility of a 20% mandate being implemented in 2020. Compliance with these biofuel mandates will be key for CPO price direction in 2020, as the median estimate in a Bloomberg analysts survey suggests an average price of $650 (2600 ringgit) per ton in 2020, the highest level since 2017. Other than support from biofuel mandates, weaker production and stronger demand from Asia are expected to support prices in 2020. The boost in demand coincides with reduced planting on previous lower price expectations. Additionally, China has increased palm oil imports as domestic soybean crushing has been impacted by the African swine flu. We however believe that the upside for CPO prices may be capped in 2020 as higher prices may dampen demand from major buyers such as India who may begin to seek cheaper alternatives.

New wave of output growth in domestic market: small step towards consolidation?

Although the domestic palm oil industry remains fragmented with small holder farmers accounting for 80% of oil production, ambitious expansion in the two largest producers (OKOMU and PRESCO) may help boost domestic output by over 90,000 tons annually by 2024. While we expect OKOMU to increase CPO output by c. 7,000 MT owing to the 5,000 ha of matured area expected to be harvested from its extension 2 plantation, we similarly envisage an increase of around 9,000 MT of CPO by PRESCO based on greater milling capacity (expected to upgrade milling plant to 90MT/day from 60MT/day) and additional matured area of c. 7,000 ha (mainly from the Sakponba plantation) expected in 2020. We highlight however that even with the jump in local production, Nigeria's production is expected to continually lag consumption by 320,000 MT. The large and rapidly growing population will continue to be a driver of demand in 2020.

Figure 24: Palm oil production vs consumption in Nigeria between 2014-2018 ('000MT)



Source: World Bank, PWC, CardinalStone Research

In addition to the investments by the two big industry players, we may possibly see greater consolidation in the domestic palm industry in the longer term as other big players prepare to join the industry. For instance, in 2018, PZ Cussons International UK and Wilmar International Limited, Singapore invested over $650 million in palm oil plantations and processing facilities, planting almost 26,500 hectares in palm in Cross River state and Dufil Prima (the manufacturer of indomie noodles) recently acquired 17,954 hectares of land in Edo State and 1,040 hectares in Abia. These investments should begin to yield output in the medium term. We view consolidation as a positive in the industry as bigger players are often more efficient in CPO extraction, farm management, energy management (which is a significant cost centre for mid-stream players) and have better storage facilities.

Okomu Oil Palm Company Plc

Prior year harvesting delay may be a fulcrum in 2020

We believe OKOMUOIL is primed to record strong revenue growth in FY'20E, after two consecutive years of muted growth (mean of 1.1% YoY). In our view, FY'20E revenue growth (24.5% YoY) is likely to be supported by increases in CPO output and prices. Output outperformance shall be driven by harvests from over 3,200 more hectares of matured land in FY'20E relative to the harvested area in FY'19E. According to management, last year, the company postponed harvesting in mature areas of its new plantation (Extension 2) to the current year to allow for improved yields and improve the commercial viability of transporting fresh fruit bunches from extension 2 to the main plantation. This output support from Extension 2, which is expected to be a fulcrum for growth in FY'20E, was the result of plantings conducted between FY'16 and FY'17. Another support for revenue is likely to come from improving price outlook for CPO, occasioned by supply concerns, strong Chinese demand, domestic border closures and expected rise in the use of CPO in biofuel. Elsewhere, we believe that a surprise currency depreciation could bolster returns from the 100.0% exported rubber (rubber revenue: 2.01% YoY to ₦3.0 billion in FY'20E). All in, we forecast FY'20E revenue at N26.1 (27.9% YoY) and PAT at ₦8.8 billion (41.7% YoY)—akin to the surge in earnings witnessed in FY'16 and FY'17. RoAE is also likely to increase to 39.4% in FY'20E (FY'19: 33.4%) but average out to 37.5% over our forecast period.

New energy turbine to tame operating costs – OKOMUOIL's recently purchased 5MW turbine is expected to be commissioned in Q1'20. The turbine, which runs on biomass such as empty fruit bunches, may reduce the company's cost of energy in FY'20E. We, however, note that OKOMU may still have to rely more on traditional energy sources during the lean season (June through December) when collection of fresh fruit bunches is traditionally low.

Valuation: We re-initiate coverage on OKOMUOIL with a 12-month TP of ₦87.8 and **BUY** recommendation. OKOMUOIL currently trades at a FY'20E PE of 9.7x compared to a mean of 25.7x for EMEA peers. Our valuation suggests an exit multiple of 15.7x, which is at c.43.1% discount to peer average.

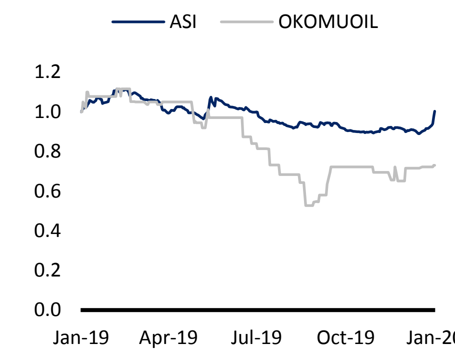
BUY	TP: ₦87.8

Stock Data	
Bloomberg Ticker:	OKOMUOIL:NL
Market Price* (₦)	66.00
Shares Outs (Mn)	953.9
Market cap (₦'Bn)	62.9

Price Performance	OKOMU	NSE
12-month (%)	-16.25	-4.2
3-month (%)	24.6	11.7
YTD (%)	18.71	9.7

Valuation	2019E	2020F	2021F
P/E (x)	12.0	7.15	5.87
EV/EBITDA (x)	6.51	4.21	3.40
Div. Yield (%)	3.0	3.0	5.3

1-year price performance (rebased)



FINANCIAL SUMMARY	2019E	2020F	2021F	2019E	2020F	2021F
		($N'Mn)			(US$'Mn)	
Revenue	20,394	26,083	28,182	56.7	72.5	78.3
EBITDA	8,849	13,675	16,938	24.6	38.0	47.0
EBT	6,411	10,757	13,111	17.8	29.9	36.4
PAT	5,248	8,807	10,734	14.6	24.5	29.8
EBITDA Margin	43.4%	52.4%	60.1%	43.4%	52.4%	60.1%
EBT Margin	31.4%	41.2%	46.5%	31.6%	42.2%	49.3%
Net Profit Margin	25.7%	33.8%	38.1%	25.9%	34.5%	40.4%
Return on Average Assets	12.6%	17.8%	18.7%	16.8%	26.0%	35.1%
Return on Average Equity	17.8%	26.3%	26.5%	23.7%	36.5%	48.6%

Presco Plc

Bold expansion plans to bear first fruit in FY'20

We forecast revenue growth of 15.4% YoY in FY'20E on expected increase in CPO output (FY'19E: 43,918.4MT FY'20F: 53,486.2MT) and stronger price projection (2020F: $700/ton; 2019E: $586/ton). On the former, Presco is likely to leverage its increase in palm oil milling capacity to 90tons/hr in 2020 (compared to 60tons/hr. previously) to accommodate greater harvest from its recently acquired Sakponba Estate (14,400 ha). Exploitation of the estate should also be supported by the 500 tons/day refining expansion works expected to be completed in Q1'20 to bring total capacity to 600 tons/day. Upon completion of this project, Presco is expected to cease partial sale of unrefined CPO and focus on sale of higher margin refined products. We forecast a 27.7% growth in operating profit before revaluation gains to ₦11.8 billion in FY'20E; and an average of 12.5% YoY growth between FY'21E through FY'24.

Lower yield environment positive for borrowing needs - While we expect operating expenses to be largely in line with historical trend (c. 32.0% of revenue), we see scope for a reduction in finance expenses over our forecast horizon. We expect Presco to take advantage of the low interest rate in 2020 to raise more debt for its ongoing expansion projects and refinance some of its expensive debt. To this point, we note that the company was carrying an outstanding debt of ₦13.8 billion with a weighted average interest rate of 14.6% as at 9M'19. In the medium-to-long term, we may see a more even blend between internally generated revenue and debt to fund investment needs.

Valuation

A blended valuation of Free Cash Flow to Equity (FCFE), EV/EBITDA and P/E for the company results in a 12-month target price of N73.67, which implies a capital appreciation of 41.0% and a BUY recommendation. Key risks to our forecasts include adverse fluctuations of international CPO prices, resumption of widespread smuggling of edible oil and its derivatives, and possible delays in expansion project completion.

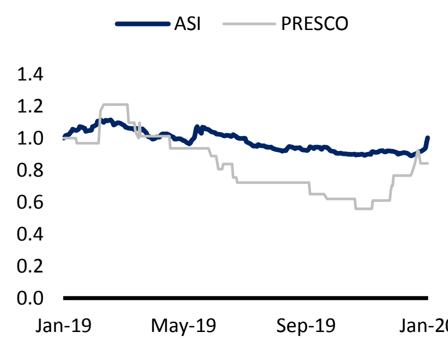
Financial Summary	2019E	2020F	2021F	2019E	2020F	2021F
		(N'Mn)			(US$'Mn)	
Revenue	20,532	23,699	26,981	57.0	65.8	74.9
EBITDA	8,163	11,428	11,872	22.7	31.7	33.0
EBT	6,271	9,050	9,761	17.4	25.1	27.1
PAT	6,335	6,833	7,552	17.6	19.0	21.0
EBITDA Margin	39.8%	48.2%	44.0%	43.4%	52.4%	60.1%
EBT Margin	30.5%	38.2%	36.2%	31.6%	42.2%	49.3%
Net Profit Margin	22.0%	26.7%	25.3%	25.9%	34.5%	40.4%
Return on Average Assets	7.2%	8.7%	8.2%	16.8%	26.0%	35.1%
Return on Average Equity	18.1%	22.7%	21.0%	20.0%	19.9%	20.1%

BUY	TP: ₦73.67
Stock Data	
Bloomberg Ticker:	PRESCO:NL
Market Price* (₦)	52.25
Shares Outs (Mn)	1000.0
Market cap (₦'Bn)	52.25

Price Performance	PRESCO	NSE
12-month (%)	-0.1	-4.2
3-month (%)	35.7	11.7
YTD (%)	10.0	9.7

Valuation	2019E	2020F	2021F
P/E (x)	11.58	8.25	7.65
EV/EBITDA (x)	3.11	2.22	2.14
Div. Yield (%)	3.8	3.8	3.8

1-year price performance (rebased)



Telecoms – Value beyond regulatory uncertainties

We see opportunities for growth in untapped rural markets despite competitive data pricing. According to the National Bureau of Statistics (NBS), approximately 50.0% of the Nigerian population live in rural areas that are currently underpenetrated by mobile voice and data access. The under-penetration in rural areas and broad mobile penetration numbers (81.0%) suggest that there is still scope for significant increase in subscriber numbers in Nigeria. The penetration numbers in other large African markets such as Egypt (93.0%), South Africa (173.0%), and Algeria (122.0%) are all significantly higher than in Nigeria. This view is supported by a projected population growth of c.5.2 million people per annum until 2022 which should translate to a 47.0 million jump in Nigeria's mobile subscriber base by FY'22E, in our view. That said, the market remains competitive as players sustain price wars. In terms of data pricing, Globacom appears to be ahead of the curve (19.3% cheaper than industry mean), followed by Airtel and MTNN. For voice, base prices are not as differentiated even though players embark on occasional promotions to boost market share. In recent times, these promotions have included MTN's Beta Talk and Awuf4U as well as Globalcom's "Yakata Ultra". All in, MTNN remains the market leader by subscriber base, followed by Globacom and Airtel. We, however, observed recent porting activities largely in favour of EMTS, which reported net inflow of 41,888 porting subscribers in 9M'19.

Figure 25: Voice market share across Nigeria's telecoms sector

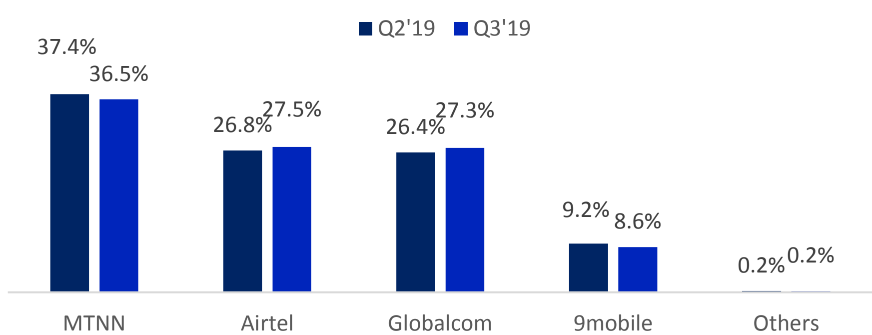
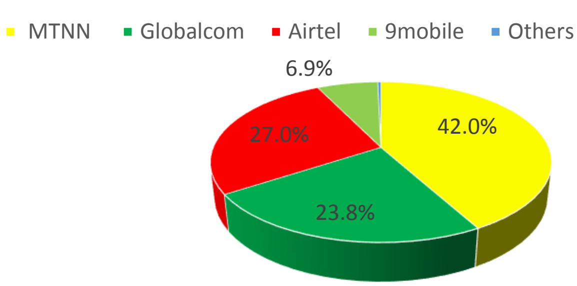


Figure 26: Data market share across Nigeria's telecoms sector



Source: NBS; CardinalStone Research

Harsh regulatory environment may limit scope for earnings growth. Telecom operators have faced stiff regulatory setbacks in recent years. These regulatory concerns range from alleged tax/repatriation protocol violations to price regulations. On price regulation, for example, the Federal Ministry of Communications recently suspended the implementation of the new billing regime (₦4 every 20 seconds) for access to banking services via USSD, which was put forward at the behest of Nigerian banks. The proposed new end-user billing (a scheme where the customer is charged directly for partial payment of USSD) contrasts with previous corporate billing plan, where banks were fully charged instead. A body of bank Chief Executive Officers (CEOs), the CBN and the Nigerian Communications Commission (NCC) have all agreed to meet at the start of 2020 to resolve the current impasse. On other fronts, the likes of MTNN have endured penalties for failure to disconnect unregistered customers and properly follow tax/capital repatriation protocols.

Investments in broadband deployment is likely to slow down in 2020 after 14 states (including Lagos, Kano, Anambra) hiked Right of Way (RoW) charges in January 2020. Specifically, agencies of these states increased RoW from a range of ₦300 – ₦500/meter to ₦3,000 – ₦6,000/meter. This, as well as a lack of proper housing plan, multiple taxation across tiers of governments are likely to cap scope for greater investments in broadband deployment. Notably, telecoms players have also decried the difficulties involved in obtaining RoW for the deployment of fibre optic cables, which was supposed to reduce reliance on microwave transmission that is easily impeded by weather changes and poor house planning.

***Electricity tariff hike may stoke additional cost pressures on Telcos*. The recent tariff hike, which is set to take full effect in April 2020, is expected to increase energy costs for major Mobile Network Operators (MNOs). While major MNOs have outsourced ownership and management of towers and on-site telecoms equipment to third party operators such as Huawei and IHS, we believe we might see renegotiation of current operating & maintenance contracts in 2020 or an upward review of current terms in cases of contract renewal.

The headwinds notwithstanding, we believe the medium-to-long term case for Nigeria's telecoms industry remains compelling. Both demographics and market penetration numbers are the clearest pointers to this. In addition, we believe current moderation in yields provide legroom for moderation in interest expense with market leader MTNN carrying ₦300 billion debt obligation at NIBOR + 1.75% with maturities in 2025 (₦200 billion) and 2026 (₦100 billion).

MTN Nigeria Plc

Unique advantage, stable earnings

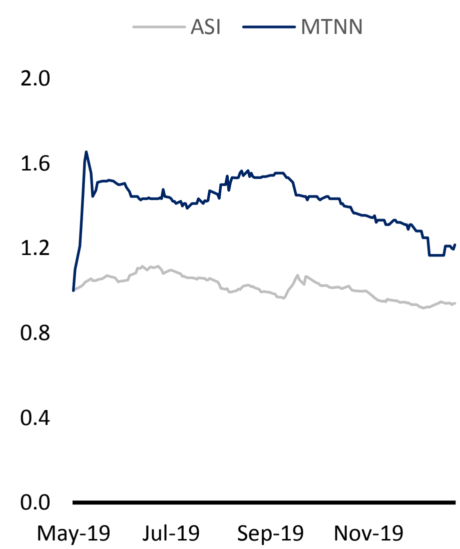
We retain a BUY rating on MTNN with a 12-month Target Price of N148.54. Our valuation is mainly supported by expectations of sustained earnings growth, reduction in interest expense and improvement in operating cashflow, following the complete repayment of the N330 billion fine.

BUY	TP: ₦148.54
Stock Data	
Bloomberg Ticker:	MTNN:NL
Market Price* (₦)	128.50
Shares Outs (Mn)	20,345.51
Market cap (₦'Bn)	2,609.4

Price Performance	MTNN	NSE
12-month (%)	29.5	-4.2
3-month (%)	-0.6	11.7
YTD (%)	22.1	9.7

Valuation	2019E	2020F	2021F
P/E (x)	15.2	12.2	10.7
EV/EBITDA (x)	3.8	3.4	3.1
Div. Yield (%)	5.0	5.8	6.5

1-year price performance (rebased)



Investment case: MTNN remains the market leader in the voice and data segments of Nigeria's telecoms market. As at October 2019, MTNN commanded a leading 36.5% market share in the voice market. In the data segment, MTNN also edges its competitors across all major metrics; fibre infrastructure, geographic spread, and active data subscribers. Along with its peers, the firm is well positioned to take advantage of opportunities in fintech, after launching its MoMo mobile money platform in August 2019. The company is poised to sustain its impressive return to shareholders in FY'19E (ROAE: 84.9%) and FY'20E (ROAE: 90.9%). In arriving at this position, we forecast c.10.0% YoY growth in sales for both FY'19E and FY'20E, aided by average growth projection in voice (+ 8.0% YoY) and data (+23.0% YoY) across both years. Growth traction should be inspired by sustained recovery from subscriber base redefinitions and regulatory-induced slowdown experienced in recent years. Elsewhere, we see legroom for improvements in operating cash flow (OCF) following the completion of the ₦330 billion regulatory fine payments. OCF is likely to increase by 27.6% YoY and 47.7% YoY in FY'19E and FY'20E respectively. Consequently, the company is likely to sustain its dividend policy in coming years (pay-out ratio of 71.4% in FY'19E vs. 80.0% in management forecast).

Risk: Probability of more regulatory fines is the key risks to outlook, even though the c.$2.0 billion tax remittance case was recently called off by the Attorney-General. Heightened competition in the data market and price controls are also key risks to outlook, in our view.

Valuation: We value MTNN at ₦148.54 per share, using a blend of DCF and relative valuation (PE and EV/EBITDA) methodologies. Our target price reflects implies a potential upside of 15.6% to current market price of ₦128.50. We retain a **BUY** rating.

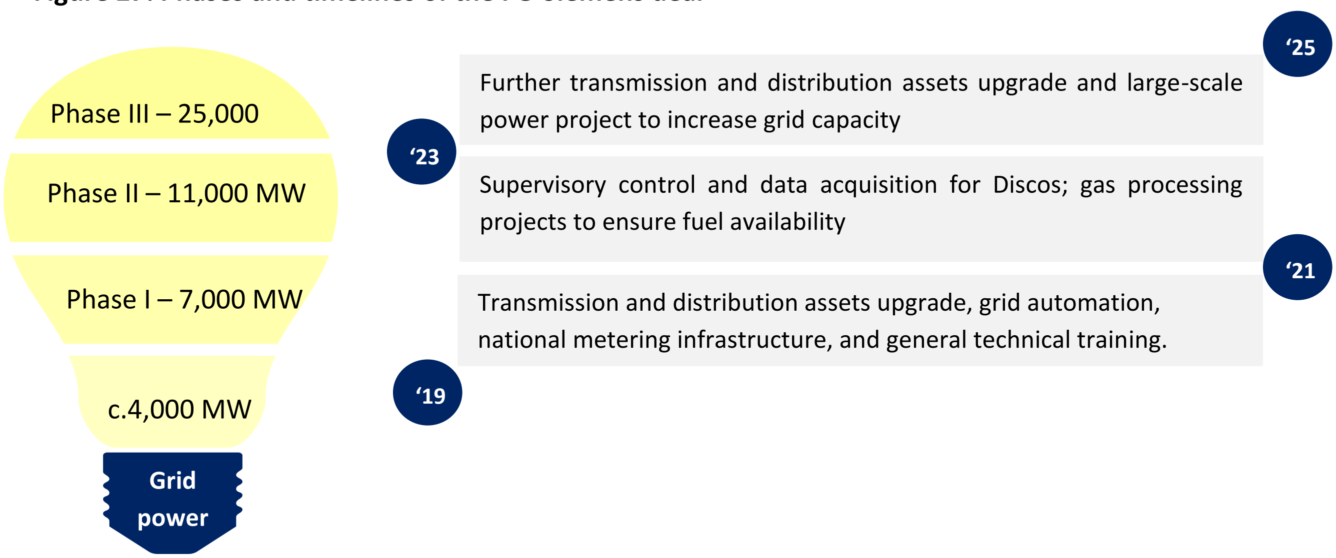
FINANCIAL METRICS	2019E	2020F	2021F	2019E	2020F	2021F
		(₦'Bn)			(US$'Mn)	
Revenue	1,143	1,261	1,380	3,174	3,501	3,832
EBITDA	592	654	716	1,644	1,817	1,989
EBT	253	316	360	702	879	999
PAT	172	215	245	477	598	680
EBITDA Margin	51.8%	51.9%	51.9%	51.8%	51.9%	51.9%
EBT Margin	22.1%	25.1%	26.1%	22.1%	25.1%	26.1%
Net Profit Margin	15.0%	17.1%	17.7%	15.0%	17.1%	17.7%
Return on Average Assets	13.9%	13.7%	14.8%	13.9%	13.7%	14.8%
Return on Average Equity	84.9%	90.9%	71.3%	84.9%	90.9%	71.3%

Energy sector: Private partnerships and reforms are key to outlook

Power: Successful execution of the Siemens deal could be a game changer

The Federal Government and Siemens struck a ₦1.2 trillion six-year, three-phase Nigerian electrification project deal which aims to achieve 25,000 megawatts (MW) of electricity by 2025. The project is expected to cover all three arms of the power value chain, including generation and distribution sub-sectors, which are currently operated by private sector players.

Figure 27: Phases and timelines of the FG-Siemens deal



Source: Federal Ministry of Power; CardinalStone Research

Elsewhere, the board of the African Development Bank (AfDB) approved a $210.0 million loan in favour of government-owned Transmission Company of Nigeria (TCN) in November 2019. The fund is expected to support the upgrade of the nation's dilapidated power lines and distribution infrastructure. The reliability of transmission grids in Kano, Kaduna, Delta, Edo, Anambra, Imo, and Abia are also expected to be improved with proceeds from the project. On completion, associated upgrades are expected to reduce the amount of stranded power and increase the evacuation capacity from the South toward the North, where power supply is limited. Nigeria is also planning to construct a 330KV double circuit quad transmission lines and sub-stations across the country. We believe that completion of this project is likely to improve the grid infrastructure across power sector value chain and lower Aggregate Technical Commercial & Collection (ATC & C) losses.

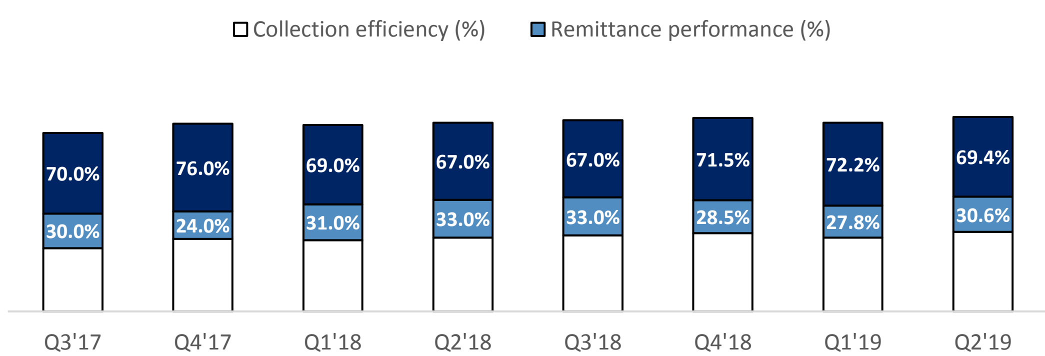
Upward tariff review: a crucial step towards a self-sustaining power sector

The Nigerian Electricity Regulatory Commission (NERC) released a revised MYTO document in August 2019. The document first outlined the over 30.0% increase in electricity tariff which became effective in January 2020. The ultimate drive on this front is achieving full cost reflective tariffs by July 2020. In addition to the communicated adjustments, the FG is expected to remit outstanding tariff shortfall (difference between pegged tariff and cost reflective tariff) between 2015 and 2018 (totaling ₦1.2 trillion) to the Discos. We believe an eventual intervention is likely to improve liquidity for the sector's smooth operational performance. This, as well as plans to fully institute cost reflective tariff by July 2020, could inspire some confidence among intending private investors.

Collection problem is another "kettle of fish" that is yet to be resolved

The Nigerian power sector has been plagued with various systemic problems that range from inadequate generation capacity to poor transmission infrastructure. Perhaps the two biggest challenges of the sector are the lack of cost reflective tariff and weak revenue collection rate of the Discos. While NERC appears to be on course to address the tariff setback, traction on resolving the collection challenge appears to be significantly slow. According to NERC, Discos' revenue collection rate was largely unchanged at 69.0% in Q2'19 compared to the 68.1% recorded in Q4'18, with remittance to the Nigerian Bulk Electricity Trading Plc (NBET) for energy received and service charge by marketing operators is still at a weak 30.6% in Q2'19 (vs. 28.5% in Q4'18). *Collection setbacks have been largely driven by high technical and commercial losses exacerbated by energy theft and consumers' apathy to payments under the widely prevailing practice of estimated billing.* In a bid to correct the collection challenges, NBET has finalized a framework for minimum market remittance threshold that would provide a basis for fair and equitable distribution of market revenues. Importantly, the regulator is aiming to fast-track the roll-out of end user meters by engaging third party investors in financing, procurement, supply, installation, and maintenance of electricity meters.

Figure 28: Discos are struggling to improve remittance to NBET



Source: NBET; CardinalStone Research

In conclusion, power sector inefficiencies have necessitated government interventions through schemes such as the ₦213.4 billion Nigerian Electricity Market Stabilization

Facility (NEMSF), the ₦300 billion Power and Airline Intervention Fund (PAIF), and the ₦701 billion Payment Assurance Guarantee Facility (PAGF).

Upstream Oil & Gas

OPEC+'s agreement to deepen supply cut could support oil prices in Q1'20

In December 2019, OPEC+ agreed to deepen production cut by a further 500,000 barrels to 1.7 million barrels effective Q1'20. This decision followed a report of International Energy Agency (IEA), which projected oil glut for 2020 on higher production expectations from non-OPEC countries. Specifically, IEA estimates non-OPEC supply growth of 2.3 million barrels of oil per day (bopd) in 2020 compared to 1.8 million bopd in 2019. The surge in output growth is expected to be driven by increased production from countries such as the United States, Brazil, Norway and Guyana. IEA's forecast Brent crude price of c.$64.86/barrel (compared to 2019 average of $64.14) is also aided by ongoing geopolitical and trade uncertainties as well as the recently enacted Annex IV of the International Convention for the Prevention of Pollution from Ships (MARPOL Convention), which lowers the maximum sulfur content of marine fuel oil used in ocean-going vessels from 3.5% of weight to 0.5%[8].

On production, we expect domestic crude output to increase by c.100,000 barrels YoY to 2.1 million barrels. The forecast is supported by expected ramp up in output from the 200,000 bpd Egina and other oil fields and OPEC's July 2019 decision to increase Nigeria's output quota to 1.774 million bopd ex-condensate compared to 1.685 million bopd previously. Our output projection still lags FG's target of 2.18 million bopd and Nigeria's capacity of 2.50 million bopd. In addition, we envisage a higher demand for Nigeria's low sulphur Bonny light crude oil in 2020 due to the new Annex IV rule that prohibits ships from using fuels containing more than 0.5% Sulphur from 01 January 2020, compared with erstwhile 3.5% stipulation. However, legacy security concerns in oil producing areas remain the biggest risk to our forecasts. This is despite the strides made by security forces towards neutralizing some threats to oil and gas assets. Latest data from the Nigerian National Petroleum Corporation (NNPC) revealed an 81.0% MoM drop in vandalized pipeline points to 35 in October 2019.

Amended PSC Act could have a mixed impact on upstream oil & gas

The amended Deep Offshore and Inland Basin PSC Act now reflects adjustments to royalty payable on a field basis, mostly for offshore players. The new policy effectively reduces royalty payment for offshore players with 200m-500m depth, while increasing that of players exploring greater depths which are largely operated by IOCs. While the increase in royalties payable for IOCs is logically expected to irk some investors, improved clarity is likely to provide slight reprieve. This stance is supported by stakeholders' early reaction to the bill, with the Managing Director of ExxonMobil in Nigeria, Mr. Paul McGrath, stating that the need of most oil players was mainly policy certainty, which the bill provides for.

[8] Brent blend contains approximately 0.37% of Sulphur, classifying it as sweet crude

According to the latest data release of the National Investment promotion Commission (NIPC), offshore oil & gas investments accounted for 87.7% of total investment announcements in Nigeria in Q3'19, totaling $8.15 billion. This data however preceded the amendment to the Deep Offshore and Inland Basin PSC Act.

Downstream: Oil marketers may face further cost pressures in 2020

Oil marketers may have to endure another calendar year of tight margins in 2020 due to the strict regulations surrounding trading of PMS. Despite persistent calls by downstream stakeholders for a deregulation of PMS pricing, current signs protrude to no deregulation in sight. Further to the current undesirable state for the marketers, they may have to suffer thinner margins from the expected increase in associated shipping costs following the new IMO shipping fuel rule. We believe the new regulation may likely stoke additional pressures on landing costs in 2020E (₦150.9 as at 15 November 2019). Elsewhere, pass-through from infrastructure deficit in power sector is a significant challenge for downstream players. For context, while Nigeria's c.200 million population requires at least 12,000 megawatts of power daily, the country is barely managing 3,500 megawatts to 4,000 megawatts daily. Relying on alternative sources of power has been expensive for downstream players and it appears that the recent c.30.0% hike in electricity tariff and planned tilt to cost reflective tariff in July are likely to increase operating cost pressures on downstream oil and gas players in 2020E. **On a positive note, lubricant businesses are likely to continue to taper the impact of thin margins from PMS on profitability in 2020**. In our view, the size and relevance of domestic lubricants market is also likely to improve in 2020 following the Department of Petroleum Resources (DPR) decision to clamp down on adulterated lubricants, citing the critical negative effects in form of damages to engines and machineries on local consumers. Thus, whilst increases in crude price brings cost pressures, the positive pass-through of DPR's action on volumes is likely to taper potential impact on margins. Across our downstream coverage, lubricant accounted for 15.7% of overall revenue in 9M'19 compared to 15.1% in 9M'18, with related lubricant gross margin improving by 5.1ppts to 24.9% in 9M'19. This lubricant margin is significantly ahead of industry-wide PMS margin of 8.1% and explains why the focus of downstream companies is increasingly shifting to growing their lubricant businesses.

11 Nigeria Plc

Non-core income pivotal to earnings growth

*We upgrade our recommendation on MOBIL to a **BUY** (vs. HOLD previously) with 12-month Target Price of ₦175.14. Despite a largely unfavorable operating turf, MOBIL has strived to retain shareholders value via the diversification of product portfolio and rental income*

MOBIL maintains a diversified income stream, with notable support from rents on large retail stores and a significant real estate portfolio. However, revenue from core operation is expected to grow by only 12.0% YoY and 10.0% YoY in FY'19E and FY'20E a piece, with likely pressures on operating cost in FY'20E. Our FY'20E revenue growth projection is lower than the 5-year average of 18.5% YoY, reflecting slower expansion of retail footprint. That said, increasing presence in lubricant segment is likely to drive gross margin to 8.4% in FY'20E, which is higher than the 8.1% recorded in 9M'19 but significantly lower than the scarcity and partial deregulation induced highs of 17.1% and 16.5% in FY'15 and FY'16, respectively. We believe MOBIL is on course to report a profit of ₦8.3 billion in FY'19E and ₦8.9 billion in FY'20E, with other income from rent expected to account for ₦8.2 billion of profit in both FY'19E and FY'20E. The opportunity to refinance expensive debt in the current declining interest rate environment will also provide some support to earnings.

An upside risk to our forecast is an unlikely deregulation of the downstream sector. We believe a fully deregulated market can offer competitiveness and cost reflective pricing of PMS (c.80.0% of revenues). On the downside, an increase in associated expenses such as shipping, and haulage costs could limit scope for favorable mark ups for downstream marketers.

Valuation:

In line with expectations of sustained weakness in core operating earnings, we revise our 12-month target price slightly lower to ₦175.14 (an 18.4% upside to current market price), considering the expected impact of yield moderation on the cost of short-term borrowing. MOBIL trades at a FY'20E P/E of 6.0x compared to 8.8x for peers. We now have a **BUY** recommendation on the stock

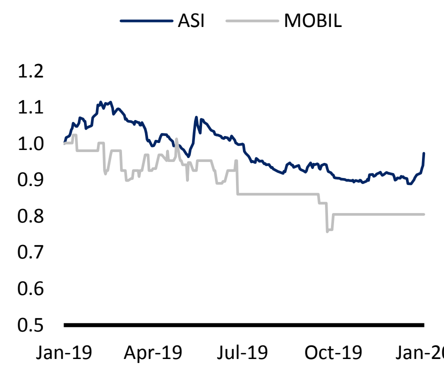
BUY	TP: 175.14

Stock Data	
Bloomberg Ticker:	MOBIL:NL
Market Price* (₦)	147.90
Shares Outs (Mn)	360.6
Market cap (₦'Bn)	53.3

Price Performance	MOBIL	NSE
12-month (%)	-19.4	-4.2
3-month (%)	0.0	11.7
YTD (%)	0.0	9.7

Valuation	2019E	2020F	2021F
P/E (x)	6.4	6.0	5.8
EV/EBITDA (x)	3.2	3.0	2.8
Div. Yield (%)	5.1	5.4	5.7

1-year price performance (rebased)



FINANCIAL SUMMARY	2018A	2019E	2020F	2018A	2019E	2020F
		(₦'Mn)			(US$'Mn)	
Revenue	164,610	184,363	202,799	457.2	512.1	563.3
EBITDA	16,702	16,477	17,552	46.4	45.8	48.8
EBT	13,242	12,436	12,860	36.8	34.5	35.7
PAT	9,329	8,313	8,882	25.9	23.1	24.7
EBT Margin	10.1%	8.9%	8.7%	10.1%	8.9%	8.7%
Net Profit Margin	8.0%	6.7%	6.3%	8.0%	6.7%	6.3%
Return on Average Assets	5.7%	4.5%	4.4%	5.7%	4.5%	4.4%
Return on Average Equity	12.8%	11.0%	10.6%	12.8%	11.0%	10.6%

Forte Oil Plc (Ardova Plc)

New phase, same struggles

We remain cautious on FO even though its new management have expressed a desire to take the company through the harsh operating environment of the downstream sector. We have a SELL recommendation on the stock with a target price of ₦15.88

Investment consideration: Few months after the erstwhile management rolled out its expansion plan, adding 23 retail stations to its armory, the company still struggles to translate more footprint to solid earnings (₦190 million loss in Q3'19). In Q2'19, FO sold its downstream segment in Ghana and its power business to its previous largest shareholder. Even though power was responsible for a large chunk of the business' receivables, it still accounted for 38.2% of the group's gross margin in 2018 (vs. 6.9% for fuels), in view of its huge contribution to revenue. We forecast gross margin at 8.0% in FY'20E (vs 8.5% in FY'19E) to reflect the exclusion of the margin supportive power business after the divestment. However, the restructuring appears to have improved operational efficiency going by the 1.2 ppts drop in SGA to sales ratio to 6.2% in 9M'19 from 7.4% in 9M'18. Overall, we forecast a 65.0% decline in earnings after tax to ₦1.3 billion in FY'20E from ₦5.3 billion in FY'19E, on impact of FY'19E high base, which was bolstered by the one off ₦2.7 billion gain from assets disposal and ₦3.9 billion interest payment on foreign exchange differential claims on PMS importation under the PSF scheme pre-2016. FO has a mean short-term borrowing rate of 18% and we envisage that current moderation in yields could open refinancing opportunities for the company. We forecast a ₦2.1 billion interest savings for the company in FY'20E.

Risk: An unlikely application of brakes to the current PPPRA PMS price regulation offers an upside risk to our estimates. Additionally, further interest payments on subsidy receivables provide added risk pressure to our estimates.

Valuation: We have revised our target price downwards to ₦15.88 on sustained weak operating performance (exclusive of key one off items) in its latest 9M'19 results and have a **SELL** recommendation on the stock

FINANCIAL SUMMARY	2018A	2019E	2020F	2018A	2019E	2020F
		(₦'Mn)			(US$'Mn)	
Revenue	134,704	164,388	174,399	440.2	537.2	569.9
EBITDA	6,051	5,305	1,918	19.8	17.3	6.3
EBT	759	6,622	1,919	2.5	21.6	6.3
PAT	361	5,298	1,285	1.2	17.3	4.2
EBITDA Margin	4.5%	3.2%	1.1%	4.5%	3.2%	1.1%
EBT Margin	0.6%	4.0%	1.1%	0.6%	4.0%	1.1%
Net Profit Margin	0.3%	3.2%	0.7%	0.3%	3.2%	0.7%
Return on Average Assets	0.3%	9.2%	2.3%	0.3%	9.2%	2.3%
Return on Average Equity	1.0%	34.7%	7.5%	1.0%	34.7%	7.5%

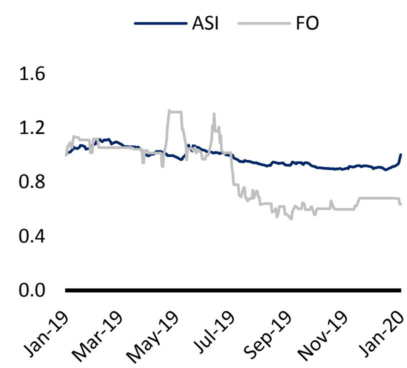
SELL **TP: ₦15.88**

Stock Data	
Bloomberg Ticker:	FO:NL
Market Price* (₦)	20.60
Shares Outs (Mn)	1,302.48
Market cap (₦'Bn)	26.8

Price Performance	FO	NSE
12-month (%)	-31.3	-4.2
3-month (%)	28.8	11.7
YTD (%)	13.8	9.7

Valuation	2019E	2020F	2020F
P/E (x)	4.2	17.1	16.6
EV/EBITDA (x)	3.7	10.2	8.8
Div. Yield (%)	9.7	1.6	2.0

1-year price performance (rebased)



Total Nigeria Plc

No respite in sight amid industry wide challenges

We revise our TOTAL's target price for TOTAL lower to ₦96.55. Our downward review is largely guided by the recent contraction in sales in 9M'19 as well as the sustained tight margins in fuels business. We now have a SELL recommendation on the stock

Investment consideration: TOTAL is poised to record a weak FY'19E operating performance going by the 9M'19 loss that was stoked by operational inefficiency and huge finance cost burden. Earnings pressure stemmed from a technical assistance and management fee (₦2.1 billion) incurred and greater reliance on bank overdraft (85.3% of total borrowings). We forecast FY'19E earnings at ₦184.9 million (-97.7% YoY). For FY'20E, we expect earnings to slightly improve to ₦1.5 billion (aided by the one-off charge in FY'19E) and opportunity for interest savings presented by sustained moderation in interest rate environment. We also forecast FY'20E FCFE at ₦9.1 billion as pressures on Petroleum Equalization Fund (PEF) cap creates scope for increase in receivables and bridging claims. Overall, we believe TOTAL's fuels business (81.9% of total revenues) is negatively impacted by the retail expansion of peers via increased competition. In addition, we attribute the drastic change in fortunes for TOTAL to poor working capital management which has resulted in a significant increase in finance costs.

Risk: An upside risk to our forecast is a full or partial payment of ₦16.9 billion in bridging claims due under the PEF. We recognize the potential positive impact of this on working capital and finance expenses. Deregulation is also an upside risk to our forecast.

Valuation: Adjustments to our model translate to a 12-month TP of ₦96.55 and a **SELL** recommendation on the stock. Our 12-month TP implies a downside potential of 9.0% on last market close. The stock is trading on a FY'20E PE of 24.9x relative to 8.3x for peers.

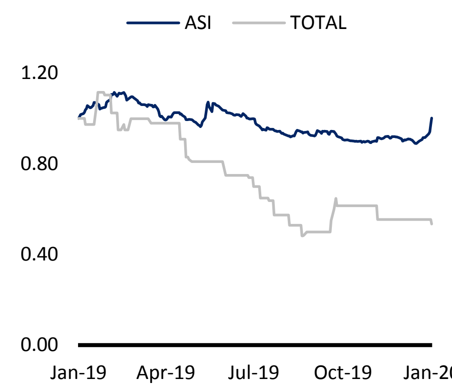
FINANCIAL SUMMARY	2018A	2019E	2020F	2018A	2019E	2020F
		(₦'Mn)			(US$'Mn)	
Revenue	307,988	299,601	305,593	1,006.5	979.1	998.7
EBITDA	13,886	13,431	14,453	45.4	43.9	47.2
EBT	12,098	243	1,917	39.5	0.8	6.3
PAT	7,961	185	1,458	26.0	0.6	4.8
EBITDA Margin	4.5%	4.5%	4.7%	4.5%	4.5%	4.7%
EBT Margin	3.9%	0.1%	0.6%	3.9%	0.1%	0.6%
Net Profit Margin	2.6%	0.1%	0.5%	2.6%	0.1%	0.5%
Return on Average Assets	6.6%	0.1%	1.0%	6.6%	0.1%	1.0%
Return on Average Equity	27.0%	0.7%	5.7%	27.0%	0.7%	5.7%

SELL	TP: ₦96.55
Stock Data	
Bloomberg Ticker:	TOTAL:NL
Market Price* (₦)	107.0
Shares Outs (Mn)	339.52
Market cap (₦'Bn)	36.3

Price Performance	TOTAL	NSE
12-month (%)	-46.6	-4.2
3-month (%)	-13.1	11.7
YTD (%)	3.5	9.7

Valuation	2019E	2020F	2021F
P/E (x)	196.5	24.9	17.4
EV/EBITDA (x)	4.8	4.4	4.3
Div. Yield (%)	0.0	2.7	4.0

1-year price performance (rebased)



Seplat Petroleum Development Company Plc

Organic and inorganic investments to buoy volume induced growth

*Despite projected decline in crude oil price in FY'20E, we retain our **BUY** rating on SEPLAT with a target price of ₦796.90. Our stance is mainly supported by the expected surge in liquids production following the acquisition of Eland Oil and efforts in its recent drilling programs*

BUY **TP: ₦796.90**

Stock Data	
Bloomberg Ticker:	SEPLAT:NL
Market Price* (₦)	588.0
Shares Outs (Mn)	588.44
Market cap (₦'Bn)	346.0

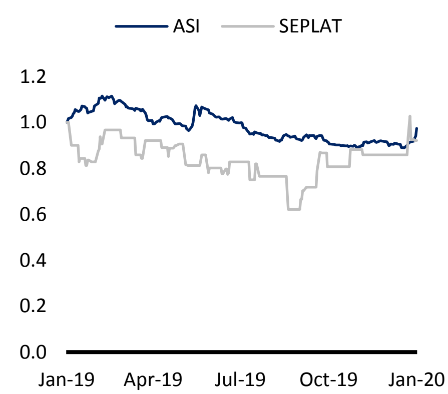
Price Performance	SEPLAT	NSE
12-month (%)	-7.9	-4.2
3-month (%)	14.0	11.7
YTD (%)	-1.4	9.7

Valuation	2019E	2020F	2021F
P/E (x)	5.0	6.4	5.9
EV/EBITDA (x)	1.1	0.9	0.9
Div. Yield (%)	7.8	7.8	7.8

Investment consideration:

We believe SEPLAT is on course to record significant growth in liquids production in FY'20E, following the acquisition of Eland (c.9,948 bopd in H1'19). Specifically, we expect liquid production to increase to 35,808 bopd (vs. 23,658 bopd in 9M'19) in FY'20E while gas production is likely to remain stable at 141.8 MMcf (4.2% YoY). Furthermore, we expect a higher demand for Nigeria's low sulphur Bonny light crude oil in 2020 due to the new rule for Ship fuels. Elsewhere, SEPLAT's diversified revenue base (including gas processing and tolling revenue) also bolsters the investment case of the company. The firm recorded gas tolling revenues of $66.9 million in 9M'19 for processing NPDC's share of the gas extracted from OML 4, 38 and 41 between 2015 to 2018. Following the resolution on the basis for determining the gas tolling fees due from NPDC, we expect to see sustained income on this front going forward. All in, we forecast a PBT growth of 23.6% YoY to ₦86.3 billion in FY'20E.

1-year price performance (rebased)



Risk: Volatility of crude oil price remains the most prominent risk to the business. We also recognize potential downsides from militant activities in the Niger Delta and greater than expected rainfall. We also expect cash flow to be slightly impacted by the $500 million acquisition of Eland. If the proposed borrowing of $350 million is unmet, the company may have to significantly drawdown on its cash flow from operations in FY'20E.

We have a 12-month target price of ₦796.9. SEPLAT currently trades on an EV/2P and EV/EBITDA ratios of 0.9x and 0.9x apiece, which compares favorably to 4.2x and 5.1x for selected peers. We retain a BUY rating on SEPLAT

FINANCIAL SUMMARY	2018A	2019E	2020F	2018A	2019E	2020F
		(₦'Mn)			(US$'Mn)	
Revenue	228,319	229,913	286,289	746.1	751.3	935.6
EBITDA	132,294	126,300	155,675	432.3	412.7	508.7
EBT	80,589	69,797	86,250	263.4	228.1	281.9
PAT	44,852	66,307	51,750	146.6	216.7	169.1
EBITDA Margin	57.9%	54.9%	54.4%	57.9%	54.9%	54.4%
EBT Margin	35.3%	30.4%	30.1%	35.3%	30.4%	30.1%
Net Profit Margin	19.6%	28.8%	18.1%	19.6%	28.8%	18.1%
Return on Average Assets	5.7%	7.9%	5.5%	5.7%	7.9%	5.5%
Return on Average Equity	9.4%	12.9%	9.4%	9.4%	12.9%	9.4%

Disclosure

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Buy ≥ +15.00% expected share price performance

Hold +0.00% to +14.99% expected share price performance

Sell < 0.00% expected share price performance

A **BUY** rating is given to equities with strong fundamentals, which have the potential to rise by at least +15.00% between the current price and the analyst's target price

An **HOLD** rating is given to equities with good fundamentals, which have upside potential within a range of +0.00% and +14.99%,

A **SELL** rating is given to equities that are highly overvalued or with weak fundamentals, where potential returns of less than 0.00% is expected, between the current price and analyst's target price.

A NEGATIVE WATCH is given to equities whose fundamentals may deteriorate significantly over the next six (6) months, in our view.

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% with investment banking relationships	0%	0%	0%	0%

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Guinness Nigeria Plc	
Nigerian Breweries Plc	
Nestle Nigeria Plc	
UAC of Nigeria Plc	
Flour Mills of Nigeria Plc	
Dangote Sugar Refinery Plc	
Dangote Cement Plc	
Lafarge Africa Plc	G
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