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EQUITY STRATEGY DIARY

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A new dawn for the naira — bullish or bearish for coverage sectors?

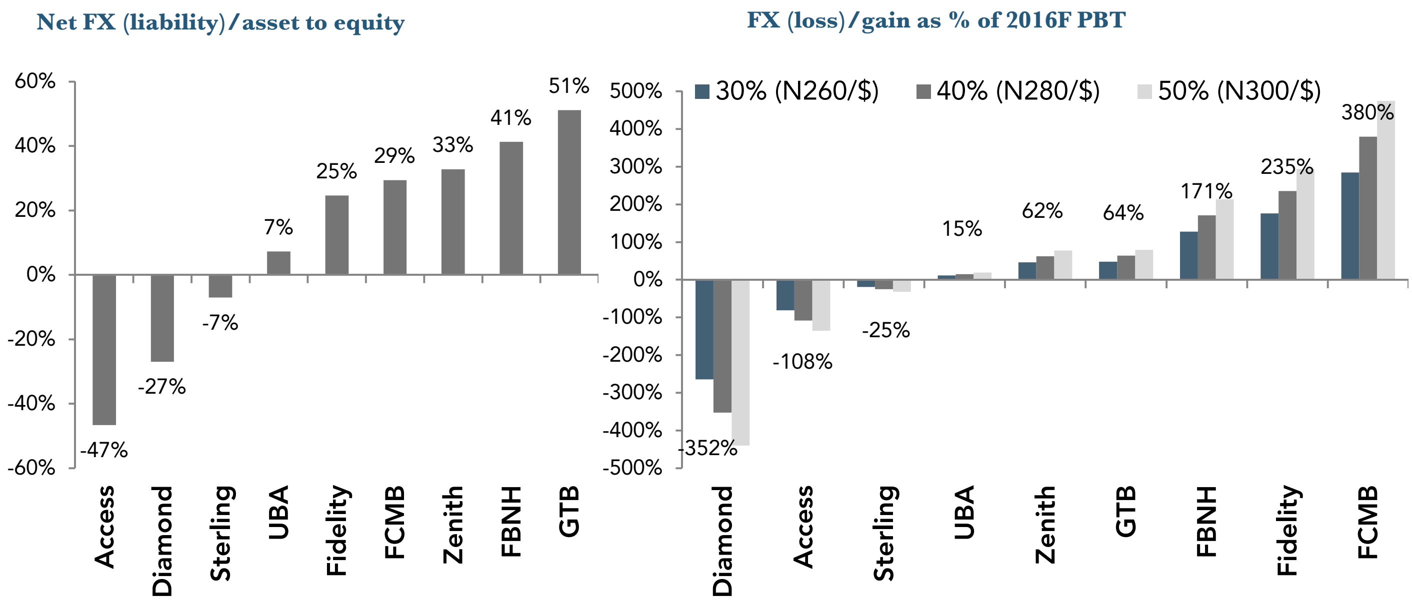
On Monday, 20th June 2016, Nigeria will float the naira for the first time in nearly three decades. Though there will be no official target under the new market structure, our base case is for depreciation of up to 40% to ₦280/$ (see our report: Goodbye naira peg, Hello floating naira). The potential depreciation of the naira against the US dollar hallmarks the foreign exchange risk we had noted was inevitable given fundamental concerns. With most corporates having some level of foreign currency exposure, **using net foreign exchange position as at FY 15[1], we review our coverage names to determine the most exposed to naira weakening and dimension potential impact on 2016F PBT**. In running our scenarios, in addition to our base case, we also tested for impact of 30% and 50% naira depreciation on PBT. On a sectoral basis **we find only the banking and oil and gas sectors with net foreign assets, while consumer goods, agriculture and building materials sectors each have net foreign liabilities.**

For banks, looking through net FCY position of our universe, Access stands out with net foreign liability of ₦174 billion as at FY 2015. Using our base scenario (40% depreciation), **Access bank could report forex exchange revaluation losses of up to ₦70 billion[2],** 30% more than our 2016F PBT. On the flip side, although GTB, FBNH

[1] Except for Total (Q1 16)
[2] This is not far from the analysis conducted by Access in its 2015 annual report which forecasts a ₦17billion loss in the event of 10% naira devaluation.

and Zenith hold the largest net foreign asset, **impact of a naira depreciation on 2016F PBT is most positive for FCMB** (nearly 4x) and Fidelity (2.3x).

Figure 1: Impact of FX volatility on banking firms



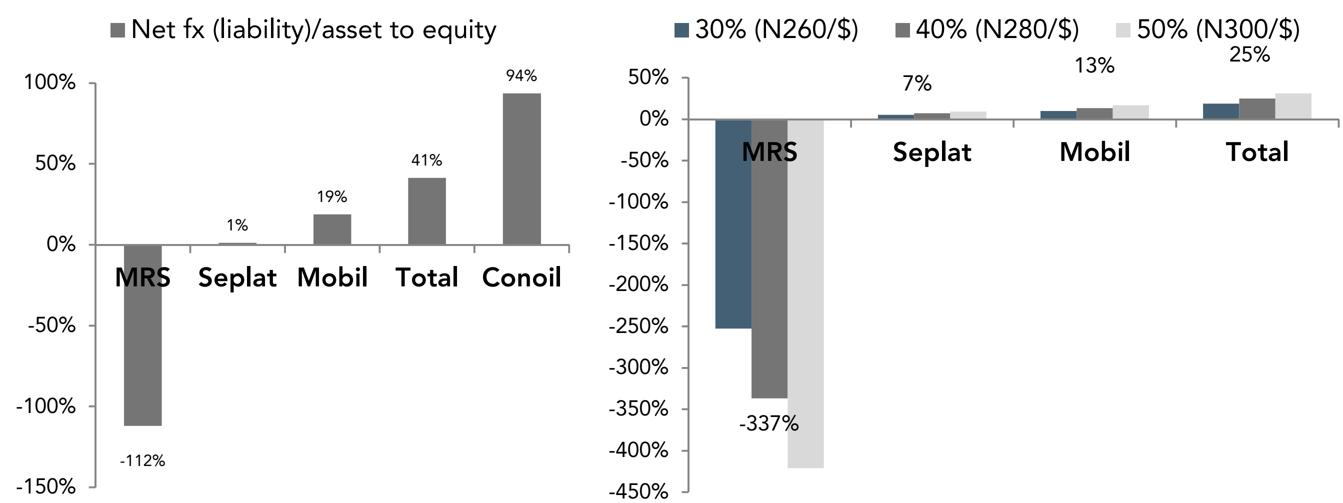
Source: Company financials, ARM Research

In the oil and gas sector, a depreciation of the naira is most positive for Total and Mobil with net foreign assets of ₦7.8 billion and ₦3.3 billion respectively while MRS is at the most of risk of reporting a sizeable foreign loss, with net foreign liability of ₦23 billion. At base case, potential foreign currency gains for Total (₦3.2 billion) and Mobil (₦1.3 billion) translate to 25% and 13% of 2016F PBT, with loss for MRS of up to 3x 2016F PBT (est. ₦9.4 billion). Unsurprisingly, Seplat with largely dollar receivable also stands to benefit to the tune of ₦1.3 billion.

Figure 2: Impact of FX volatility on downstream oil and gas companies

Net FX (liability)/asset to equity

FX (loss)/gain as % of 2016F PBT



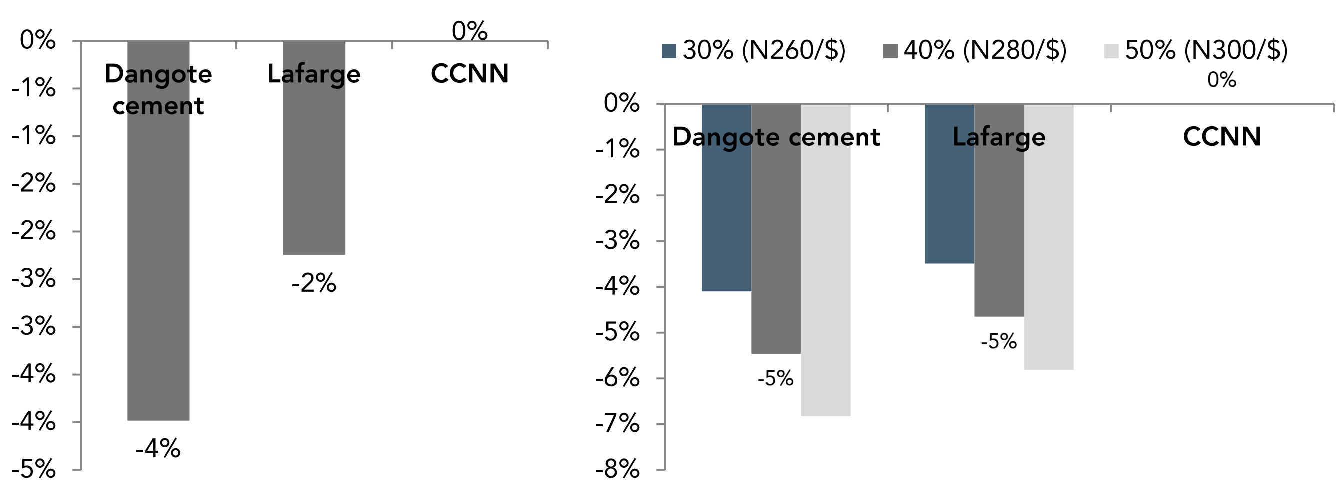
Source: Company financials, ARM Research

In the cement sector, Dangcem and Lafarge appear the most exposed to foreign currency risk given their respective net foreign currency liability position of ₦25 billion (or ~4% of FY 15 Equity) and ₦4billion (2% of FY 15 Equity) while CCNN, whose operations are Nigeria-centric, have no reported foreign currency liability position. Estimate losses of Dangcem and Lafarge are both 5% of 2016F PBT.

Figure 3: Impact of FX volatility on cement companies

Net FX (liability)/asset to equity

FX (loss)/gain as % of 2016F PBT

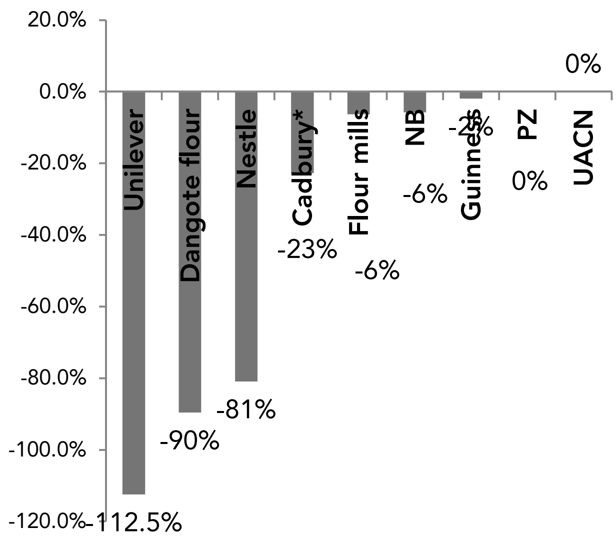


Source: Company financials, ARM Research

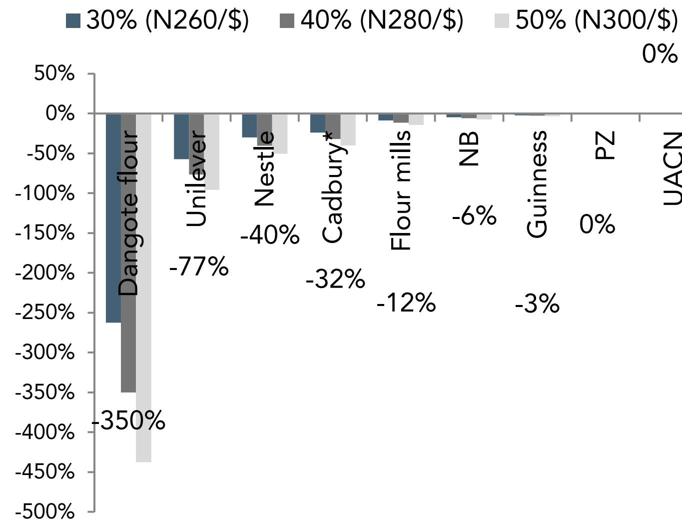
Among the consumer names, we find DFM, Unilever and Nestle as having the highest risk of foreign exchange losses of at least 40% of our 2016F PBT. On the other hand, UACN and PZ sit in a fairly comfortable position with net FX asset of ₦56.1 million and negligible net FX liability, respectively. For the agriculture players, Okomu is at risk of a bigger forex loss (₦660 million) relative to Presco (₦365million) with respective 25% and 6% impact on 2016F PBT.

Figure 4: Impact of FX volatility on consumer goods companies

Net FX (liability)/asset to equity

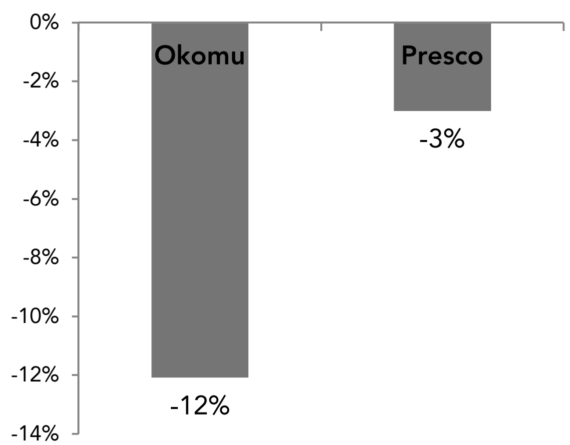


FX (loss)/gain as % of 2016F PBT

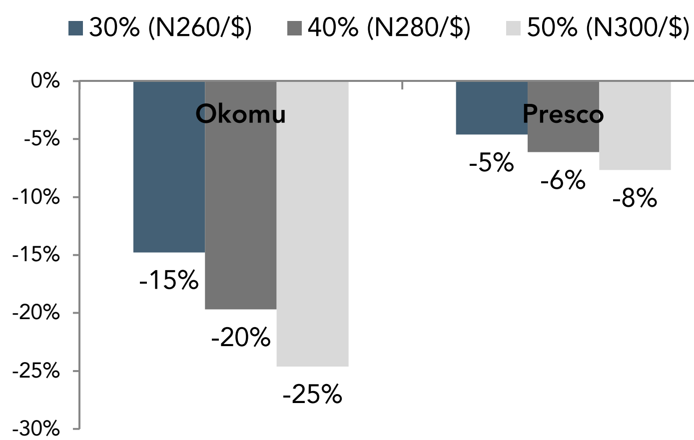


Source: Company financials, ARM Research

Net FX (liability)/asset to equity



FX (loss)/gain as % of 2016F PBT



Source: Company financials, ARM Research

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