



## United Capital Plc

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Income Stock

May 06, 2016

## Executive Summary

- The company recorded growth in its funds under management from the Trustees and Segregated managed funds
- The possibility of an increase in yields in the market may have an adverse impact on the mark-to-market position of its bond portfolio
- The company's trustee business exposes it to State Governments Bonds. The drop in the revenue of the State Governments may affect United Capital revenue
- United Capital has strong alliance with the UBA Group. It is exposed to a Key Man Risk from the relationship
- The company has been recording growth in receivables and impairment charge
- We estimate a dividend per share of N0.32 for the FY 2016
- **Our fair value of the shares of United Capital is N2.80, while our target price is N2.20 per share**
- **Our rating of the shares of United Capital is a BUY at the current market price of N1.75 per share.**

Table 1:	
Rating:	BUY
Current Price	N1.75
Fair Value	N2.80
Price Target	N2.20
Horizon	One Year

*The large assets the company have under management led to the growth in its income during the year.*

*The T/O increased by 31.59% to N6.15bn in 2016.*

### 1.1 FY 2015 Performance Analysis:

The large assets the company have under management led to the growth in its income during the year. As at Financial Year (FY) 2015, Gross Earnings (GE) increased by 31.59% to N6.15bn, compared with N4.68bn recorded in the corresponding period of 2014. The company derives its income from various sources in the financial services sector. The investment income, which is income on fixed deposits accounted for 49.93% of GE. Fees and Commission income which represents financial advisory fees and other fees changes accounts for 26.21% of GE. Net Interest Margin accounted for 13.18% of GE. The other income which covers dividend on equity instruments and others accounted for 10.68% of GE.

Investment income increased by 83.89% to N3.07bn in 2015, while fees and commission income decreased by 12.66% to N1.61bn in 2015. The operating expenses increased by 29.82% to N3.24bn in 2015. The Profit Before Tax (PBT) increased to N3.26bn, an increase of 41.29% from N2.31bn recorded in the corresponding period of 2014. The tax provision increased by 49.55% to N693.19mn from N463.53mn, leading to a Profit After Tax (PAT) of N2.57bn in 2015 from N1.85bn in the corresponding period of 2014, representing an increase of 39.22%.

The PBT margin increased to 53.04% in 2015 from 49.39% in 2014. Also, the PAT margin increased to 41.77% in 2015, from 39.48% in 2014.

The cost-to-income ratio stood at 58.91% in 2015, up from 53.21% in 2014. We noticed an impairment charge of N665.66mn in 2015, from N124.65mn in 2014.

**Table 2: Composition of Gross Earnings – FY 2015 vs FY 2014**

Income Segment	FY 2015		FY 2014	
	Amount (N'bn)	Contribution	Amount (N'bn)	Contribution
Investment Income	3.07	49.93%	1.67	35.61%
Fees & Commission Income	1.61	26.21%	1.85	39.45%
Net Trading Income	-	-	0.03	0.64%
Net Interest Margin	0.81	13.18%	0.42	9.17%
Other Income (Net)	0.66	10.68%	0.71	15.14%
<b>Total</b>	<b>6.15</b>	<b>100.00%</b>	<b>4.68</b>	<b>100.00%</b>

*Source: Company Annual Account and FSDH Research Analysis*

	FY 2015	FY 2014	Change
T/O	6.15	4.68	31.59%
Operating Profit	5.50	3.97	38.50%
PBT	3.26	2.31	41.29%
PAT	2.57	1.85	39.22%

*Source: Company Annual Account and FSDH Analysis*

Assets	Amounts (N'bn)	Contribution to Total Assets
Cash and Cash Equivalents	72.74	50.47%
Loans and Receivables	30.87	21.41%
Available for Sale Securities	10.55	7.32%
Held to Maturity Securities	23.16	16.07%
Investment in Associates	2.27	1.57%
Trade and Other Receivables	3.42	2.37%
Others	1.12	0.77%
<b>Total</b>	<b>144.11</b>	<b>100.00%</b>

*Source: Company Annual Account and FSDH Analysis*

Liabilities	Amount (N'bn)	Contribution (%)
Managed Funds	109.11	83.47
Other Borrowed Funds	16.14	12.35
Other Liabilities	3.29	2.51
Tax Provisions	2.18	1.66

*Source: Company Annual Account and FSDH Analysis*

	FY 2015	FY 2014	FY 2013
Operating Profit Margin	89.32%	84.86%	86.83%
PBT Margin	53.04%	49.39%	57.59%
PAT Margin	41.77%	39.48%	38.55%

*Source: Company Annual Account and FSDH Analysis*

## 2.0 Q1 2016 Performance Analysis:

The unaudited Q1 2016 result of United Capital Plc (UniCapital) for the period ended March 31, 2016 shows that its Gross Earnings (GE) increased by 42.08% to N1.86bn, compared with N1.31bn recorded in the corresponding period of 2015. The improvement in the GE can be attributed to the increased income generated from investment income. This category grew by 53.88% to N947.55mn in 2016 from N615.79mn in 2015. Fees and commission income grew by 55.97% to N550.89mn in Q1 2016, from N353.19mn in Q1 2015. Net interest margin income from managed funds grew by 59.20% to N260.73mn. The growth in the GE was weighed down by the 95.55% drop in the fee and commission income to N2.17mn from N48.84mn in 2015. The total operating expenses (depreciation & amortization, personnel expenses, impairment charge auditors remuneration, directors emoluments, and other expenses) decreased by 11.50% to N452.98mn. **The cost-to-income ratio decreased to 25.72% in 2016 from 43.32% in 2015.**

*The cost-to-income ratio decreased to 25.72% in Q1 2016 from Q1 2015*

The other operating income decreased by 38.08% to N95.24mn in 2016 from N153.82n in 2015. The PBT increased to N1.42bn, an increase of 59.29% from N892.45mn recorded in the corresponding period of 2015. The tax provision also increased by 53.37% to N283.78mn from N185.03mn. This resulted to a PAT of N1.14bn from N707.42mn in the corresponding period of 2015, representing an increase of 60.84%. The company's profit margins recorded a mixed performance in Q1 2016 compared with Q1 2015.

*The company's profit margins recorded an improved performance in Q1 2016 compared with Q1 2015.*

The company's profit margins recorded improved performance in Q1 2016 compared with Q1 2015. The Operating Profit Margin increased in 2016 to 94.87% from 90.42% in 2015. The PBT margin increased to 76.57% in 2016 from 68.30% in 2015. The PAT margin increased to 61.29% in 2016, up from 54.14% in 2015.

**Table 7: Financial Performance (N'bn)**

	Q1 2016	Q1 2015	Change
T/O	1.86	1.31	42.08%
Operating Income	1.76	1.18	49.07%
PBT	1.42	0.89	59.29%
PAT	1.14	0.71	60.84%

Source: Company Annual Account and FSDH Analysis

The result also indicates that the percentage of T/O, PBT, and PAT in the Q1 2016 to the Audited T/O, PBT and PAT for the period ended December 2015 are: 30.17%, 43.56% and 44.27%, respectively. Given the run rate, the company is likely to meet and surpass its previous year's performance. However, the possibility of an increase in yields in the market may have an adverse impact on the mark-to-market position of the bond portfolio. We also note that the company has exposure to State Governments Bonds. These arose principally because of its trustee business. The drop in the revenue of the State Governments may affect United Capital's revenue.

	Q1 2016	Q4 2015	Q3 2015	Q2 2015	Q1 2015
<b>Turnover</b>	1.86	2.07	1.34	1.44	1.31
<b>PBT</b>	1.42	0.87	0.61	0.90	0.89
<b>PAT</b>	1.14	0.66	0.50	0.70	0.71

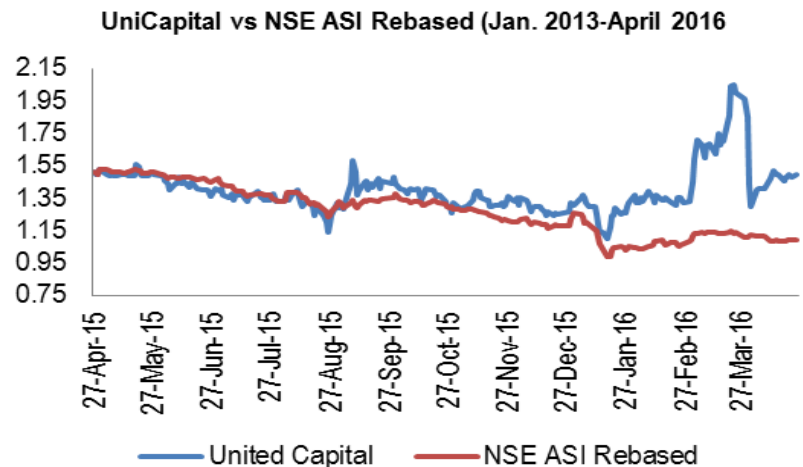
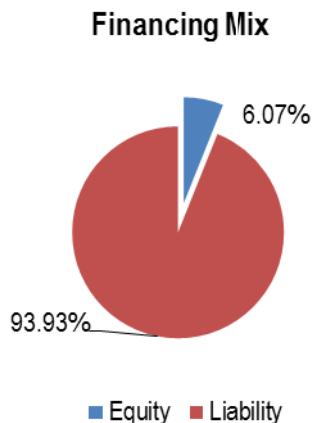
*Source: Company Annual Account and FSDH Analysis*

A cursory look at the balance sheet position as at Q1 2016 compared with the position as at Q1 2015 shows an increase in the company's total assets. The company's financial assets (loans and receivables, available for sale and held to maturity) increased by 29.25% to N83.45bn from N64.57bn in Q1 2015. Loans and receivables as a component of the financial instrument were majorly responsible for the increase in the financial assets, as it increased by 58.09% to N48.78bn in 2016. The loan receivable is a loan facility indexed to LIBOR for a period of 24 months. The commercial paper represents investment in a discounted note for a period of 60 months. The cash and cash equivalent recorded an increase of 33.14% from N72.74bn in Q1 2015 to N96.84bn in Q1 2016. Included in the Group's cash balance is a money market placement of N96.03bn. The trade receivables and prepayments increased in 2016 by 24.48% to N3.92bn from N3.42bn in Q1 2015 period. The impairment on the trade receivables amounted to N1.02bn in Q1 2016. There was also a marginal increase in other borrowed funds, which increased by 0.71% to N16.26bn in 2016. The net assets for the period increased by 9.16% to stand at N11.37bn from N10.42bn as at Q1 2015.

*The trade receivables and prepayments increased in 2016 by 24.48% to N3.92bn from N3.42bn in Q1 2015 period.*

The total assets of the company which stood at N187.34bn as at Q1 2016 were financed by a mix of equities and liabilities in the ratio of 6.07% and 93.93% respectively.

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### 3.0 Drivers of Performance:

#### Positive Factors:

- High yields on fixed income securities as a result of the tight monetary policy
- Growth in its funds under management from the Trustees and Segregated managed funds
- Aggressive marketing drive of its products
- Experienced Management
- Strategic relationship with UBA Group.

#### Negative Factors:

- The decline in the equity market
- Difficult operating environment due to fall in oil prices and pressure on the value of the Naira
- Growth in trade receivables and impairment charges
- The lull in the corporate finance and financial advisory business
- Low interest rate on fixed deposit investments due to high liquidity in the market
- Low net interest margin.

#### 4.0 Strategic Focus:

United Capital's strategic focus is to build an African Leading Investment Banking and Financial Services Group. The company's priorities are listed below:

- Driving effectiveness and efficiency initiatives to improve productivity whilst optimizing costs
- Improving its brand awareness, corporate image and brand value to achieve market-wide recognition and appreciation of its corporate identity
- Renewed focus on service excellence and execution to drive client growth and retention
- Expansion of its footprint and development of innovative product lines
- Driving growth in its market share along core areas of product coverage and expertise
- Improved focus on developing human capital and strengthening of staff its employees.

*United Capital's strategic focus is to build an African Leading Investment Banking and Financial Services Group.*

#### 5.0 Business:

United Capital is a holding company with three subsidiaries: United Capital Trustees Limited, United Capital Asset Management Limited and United Capital Securities Limited. The principal activities of United Capital is investment banking and provision of issuing house, corporate investment advisory services, project finance, debt restructuring, mergers and acquisitions and capital market activities. The company, through its subsidiaries and associates provides additional services such as trusteeship, asset management, securities trading and insurance.

*United Capital is a holding company with three subsidiaries.*

**The company competes with merchant banks, asset management companies and investment banking outfits in Nigeria.**

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##### 5.1.1 Key Transactions and Events in 2015

- Lead Issuing House/Underwriter and Sole Trustee on N30bn Transcorp Hotels Plc Medium Term Debt Issuance
- Structuring Bank/Facility Agent on US\$250mn Pre-Export Finance for Orion Oil



- Joint Trustee on Fidelity Bank Plc N30bn Fixed Rate Unsecured Subordinated Bond
- Appointed Joint Fund Manager for the KfW-sponsored US\$30mn African Local Currency Bond Fund
- Joint Trustee on the Cross River State N8.5bn Fixed Rate Bond Issue
- Sole Trustee on the N5bn Gombe State Bond Issue
- Successfully completed the first direct trade between two West African countries under Phase 1 of the West African Capital Market Integration Initiative.

Table 9: Directors' Shareholding as at December 31, 2015

Director	Position	Holdings
Chika Mordi	Chairman	48,086
Oluwatoyin Sanni	Managing Director	1,015,350
Emmanuel N. Nnorom	Non-Executive	2,640,486 23,486,645*
Amb. J.K. Shinkaiye	Non-Executive	3,114,308
Adim Jibunoh	Non-Executive	N/A
Yoro Mohammed Diallo	Non-Executive	N/A

\*Indirect Shareholding

Table 10: Shareholding Structure as at December 31, 2015

Shareholders	No. of Shares Held	% of Shareholding
West Coast Equity Limited	668,367,002	11.14%
West Coast Equity Limited (NG)	637,111,568	10.62%
Others	4,694,526,430	79.24%
<b>Total</b>	<b>6,000,000,000</b>	<b>100.00%</b>

<b>Table 11: Company Summary</b>	
<b>Ticker</b>	UCAP
<b>Sector</b>	Financial Services
<b>Sub-sector</b>	Other Financial Institution
<b>Date of Incorporation</b>	March 14, 2002
<b>Date of Listing</b>	January 2013
<b>Financial Year End</b>	December
<b>Number of Fully Paid Share</b>	6,000,000,000
<b>Current Capitalization(NGN)</b>	9,360,000,000
<b>NSE Capitalization (NGN)</b>	8,538,947,605,788
<b>% of NSE Capitalization</b>	0.11
<b>52 Week high NGN</b>	2.05
<b>52 Week low NGN</b>	1.10
<b>YTD Return (%)</b>	45.80
<b>52 Weeks Average Volume Traded</b>	5,041,606
<b>Trailing EPS NGN</b>	0.50
<b>Trailing P/E Ratio (X)</b>	3.12
<b><i>*As at the April 26, 2016</i></b>	

## **6.0 Product Analysis:**

United Capital's businesses include investment banking, trusteeship, asset management and securities trading.

### **6.1 United Capital Investment Banking (UCIB):**

UCIB is an integrated investment bank providing advisory services along the following business lines:

- Project Finance
- Capital Markets
- Mergers & Acquisitions
- Structured Finance.

### **6.2 United Capital Asset Management (UCAM):**

The subsidiary provides investment services to a diverse client base that includes; Corporate Institutions, Government and Agencies, High Net worth Individuals and Retail Investors. The assets under its management are in excess of N150bn. The products the subsidiary offers are:

- Collective Investment Scheme
- Fixed Income Investment
- Portfolio Management Services
- Wealth Management, and
- Investment Advisory Services.

### **6.3 United Capital Trustees (UCT):**

UCT works closely with individuals, families and foundations, guiding them in the preservation and transfer of wealth across generations. The products offered by this subsidiary include:

- Bond Trusteeship
- Collective Investment Scheme

- Private Trusts
- Security and Debenture Trusts.

#### **6.4 United Capital Securities (UCS):**

UCS operates a business model that encompasses sales and trading of listed and unlisted securities for a diverse universe of private and institutional clients.

UCS also provides access to primary market opportunities for listed equities (IPOs, Right Issues, Offer for Sale and Offer for Subscription) and fixed income securities.

The products offered by the subsidiary include:

- Securities Dealing Services
- Portfolio Management Services
- Receiving Agent to New Issues
- Stockbroker to Primary Issues, and
- Designated Advisers to Small and Medium Scale Enterprises (SMEs).

## 7.0 SWOT Analysis:

<p><b>7.1 Strengths:</b></p> <ul style="list-style-type: none"> <li>- Diversified income stream</li> <li>- Stable management</li> <li>- Robust Trustees business</li> <li>- Improved profit margins</li> <li>- Low cost-to-income ratio</li> <li>- Large asset under management</li> <li>- Strong alliance with the UBA Group</li> </ul>	<p><b>7.2 Weaknesses:</b></p> <ul style="list-style-type: none"> <li>- Rising finance costs</li> <li>- Key man risk</li> <li>- Overconcentration in assets</li> <li>- Low net interest margin</li> <li>- Growing receivables and impairment charge</li> </ul>
<p><b>7.3 Opportunities:</b></p> <ul style="list-style-type: none"> <li>- Growing debt market in Nigeria</li> <li>- The tight monetary policy stance of the CBN</li> <li>- Large infrastructure deficit which would require various project finance opportunities</li> <li>- Local content financing</li> </ul>	<p><b>7.4 Threats:</b></p> <ul style="list-style-type: none"> <li>- Rising inflation rate</li> <li>- Foreign exchange risk</li> <li>- Lull in the stock market</li> <li>- Sharp drops in the State Governments revenue</li> <li>- Possible increase in interest rates</li> <li>- Weak saving and investment culture.</li> </ul>

## 8.0 Forecast:

### Our Forecast Drivers

We considered the following factors in arriving at our 5-year forecasts:

#### Positive Factors:

- Expected high yields on the fixed income securities in the market
- Diversified income stream
- Growing and vibrant bond market in Nigeria
- Large infrastructure deficit in Nigeria looking for funding
- Drive to ensure operational efficiencies, leading to cost reduction
- Expected recovery in the equity market.

#### Negative Factors:

- Low net interest margin
- The weak consumers savings/investment culture
- High receivables and impairment charge.

We are of the opinion that the impact of the positive factors would be higher on both the revenue and the profitability of the company than the negative factors. We therefore estimate Gross Earnings of N7.02bn, N7.76bn, N8.05bn, N8.36bn and N8.51bn for the periods ending December 2016, 2017, 2018, 2019 and 2020. Our PBT forecasts for the periods are: N3.70bn, N4.05bn, N4.12bn, N4.20bn and N4.01bn. Adjusting for tax, our PAT forecasts are N2.94bn, N3.21bn, N3.27bn, N3.33bn and N3.18bn. PAT Margin for the period are 41.84%, 41.43%, 40.62%, 39.80% and 37.36%. **Our forecast final dividend for the FY 2016 is N0.32 per share.**

*Our forecast final dividend for the FY 2016 is N0.32 per share.*

N'bn	DecA-15	Dec-16	Dec-17	Dec-18	Dec-19	Dec-20
Gross Earnings	6.15	7.02	7.76	8.05	8.36	8.51
Investment Income	3.07	4.73	4.82	4.92	5.02	5.07
Fee and Commission Income	1.61	1.77	1.77	1.86	1.96	2.05
Other Income	0.66	0.40	0.44	0.46	0.48	0.48
Interest Income on managed funds	4.68	5.78	5.84	5.90	5.96	5.99
Interest expense on managed funds	(3.87)	(5.18)	(5.03)	(5.00)	(4.96)	(5.00)
Net Interest Income	0.81	0.60	0.81	0.90	1.00	0.99
Total Income	6.15	7.02	7.76	8.05	8.36	8.51
Total Operating Expenses Less Depreciation	(3.17)	(3.47)	(3.88)	(4.11)	(4.35)	(4.68)
Group's Share of Associate Result	0.35	0.25	0.27	0.29	0.30	0.30
Depreciation and Amortisation	(0.06)	(0.09)	(0.10)	(0.11)	(0.12)	(0.13)
Total Operating Expenses	(3.24)	(3.57)	(3.98)	(4.22)	(4.46)	(4.80)
PBT	3.26	3.70	4.05	4.12	4.20	4.01
Tax	(0.69)	(0.76)	(0.84)	(0.85)	(0.87)	(0.83)
PAT	2.57	2.94	3.21	3.27	3.33	3.18

Source: Company Annual Account – 2015 and FSDH Research Analysis

	DecA-15	Dec-16	Dec-17	Dec-18	Dec-19	Dec-20
PBT Margin	53.04%	52.73%	52.22%	51.19%	50.16%	47.08%
PAT Margin	41.77%	41.84%	41.43%	40.62%	39.80%	37.36%
Total Expenses to Gross Earnings	52.62%	50.81%	51.32%	52.35%	53.38%	56.46%
Cost to Income Ratio	52.62%	50.81%	51.32%	52.35%	53.38%	56.46%
EPS(N)	0.43	0.49	0.54	0.55	0.55	0.53
DPS(N)	0.35	0.32	0.35	0.36	0.36	0.35
Dividend Payout	81.70%	65.79%	65.79%	65.79%	65.79%	65.79%
Earnings Yield*	32.70%	17.50%	19.14%	19.49%	19.83%	18.94%
Dividend Yield*	26.72%	11.51%	12.59%	12.82%	13.05%	12.46%
P/E Ratio	3.06	5.71	5.22	5.13	5.04	5.28
Number of Shares ('bn)	6.00	6.00	6.00	6.00	6.00	6.00

\*At Our Fair Value of N2.80

Source: Company Annual Account – 2015 and FSDH Research Analysis

## 9.0 Valuation

In arriving at a fair value for the ordinary share of the company, we used the Discounted Free Cash Flow (DCF) model. We applied a terminal growth rate of **2.79%**. We used a beta value of **0.82x** based on the 5-year daily historical returns on the company share price and The Nigerian Stock Exchange All Share Index (NSE ASI). We used the yield of **11.97%** as our risk free rate, and market premium of **11.15%**. Applying the foregoing parameters on the Capital Asset Pricing Model (**CAPM**), the cost of equity generates **21.16%**. Using 6bn shares in issue, the DCF model generates **N2.80** per share, which is our fair value.

The current market price of United Capital shares is N1.75. The highest and the lowest closing price in the last 52 weeks are N2.05 and N1.10 respectively. The 2016 forward earnings yield and dividend yield based on our fair value are: 17.50% and 11.51% respectively. The expected capital appreciation from the current price to our fair value is 59.86%. This is higher than our minimum equity return benchmark of 16.65%. We therefore place a **BUY** on the shares of United Capital Plc at the current price of N1.75 as of May 04, 2016.

*The fair value for United Capital Plc is N2.80.*

### 9.1 Risks to Price Target:

The following risks may affect the price target:

- Increase in the yield on fixed income securities
- Drop in market liquidity
- Issuance of new equity
- Reduction in dividend payment



Table 14 : Analyst Rating	
Rating	Criteria
BUY	Fair value of the stock is $\geq$ 16.65%* compared with the current market price.
HOLD	Fair value of the stock ranges between -10% and 16.65% of the current market price.
SELL	Fair value of the stock is > 10% below the current market price.
<b>*16.65% is our estimated minimum equity return. It is the combination of our risk free rate and risk premium. Our risk free rate is the average yield on a five-year FGN Bond. We adopted a 5% risk premium and set the risk free rate every quarter.</b>	

**Fair Value:** This is the value of the ordinary shares of the company using the valuation method appropriate for the company. It is the intrinsic or true value of the stock based on fundamentals of the company. The market price may either trade at a premium or discount to the intrinsic value.

**Price Target:** This is the price that we believe the shares of the company will trade within our time horizon. Other risk factors may affect the attainment of this price. This price may or not be different from the intrinsic value.

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