CardinalStone Partners Limited

Final Rating Report

Agusto&Co.

Research, Credit Ratings, Credit Risk Management

CardinalStone Partners Limited

Rating:

Bbb

Outlook: Stable
Issue Date: 5 August 2021
Expiry Date: 30 June 2022
Previous Rating: Bbb-

Industry:
Financial Services

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Rating Rationale

Agusto & Co. hereby upgrades the rating of CardinalStone Partners Group ("CSPG" or "the Group") to 'Bbb'. The upgrade is hinged on CSPG's improved risk management structure, asset quality and funding profile following the Group's debut commercial paper and bond issuances in 2020. Furthermore, the rating is supported by CSPG's good profitability, good liquidity profile, adequate capitalisation and competent and stable management team. The rating is, however, constrained by the Group's exposures to unrated financial institutions and significant concentrations in asset portfolios in the review period. The negative impact of the COVID-19 pandemic on the global and domestic business environments has also been taken into cognisance.

CSPG is a financial services group that provides a bouquet of services including asset management, financial advisory and investment banking to blue-chip and midcap companies, high net-worth individuals (HNIs), institutional investors and retail clients. The Group, through its businesses, has broker, fund manager, registrar and trustees licences from the Securities and Exchange Commission ("SEC") and a finance house licence from the Central Bank of Nigeria ("CBN"). As at 31 December 2020, CSPG's total assets stood at ₦38.3 billion, representing a 44% increase from the prior year as the Group's debut bond and commercial paper issuances of ₦5 billion respectively supported asset growth.

As at 31 December 2020, the Group had a placement portfolio of ₦9.6 billion, which accounted for the second largest fraction of CSPG's total assets at 24.9%. The Group had exposures to speculative financial institutions amounting to ₦1.4 billion, which equated to 4% of total assets and 24% of the Group's shareholders' funds, which was sizeable in our view. There was also concentration in the portfolio as the top two counterparties accounted for 54% of placements. However, based on the unaudited accounts for Q1 2021, exposures to speculative grade institutions stood at 10.2% of CSPG's shareholders' funds, representing a decline as the Group's financial institutions placement policy was reviewed to include credit rating requirements and limits.

CSPG's loans & advances portfolio accounted for the third largest fraction or 16% of the Group's total assets. The portfolio comprises consumer, margin and structured finance loans. As at 31 December 2020, structured finance loans, which are short-term collateralised loans to mid-sized companies and HNIs, accounted for 59% of the Group's loans & advances portfolio. There was some concentration in the portfolio as the top four obligors accounted for 54% (2019: 70%) of structured loans. Exposures to related parties, which in our opinion are of speculative grade credit quality, also stood at 25.7% (2019: 53%) of the structured loan portfolio or 17% of CSPG's shareholders' funds. As at the 2020 FYE, the ratio of non-performing loans (NPLs) to the gross structured loan portfolio stood at 3.1% in 2020 (2019: 7%). CSPG's consumer loan portfolio accounted for the second largest fraction of the Group's loans and advances portfolio with 24%. Due to the COVID-19 pandemic, CSPG focused on collections – engaging customers on loan restructuring and appointing debt collector agencies for higher-risk sectors. Up to 25% of the consumer portfolio was restructured in the 2020 FY. The size of the consumer loans portfolio thus remained flat while the ratio of NPLs to consumer loans stood at 7.7% as at 31 December 2020. This was significantly lower than the 22.6% NPL ratio of prior year, a notable improvement but still higher than our benchmark of 5%. As at the 2020 FYE, the cumulative loan loss provision was sufficient to cover 100% of the NPLs in the structured and consumer loan portfolios. We expect the consumer loan book to grow moderately as the Group expands product offerings to public sector employees and asset financing. However, we do not expect this growth to negatively impact asset quality given the complementary investments in integration with Nigeria Inter-Bank Settlement System (NIBSS) and Remitta to support first charge deductions.

During the financial year ended 31 December 2020, the Group recorded net earnings of ₦5.8 billion, up 94% from ₦3.0 billion in the prior period. This was due to the stand out performance of the equities market, with the Nigerian Stock Exchange ("NSE") All-Share Index closing 2020 with a gain of 50%. The notable growth in net earnings translated to an improved cost to income ratio of 43.1% (2019: 56.4%), albeit higher than the 38.3% recorded by peer, United Capital Plc ("United Capital"). However, CSPG recorded superior profitability ratios with a pre-tax return on average equity (ROE) of 64.3% (2019: 43.2%) and a pre-tax return on average assets (ROA) of 10.1% (2019: 5.4%) in comparison to United Capital's pre-tax ROE and pre-tax ROA of 36.1% and 4.3% respectively. We expect to see a moderate decline in the Group's earnings, largely from the proprietary trading business given that 2020's performance was extraordinary and facilitated by the low money market and fixed income yields, which have risen gradually subsequent to the FYE. Thus, we expect to see a moderate decline in CSPG's profitability indicators.

As at 31 December 2020, CSPG had shareholders' funds of ₦5.9 billion. As at the same date, our estimate of (Basel I) adjusted capital to risk weighted assets ratio for the Group stood at 24%, which was above our benchmark. When we subject the Group's adjusted capital to a stress test by considering only the core capital available to provide buffers for periods of uncertainty (adjusted capital less all related party loans), CSPG's Basel I ratio declines to 18%, which is still acceptable in our view. CSPG had a debt to equity ratio of 2.3 times, which was better than United Capital's 3.4 times at the end of the review period. We expect capitalisation to remain adequate to support the Group's current business risk, but debt to equity ratio to rise above our benchmark as CSPG issues additional short-term debt under the ₦10 billion commercial paper programme.

The Group was primarily funded by clients' fund under management ("FuM"), which financed 36% of CSPG's total assets as at the 2020 FYE. The Group's clients' FuM portfolio comprises CSPG's fixed income notes product in local currency (98%) and foreign currency (2%). The clients' FuM portfolio had a large client base with over 300 individuals and organisations but showed concentration with the top 10 investors accounting for 40.2% of the total. As at 31 December 2020, the Group had liquid assets totalling ₦26.9 billion, which were sufficient to cover 119% of clients' FuM and other liabilities. CSPG recorded a liquid asset to total liabilities ratio of 83%, which is good in our view.

Table 1: Financial Data for CardinalStone Partners Group

	31 December 2020	31 December 2019
Total Assets	₦38.3 billion	₦26.7 billion
Gross Earnings	₦7.6 billion	₦4.3 billion
Pre-tax return on average assets	10.1%	5.4%
Pre-tax return on average equity	64.3%	43.2%

Source: CardinalStone Partners Limited

Strengths

- Good profitability
- Good liquidity and funding profile
- Stable and experienced management team

Weaknesses

- Concentration to related entities in the structured loan portfolio
- Exposure to speculative grade financial institutions
- New risk management structures yet to take full effect

Challenges

- Ability to sustain asset quality in the weak macroeconomic climate
- Sustaining performance in the adverse business environment

GROUP PROFILE

CardinalStone Partners Limited ("CSPL" or "the Company") was incorporated as a private limited liability company and began operations in 2008. The Company was licensed by the Securities and Exchange Commission ("SEC") to provide asset management, financial advisory, investment banking and trustees services. CSPL along with its subsidiaries has subsequently expanded operations and offerings to include registrar, consumer and structured lending and securities brokerage services in a vertically integrated group structure.

The Company has four operating subsidiaries: CardinalStone Asset Management, CardinalStone Registrars, CardinalStone Securities, CS Advance Finance Company and CardinalStone Trustees. CardinalStone Registrars, CardinalStone Securities, CardinalStone Asset Management and CardinalStone Trustees are licensed by the SEC as registrar, broker, fund manager and trustees respectively while CS Advance Finance Company has a finance company licence from the Central Bank of Nigeria.

Figure 1: CardinalStone's Group Structure

Source: CardinalStone Partners Limited

CSPL and its subsidiaries ("CSPG" or "the Group") provide financial services to blue-chip and midcap companies, high net-worth individuals (HNIs), institutional investors and retail clients. CSPG's provides services including asset management, financial advisory, investment banking, registrar, trustees' services and stockbroking to clients. The Group also makes investments in fixed income and equity securities via a proprietary trading desk and has equity investments in unlisted companies. In addition, CSPG holds a 20% equity stake in CardinalStone Capital Advisers, which was established in 2016 to promote and manage private equity funds.

CSPG is governed by an eight-member Board of Directors, which is chaired by Mr Fola Adeola. The Group's operations are led by Mr Michael Nzewi, who is the Group Managing Director. Five members of the board indirectly own 46.1% of CSPG's equity through investments in CardinalStone Partners Limited, while Mr Fola Adeola directly owns 8.2% of the Company's equity. Thus, the members of the Board jointly own 53.4% of CSPG. The Group operates offices in Lagos State and Abuja, Federal Capital Territory, with the head office located at 5 Okotie Eboh Street, Ikoyi, Lagos. During the financial year ended 31 December 2020, CSPG had an average staff strength of 143 persons.

Table 2: Board of Directors

Directors	Position	Shareholding
Mr Fola Adeola	Chairman	8.2%
Mr Michael Nzewi	Group Managing Director	10.2%*
Mr Mohammed Garuba	Managing Director CardinalStone Asset Management	10.2%*
Mr Asue Ighodalo	Non-Executive Director (Independent)	Nil
Mr Femi Ogunjimi	Non-Executive Director	10.2%*
Ms Mairo Bashir	Non-Executive Director (Independent)	Nil
Mr Yomi Jemibewon	Non-Executive Director	10.2%*
Chief Callistus Nweke**	Non-Executive Director	5.3%*

**Indirect*

***Appointed 12 March 2020*

Business Strategy

CSPG's primary strategy is to leverage its core competence of offering asset management, investment banking and advisory services to HNIs, institutional clients and blue-chip companies. The Group's sizable balance sheet and notable performance are attributable to strong referrals from domestic networks. CSPG also develops strategic partnerships with international brokers to expand the client base and grow the securities trading business. To grow assets under management (AuM), the Group plans to focus on launching local and foreign currency denominated collective investment schemes (CISs) while leveraging on technology to deliver products to HNI, institutional and retail clients in Nigeria and the diasporas in the near to medium term.

CSPG, through CS Advance Finance Company, also plans to grow the consumer lending business in the medium term by launching loan products for public sector employees and asset financing. CS Advance Finance Company aims to achieve this through strategic partnerships with telecommunications providers and a reengineering of existing technology infrastructure to accommodate more users and additional risk management protocols. The Group has obtained a trustee licence to deepen service offerings, leverage group-wide economies of scale and support the expansion of the customer base and growth in AuM in the short to medium term.

Business Structure

CSPG operates a hybrid group organisational structure with CSPL, CardinalStone Asset Management, CardinalStone Securities - operating a centralised system for support functions such as legal/company secretary, financial control, risk management, internal control, compliance, internal audit, information technology and human resources. The other subsidiaries – CardinalStone Registrars and CS Advance Finance Company – have dedicated support functions, excluding legal/secretary, that are overseen by the respective central support departments. The group heads of the various divisions under each subsidiary report to the Managing Director/CEO overseeing the business, while the heads of the business support groups either report to the Group Managing Director/CEO or the Group Executive Director.

The asset management business is led by a Managing Director, who is also a Group Executive Director. The securities business is led by a Managing Director, the registrar business is helmed by a Chief Business Strategist and the consumer lending business is overseen by an Ag. Managing Director. The heads of the Group's human resources, legal/company secretary and financial control units report to the Managing Director/CEO while the heads of the risk management, internal control, compliance, internal audit, information technology and brand units report to the Executive Director. All the entities in the Group have separate boards of directors.

Information Technology

CSPG operates a centralised information technology structure with two major units: software development and infrastructure/application support. The software development unit comprises frontend and backend developers responsible for creating proprietary applications for subsidiaries: CardinalStone Registrars and CS Advance Finance Company; and platforms to promote CardinalStone Asset Management's CIS products. CardinalStone Securities has a trading portal called Trade Direct, which is an online trading platform that provides clients with direct access to real time quotes, execution and information on the floor of the Nigerian Stock Exchange. The Group uses applications provided by Microsoft's Office 365, with client files stored on the cloud drive while other files are stored locally on a server. Infoware and other enterprise applications of the Group's various businesses are hosted on high-availability infrastructure, with the business continuity and disaster recovery solution either provided by the software vendors or using in-house capacity. CSPG also develops some proprietary software to improve the efficiency of business processes.

Management Team

Mr Michael Nzewi is one of the founders of CardinalStone Partners and the Managing Director/CEO. He was appointed to this role in January 2017. Prior to co-founding the Group in 2008, Mr Nzewi served as a director in the Capital Markets division of Standard Chartered Bank, London from 2007 to 2008. Prior to this, he headed Corporate Finance at Vetiva Capital Management between 2004 and 2007.

Mr Nzewi obtained a BSc in Accounting from the University of Benin, Nigeria in 1997 and an MBA from Said Business School, Oxford University, United Kingdom in 2006. He is an associate member of the Institute of Chartered Accountants of Nigeria.

Mr Mohammed Garuba is one of the founders of CardinalStone Partners and an Executive Director. He is also the Managing Director of CardinalStone Asset Management. Prior to co-founding the Group in 2008, Mr Garuba served as Director of Equity Securities at Renaissance Capital, Lagos from 2007 to 2008 and before then the Managing Director/COO of Zenith Securities from 2005 to 2007.

Mr Garuba obtained a BSc in Insurance from the University of Lagos in 1998 and an MBA from London Business School. He is a fellow of the Institute of Chartered Accountants of Nigeria. He is also a fellow of the Chartered Institute of Stockbrokers.

The Group's senior management team includes:

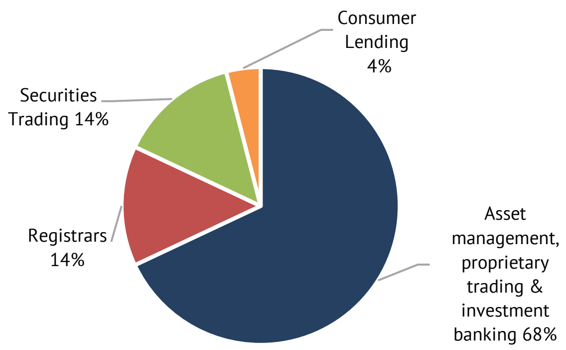
▪ Mrs. Elile Olutimayin	Managing Director, CardinalStone Securities
▪ Mr. Ayoola Adeola	Chief Business Strategist, CardinalStone Registrars
▪ Ms. Ereifemi Akeredolu	Managing Director, CardinalStone Trustees
▪ Mr. Oloruntoba Ayodele	Ag. Managing Director, CS Advance Finance Company
▪ Mrs. Onyebuchim Obiyemi	Head, Investment Banking
▪ Mr. Olutayo Oyawale	Head, Information Technology
▪ Mr. Peter Omoregie	Head, Proprietary Trading
▪ Ms. Azizah Abiola	Head, Legal/Group Company Secretary
▪ Mr. Bukola Joshua	Head, Financial Control
▪ Ms. Omotoyosi Kola-Ojo	Head, Compliance
▪ Mrs. Pelumi Adeosun	Head, Risk Management
▪ Mr. Philip Anegbe	Head Research
▪ Ms. Tolulope Salami	Head, Human Resources

ANALYSTS' COMMENTS

ASSET QUALITY

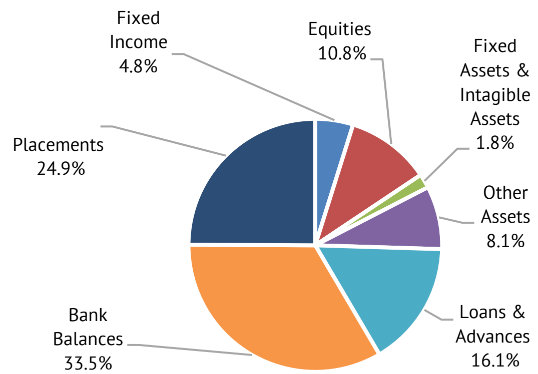
As at 31 December 2020, CSPG had total assets of ₦38.3 billion, up 43.5% from ₦26.7 billion at the end of the prior year. The notable growth in total assets was largely driven by a considerable increase in liquid assets following the issuance of a ₦5 billion bond at the end of 2020 and the good performance of the Group's capital markets-related businesses in the period in spite of the challenges due to the COVID-19 pandemic. The asset management, proprietary trading and investment banking businesses jointly accounted for the largest fraction of CSPG's total assets with a 68% share in 2020 while the registrar and securities trading businesses were the second-joint largest contributors, each with 14% of total assets. The consumer lending business accounted for the remainder 4% of total assets as at the 2020 FYE. We expect moderate growth in total assets in the near term as the economy improves and the Group continues to expand through planned product and business launches.

Figure 2: Breakdown of assets by business



Source: CardinalStone Partners Limited

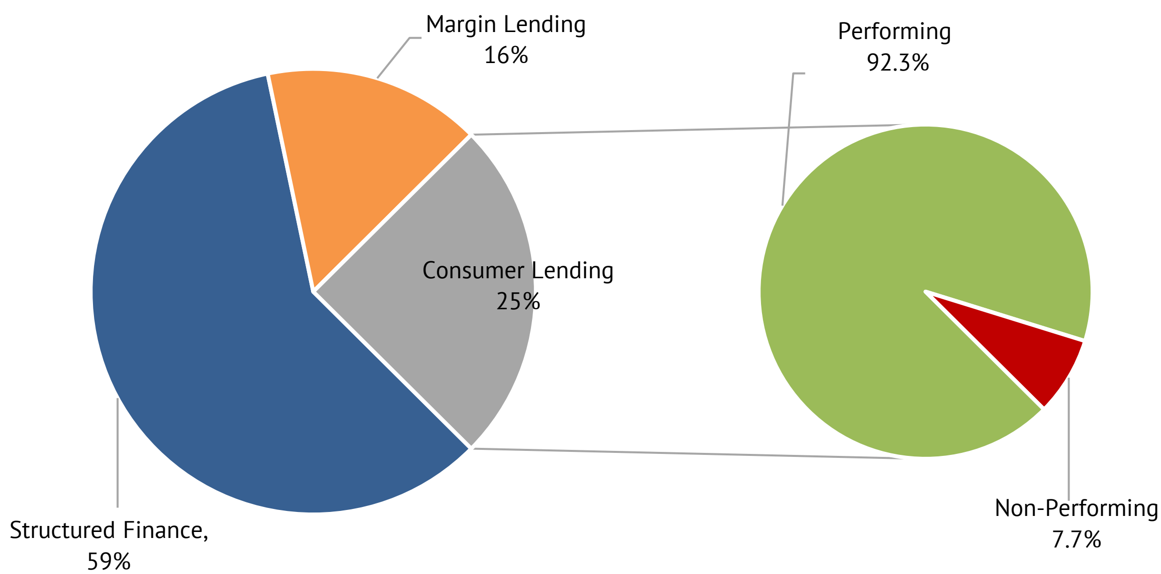
Figure 3: Breakdown of CSPG's total assets



Source: CardinalStone Partners Limited

As at 31 December 2020, ₦9.6 billion or 24.9% of the Group's total assets were placements with financial institutions. This represented a 113% increase from the ₦4.5 billion recorded at the end of the prior period. The significant increase was due to the unutilised proceeds from CSPG's debt instruments issued in H2 2020 and growth in clients' funds under management. However, we note with concern the Group's placements with speculative grade financial institutions. As at the 2020 FYE, CSPG's total placements with speculative grade institutions stood at ₦1.4 billion, which equated to 4% of total assets and 24% of the Group's shareholders' funds, which was sizeable in our view. There was also notable concentration in the portfolio as the top two counterparties accounted for 54.4% of total placements. Notwithstanding, based on unaudited accounts as at the end of Q1 2021, we note a significant reduction in concentration and exposure to speculative financial institutions in the portfolio following a review of the Group's financial institutions placement policy led by the new risk management and internal control team heads.

Figure 4: Breakdown of CSPG's loan portfolio



Source: CardinalStone Partners Limited

As at 31 December 2020, loans & advances accounted for 16% of CSPG's total assets. The Group provides loans & advances to retail, HNI and corporate clients under three business lines: consumer lending, margin lending and structured finance. As at 31 December 2020, CSPG's structured finance portfolio, which are short-term collateralised loans to mid-sized companies and HNIs stood at ₦3.8 billion, a 201% growth from ₦1.3 billion in the prior year. The significant increase was due to the Group's focus on growing loans to mid-size businesses as the COVID-19 pandemic brought opportunities to fund working capital requirements and to access the debt markets to support lending. CSPG's structured loan book as at the 2020 FYE comprised 25 obligors, with mid-sized companies accounting for 68% of the value while individuals accounted for the balance of 32%. There was concentration in the structured loan portfolio as the top 4 obligors constituted 54% (2019: 70%) of the total while exposure to related parties was 25.7% (2019: 53%) or 17% of the Group's shareholders' funds. The non-performing loans (NPLs) ratio in the structured finance loan portfolio stood at 3.1% in 2020 (2019: 7%). The NPLs entirely comprised exposures to related parties, which in our opinion are of speculative grade credit quality. The improvement in NPL was achieved as the Group intensified recovery efforts through restructuring and partial disposal of assets pledged by customers. Notwithstanding, we note that the cumulative loan loss provision was sufficient to cover 100% of the outstanding NPLs as at the 2020 FYE. In the near term, we expect an increase in NPLs due to slow economic recovery, heightened insecurity and lingering threat of a third wave of the COVID-19 pandemic, which will keep credit risk elevated.

As at the 2020 FYE, CSPG's consumer loan portfolio stood at ₦1.6 billion, which represented a 24% decline from ₦2.1 billion at the end of the prior period. The drop came as the Group focused on collections due to the negative impact of the COVID-19 pandemic on the Nigerian business environment and the disposable incomes of consumers. Following the easing of the six-week lockdown in H1 2020, CS Advance Finance Company, embarked on an aggressive loan recovery drive to minimise losses by engaging customers on loan restructuring and appointing debt collector agencies for the higher-risk sectors such as hospitality, aviation and education. This translated to a restructuring of up to 25% of the consumer loan book during the 2020 FY. Consequently, the non-performing loans (NPLs) to gross consumer loans ratio as at 31 December 2020 was 7.7%, significantly lower than the 22.6% ratio of 2019 but above our benchmark of 5%. As at the 2020 FYE, the cumulative loan loss provision was sufficient to cover 100% of the outstanding NPLs in the consumer portfolio. The Group's good performance in the collection of consumer loans in a pandemic year is noteworthy. We do not expect to see a significant increase in CSPG's consumer NPLs as product offerings are expanded to public sector employees and asset financing in the near term given the planned integration with Nigeria Inter-Bank Settlement System (NIBSS) and Remitta and collateralisation of asset finance loans.

As at the 2020 FYE, the Group's margin loans, which are collateralised by marketable securities stood at ₦1.0 billion. As at the same date, the market value of the securities provided as collateral for the margin loans was ₦2.2 billion or 2.2x the outstanding obligations, which provided good coverage in our view. The margin loan book did not record any NPLs in the period under review.

CSPG's portfolio of listed equities, which stood at ₦4.1 billion or 10.8% of the Group's total assets as at 31 December 2020, primarily comprised corporates and financial institutions that Agusto & Co. considers to be of investment grade credit quality. Notwithstanding, our analysis of the Group's equity portfolio shows marked risk due to concentration as the largest equity investment accounted for 46% of the portfolio or 32% of the Group's shareholders' funds while exposures to the banking industry equated to 53% of the portfolio. In our opinion, the high level of concentration in CSPG's equity portfolio raises the Group's susceptibility to stress in the operations of a single entity and the banking industry. However, we note that the largest equity investment was a strategic decision approved by the Group's management and based on unaudited accounts as at the end of Q1 2021, these investments had been sold down.

As at 31 December 2020, the Group's fixed income investments accounted for 4.8% of total assets and stood at ₦1.9 billion. This represented an 80% decline from ₦9 billion in the prior year due to the low yields in the financial markets as CSPG rebalanced the portfolio to increase exposures to higher-yielding instruments. The Group's bond portfolio as at 31 December 2020 comprised 76% FGN, State and Corporate bonds and 24% Eurobonds. Corporate bonds of investment grade credit quality accounted for the largest fraction or 50% of CSPG's portfolio while FGN bonds, which we consider to be of "Aaa" credit quality on our national scale, accounted for 28%. State government bonds accounted for the balance of 22%. Based on the unaudited accounts as at 31 March 2021, CSPG's fixed income portfolio stood at ₦5.9 billion, which represented a 221% growth from the 2020 FYE. We expect the fixed income portfolio to record sizable growth in 2021 as the yield environment in Nigeria improves.

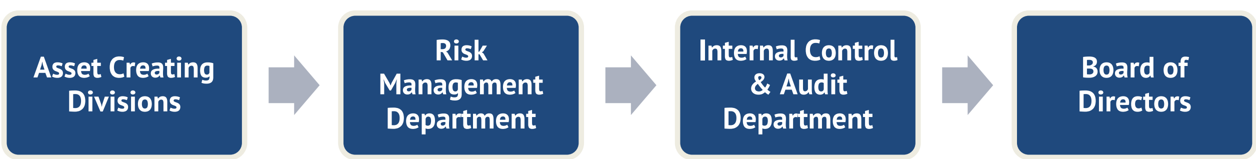
Overall, we believe CSPG's asset quality is acceptable.

RISK MANAGEMENT

CSPG's Board of Directors ("Board") has the overall responsibility for setting the Group's risk appetite and establishing the enterprise risk management framework. This is achieved through the Board Risk Management Committee ("RMC"), which is chaired by an independent director, Ms. Mairo Bashir. The RMC, comprising executive and non-executive board members, is responsible for monitoring CSPG's risk profile and strategy as approved by the Board. The RMC is supported by three management committees namely: Credit Review Committee, Asset & Liability Management Committee and Internal Audit & Risk Management Committee. CSPG operates a partially centralised risk management system with CS Advance Finance Company and CardinalStone Registrars having dedicated risk management staff, while the other companies in the Group are overseen by a single risk management team at the group level.

The first line of defence in CSPG's risk management structure is provided by the teams responsible for asset creation in the Group. The business heads overseeing these teams are responsible for ensuring that the risk standards approved by the Board are strictly adhered to. The risk management and internal control & audit departments serve as the second and third lines of defence respectively in the Group's risk management structure. The risk management and internal control & audit teams are responsible for providing independent risk oversight, monitoring and challenging the effectiveness of approved processes.

Figure 5: CSPG's Risk Management Structure



Source: CardinalStone Partners Limited

The proprietary trading team is responsible for managing CSPG's proprietary portfolio in line with the Proprietary Trading Policy ("PTP"), which sets the objective of preserving capital and maintaining return on investments by consistently seeking opportunities within the acceptable risk limit. The PTP only permits investments in equity instruments listed on local or international exchanges and fixed income securities in LCY or FCY. For equity instruments, the PTP classifies tradeable stocks into three buckets: low risk stocks, medium risk stocks and high risk stocks after considering key parameters such as stock liquidity, 5-year financial performance and outlook for the industry and business. The proprietary trading team can purchase low risk stocks subject to the maximum portfolio and sector limit. However, investments in stocks that fall under medium and high risk are to be advised by the risk management team (with the research team's guidance) on an annual basis. For investments in fixed income instruments, two stages of analysis are carried out. Firstly, the preliminary analysis, which relies on the external credit rating of the counterparty with the benchmark set at investment grade. The second stage of the analysis is the review of the issuer's profitability, liquidity, leverage and solvency ratios to assess the ability to repay obligations. This is followed by a review from the risk management team, who must grant the final approval before the investment is consummated.

The consumer lending business' underwriting team is responsible for generating risk assets for CS Advance Finance Company following the Credit Risk Management Policy ("CRMP"). The CRMP provides guidelines for the pricing of loans, lending process, documentation, loan provisioning, write-offs, recovery and foreclosure. Following the successful submission of client documentation including valid IDs and bank statements, a preliminary analysis is conducted by the business' underwriting team. The preliminary analysis focuses on the applicant's character and attitude towards repayment using the qualitative information available. The second stage of analysis is the risk evaluation, which focuses on quantitative metrics (customer's debt to income ratio, loan amount and credit history) and is conducted by the credit risk management team. The outcome of the risk evaluation is an obligor risk rating, which is used to decide whether to lend to an applicant. If the obligor credit risk rating is satisfactory, the application is approved by the risk management team and the loan is disbursed.

The structured finance team under the investment banking division of CSPL is responsible for generating risk assets relating to short- and medium-term funding for clients under the Structured Finance Credit Framework ("SFCF"). The team reviews and evaluates client applications using the Group's approved 3C evaluation metrics (Character, Collateral and Capacity). All financing applications are collateralised either by listed (equity and fixed income) investments that fall under CSPG's eligible securities or a commitment from the client's bank. Applications that meet the team's minimum criteria are sent to the risk management department and RMC for approval. Post-disbursement, the team conducts daily checks on the portfolio to ensure the collateral value (post-haircut) remains above the loan outstanding.

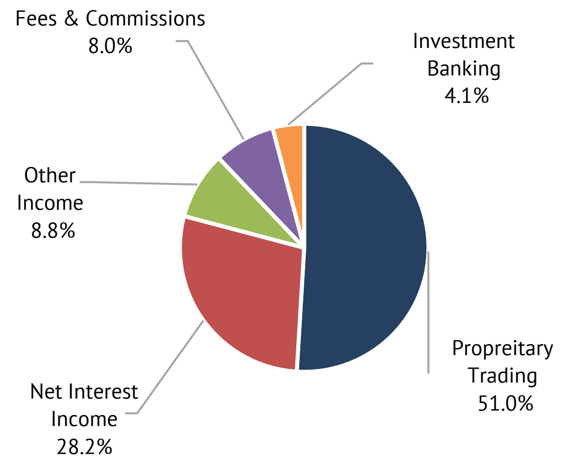
CSPG's risk management and internal control departments are responsible for reviewing credit applications, proprietary and asset management investment decisions and managing the Group's operational risks through the use of policies, controls and enterprise software applications. CSPG has separated the risk management and internal control units (which were hitherto combined) to improve service delivery and create independence for both functions. In Q1 2021, the Group strengthened its risk management capacity with the appointment of heads for the newly separated units. The new heads have since led a review of the Group's risk management framework and investment policies with a view to strengthen the risk monitoring processes. This review was concluded in the first half of 2021 and the Group is in the process of implementing the newly approved risk management framework. An internal audit exercise, reviewing the processes and controls of each of CSPG's businesses, is conducted at least once every year by the audit team at the group level.

In our opinion, CSPG's new risk management structure is suitable for current operations. However, its effectiveness remains untested.

EARNINGS AND PERFORMANCE

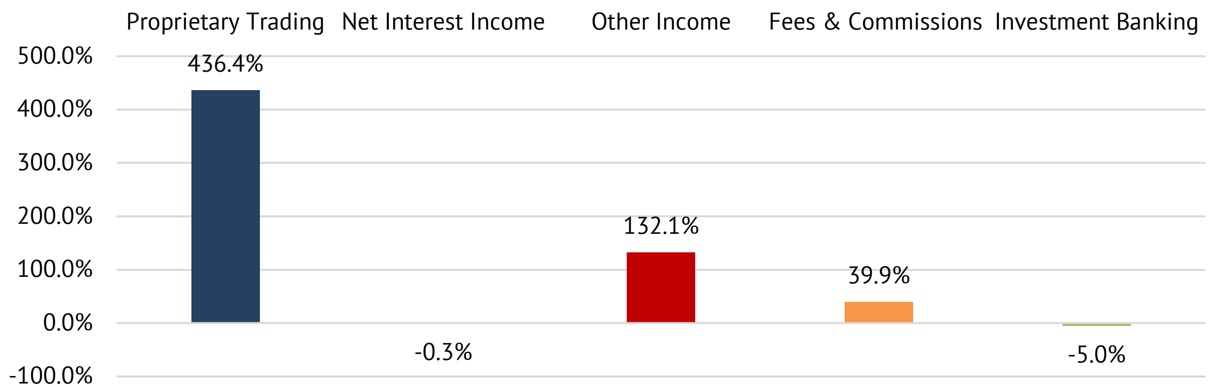
During the financial year ended 31 December 2020, CSPG generated net earnings of ₦5.8 billion, up 94% from ₦3.0 billion in the prior period. The Group's proprietary trading business with gains of ₦2.9 billion or a 51% share of net earnings was the largest source of income in 2020. The net interest income of ₦1.6 billion from the interest-bearing assets of all CSPG's business lines constituted the second largest fraction of net earnings at 28.2%. The Group's ₦0.5 billion in other income, which largely comprised dividend income and portfolio management fees, was the third largest contributor to net earnings with 8.8%. The fees and commission of the registrar and securities trading businesses accounted for 8% of CSPG's net earnings in 2020 while fees from the investment banking business made up the balance of 4.1%.

Figure 6: Net Earnings by Source



Source: CardinalStone Partners Limited

Figure 7: Performance of CSPG's Earning Sources (2020 v 2019)

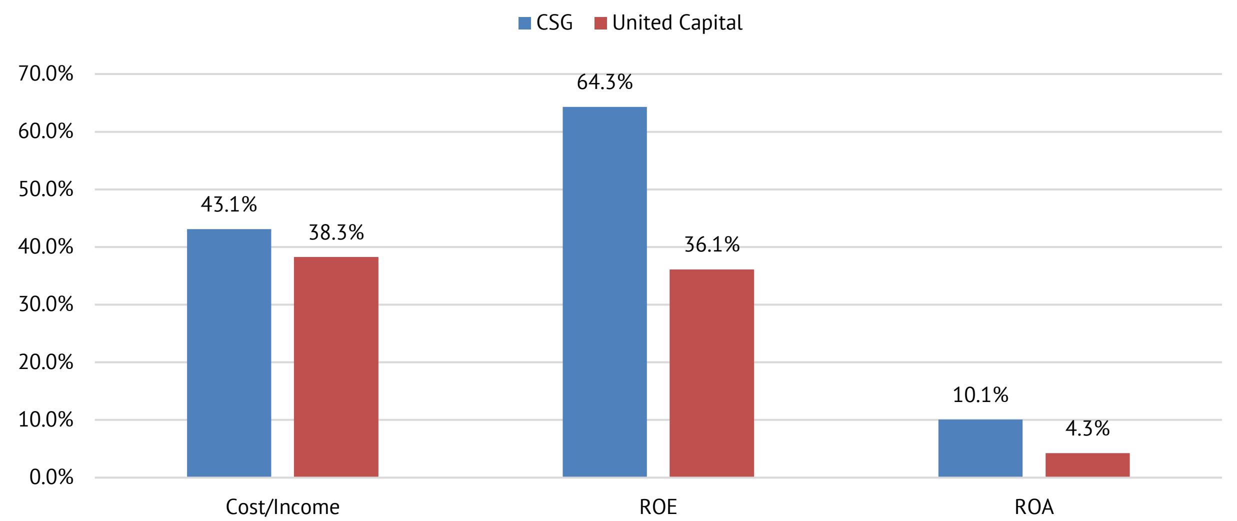


Source: CardinalStone Partners Limited

During the financial year ended 31 December 2020, CSPG's proprietary trading earnings, which represented trading income and gains from the Group's equity and fixed income portfolios, recorded a 436% growth from ₦0.5 billion generated in the prior period. The notable growth in CSPG's proprietary earnings was attributable to the standout performance of the stock market with the NSE All-Share Index closing 2020 up 50%. The low yields in the financial markets also drove increases in bond valuations. The Group's interest income recorded a small decline of 0.3% during the review period. This was largely attributable to CSPG's strategy to restrict growth in the consumer loan book due to the negative impact of the COVID-19 pandemic on the economy. The low money market yields also adversely impacted the interest income earned from placements with financial institutions.

Overall, we expect a moderate decline in the Group's earnings, primarily from the proprietary trading business given that 2020's performance was extraordinary, facilitated by the low money market and fixed income yields, which have risen gradually subsequent to the FYE. Nonetheless, we expect expansion of the registrar business' service offerings, the launch of collective investment schemes, strategic partnerships with foreign brokers and the commencement of the trustee business to support CSPG's earnings in the near term. The gradual increase in market yields in 2021 will also drive interest income.

Figure 8: Group Profitability Indicators (2020)



Source: CardinalStone Partners Limited, United Capital Plc

During the FYE 31 December 2020, the Group had operating expenses of ₦2.9 billion, which represented a 48% growth from ₦1.6 billion in the prior year. The notable increase in CSPG's operating expenses was largely due to costs incurred on publicity and branding and the higher staff bonus for the year. Nonetheless, in the review period, the Group recorded an improved cost to income ratio of 43.1%, down from 56.4% in 2019 largely due to the significant growth in net earnings in 2020. CSPG's cost to income ratio was, however, higher than the 38.3% recorded by peer, United Capital Group ('United Capital'), which runs a relatively leaner operation. We expect a moderate increase in the Group's cost to income ratio in the near term as CSPG implements expansion plans in a higher cost environment.

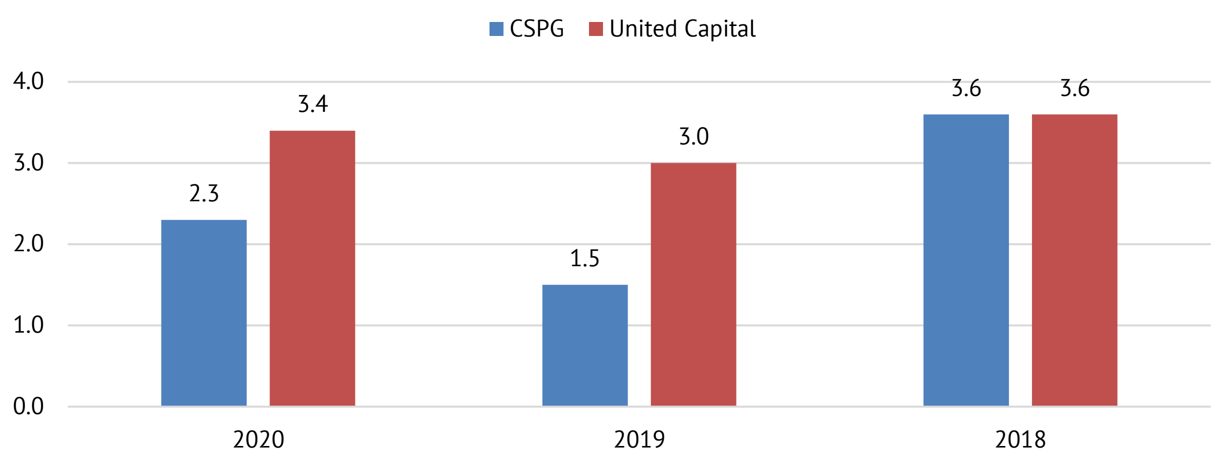
In 2020, the Group recorded a profit before tax of ₦3.3 billion, which was 2.75x the prior year's ₦1.2 billion. CSPG thus had much improved profitability ratios, with a pre-tax return on average equity (ROE) of 64.3% (2019 FY: 43.2%) and a pre-tax return on average assets (ROA) of 10.1% (2019 FY: 5.4%). The Group's ratios were significantly better than United Capital's pre-tax ROE and pre-tax ROA of 36.1% and 4.3% respectively. Based on unaudited accounts for Q1 2021, the Group's annualised profitability ratios have moderately declined with pre-tax ROE and pre-tax ROA of 45.4% and 7% respectively. We expect a moderate decline in the Group's profitability as the business continues to expand operations in a period of higher inflation and rising interest rate.

In our opinion, CSPG's profitability is good.

CAPITAL ADEQUACY & LEVERAGE

As at 31 December 2020, CSPG's shareholders' funds stood at ₦5.9 billion, up 35% from ₦4.3 billion at the end of the prior year. The increase in the Group's shareholders' funds was largely driven by higher retained earnings and minority interests, which grew by 103% and 26% respectively from the prior period. CSPG's businesses have maintained sufficient capitalisation to meet the regulatory minimum capital requirement for the respective capital or financial market operator licences as at 31 December 2020. Subsequent to the 2020 FYE, the Group's shareholders' funds have remained flat at ₦5.9 billion.

Figure 9: Group's Debt to Equity Ratio vs Peer (2018 – 2020)



Source: CardinalStone Partners Limited, United Capital Plc

Despite the increase in CSPG's shareholders' funds in 2020, the Group's core capital funded just 15% of total assets. This was due to the growth in CSPG's clients' FuM and interest bearing debt during the 2020 FY. Our estimate of (Basel I) adjusted capital to risk weighted assets ratio for CSPG stood at 24.4%, slightly lower than the previous year's 27% but better than our benchmark for capital market operators. When we subject the Group's adjusted capital to a stress test by excluding all related party loans (performing and non-performing) and consider only the core capital available to provide buffers for periods of uncertainty, CSPG's Basel I ratio declines to 18%, which is adequate in our view. As at 31 December 2020, the Group had a debt to equity ratio of 2.3 times (2019 FYE: 1.5 times), better than our benchmark of 3.0x. The jump in the debt to equity ratio was due to the short- and medium-term debt instruments (271-day commercial paper and 5-year bond) issued by

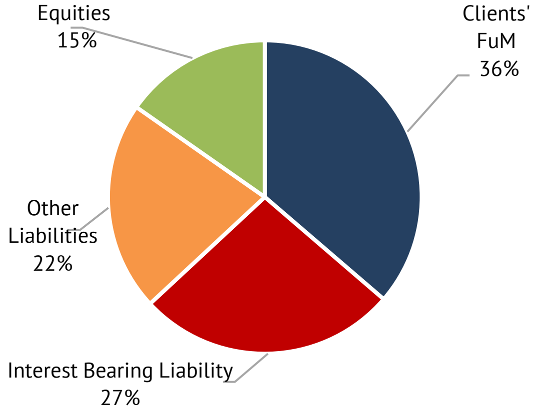
CSPG in 2020. However, the Group's debt to equity ratio remained lower than United Capital's 3.4 times as at the 2020 FYE. We expect leverage to rise above our benchmark of 3.0x in the near term as CSPG issues additional short-term debt under the ₦10 billion commercial paper programme.

Notwithstanding, we believe the Group's capital adequacy is acceptable for current business risks while leverage is satisfactory.

FUNDING AND LIQUIDITY

The Group's clients' FuM liabilities of ₦13.9 billion comprised term deposits in local currency (98%) and foreign currency (2%) of more than 350 individuals and organisations. There was some concentration in the Group's funding base, with the top 20 clients accounting for 39% of clients' funds under management (2019 FYE: > 50%). CSPG pays a (guaranteed) fixed interest rate on the term deposits which is calculated by marking up a relevant benchmark agreed with each client. The maturities of clients' local currency (LCY) term deposits are relatively short-tenured with 97% maturing within 365 days, while the balance of 3% is due in more than one year. As at 31 December 2020, the Group's interest bearing liabilities comprised CSPG's debut 5-year ₦5 billion bond and 270-day ₦5 billion commercial paper, which were issued in the review period. The Group's other liabilities at the 2020 FYE were 42% due in a year or less while the balance of 58% were due in more than one year.

Figure 10: Breakdown of CSGP's Liabilities



Source: CardinalStone Partners Limited

As at the 2020 FYE, CSPG had liquid assets totalling ₦22.8 billion, comprising FGN securities, money market placements and cash. This amounted to a 28% increase from ₦17.8 billion in the prior year. The growth in liquid assets was largely due to the yet-to-be-deployed proceeds from the Group's 5-year bond issued in Q4 2020 that were held in short-term placements with financial institutions at the year end. The liquid assets were sufficient to cover 103% of the Group's total clients' FuM and other liabilities as at the 2020 FYE. Our analysis of CSPG's liquidity management shows the Group's short term liquid assets were sufficient to meet obligations falling due within one year. Furthermore, CSPG recorded a liquid asset to total liabilities ratio of 70% and a liquid asset to total assets ratio of 67%, better than our benchmark of 60% for capital market operators.

In our opinion, CSPG's liquidity position and funding profile are good.

OWNERSHIP, MANAGEMENT & STAFF

CSPG is a private financial services group co-founded in 2008 by Messrs Femi Ogunjimi, Michael Nzewi, Mohammed Garuba and Mr Yomi Jemibewon. The co-founders jointly own 40.7% of the Group's equity via an investment company, CardinalStone Limited while other major shareholders of the Group are Bridgehampton Integrated Service Limited, Ifenwona Investments Limited, Mr Fola Adeola and Chizzy Nigeria Limited. The remainder of CSPG's shares is held by 10 other individuals and organisations. In our opinion, the Group's ownership is reasonably diversified and comprises individuals with a significant experience in the financial services industry in Nigeria.

Table 3: Ownership of CSPG

Shareholders	Shareholding
CardinalStone Limited	40.7%
Bridgehampton Integrated Service Limited	16.8%
Ifenwona Investments Limited	8.3%
Mr Fola Adeola	8.2%
Chizzy Nigeria Limited	5.2%
Others	20.8%

Source: CardinalStone Partners Limited

CSPG's activities are governed by an eight-member Board of Directors ("Board"), comprising six non-executive directors (including two independents), the Group Managing Director and the Group Executive Director. The Board is chaired by Mr Fola Adeola and members of the Board jointly own 54.3% of CSPG's equity. In our opinion, the Board has a good mix of non-executive and independent directors with adequate representation of CSPG's shareholders. The Board has two standing committees: the Finance, Credit & Risk Management Committee and the Corporate Governance Committee, which meet at least four times a year and are chaired by independent directors. The committees are, in our view, well composed with three non-executive directors (two of which are independent directors) and either the Group Managing Director or Group Executive Director.

Table 4: Key Functions of the Board's Committees

S/N	Board Committee	Key Function	Composition
1.	Finance, Credit & Risk Management Committee	The committee considers and advises the Board on finances, financial policy, financial and other risk exposures of CSPG from time to time.	▪ Ms Mairo Bashir (Chair) ▪ Mr Asue Ighodalo ▪ Mr Yomi Jemibewon ▪ Mr Mohammed Garuba
2.	Corporate Governance, Remuneration & Governance Committee	The committee sets the corporate governance standards, code of business conduct and ethics applicable to the Group. In addition, the committee oversees the employment, remuneration and evaluation of top management.	▪ Mr Asue Ighodalo (Chair) ▪ Ms Mairo Bashir ▪ Mr Femi Ogunjimi ▪ Mr Michael Nzewi

Source: CardinalStone Partners Limited

The operations of CSPG are overseen by the Group's Managing Director/CEO, Mr Nzewi. The Group MD/CEO is supported by the Group Executive Director, Mr Garuba, who also serves as the Managing Director of the asset management business. The three other operating subsidiary businesses: registrar, securities trading and consumer lending, are led by a Chief Business Strategist, Managing Director and Ag. Managing Director respectively. In our view, the Group's executive management team has significant capacity with an average of over two decades of experience in the financial services industry.

Table 5: CSPG's Staff Productivity (2018-2020)

CSPG	2020	2019	2018
Average number of employees	143	145	112
Staff cost per employee (₦'000)	8,402	5,643	6,269
Net earnings per staff (₦'000)	40,216	20,458	17,531
Net earnings/staff cost	4.8x	3.6x	2.8x
Staff cost/Net income	21%	28%	36%
Staff cost/Operating expenses	48%	49%	52%

Source: CardinalStone Partners Limited

During the 2020 FY, CSPG had an average staff strength of 143 employees (2019: 145). Our review of the Group's staff productivity indicators for the year showed net earnings per staff was ₦40.2 million (2019 FY: ₦20.5 million), which was significantly lower than United Capital's ratio of ₦137.0 million in the same period. CSPG's net earnings in 2020 covered staff cost 4.8 times, which was significantly lower than the 9.5x recorded by peer United Capital but higher than our benchmark of 3x for asset management companies.

In our opinion, the Group's management is well qualified and experienced while staff productivity is satisfactory.

OUTLOOK

The Nigerian economy has started showing early signs of recovery from the impact of the COVID-19 pandemic as businesses adjust to the new realities. The yields in the money market have gradually increased in the first half of the year as the Federal Government of Nigeria has gradually increased local currency borrowings to fund the 2021 budget. The OPEC basket price has also improved to an average of $60 per barrel during the same period compared to $41 in 2020. However, the heightened insecurity across the country and unfavourable regulatory policies from the fiscal and monetary authorities in Nigeria have dampened investors' confidence. This has translated to a significant dip in foreign portfolio investments by 77.4% (YoY) to US$974.1 million in Q1 2021. While we remain optimistic and expect better economic performance in comparison to 2020, we believe this will be hinged on favourable economic policies, enhanced investors' confidence and improved security in the country.

The Nigerian equities market has remained bearish since the start of the year following massive sell-offs in Q1 2021, with the NSE All-Share Index declining by 7.9% (YTD – 30 June 2021). In our view, the performance of the equities market in H2 2021 will largely depend on the direction of CBN's monetary policy and yields in the financial markets. Notwithstanding the aforementioned challenges, Agusto & Co. expects the demand for the Group's bouquet of financial services to remain positive, particularly the fixed income investment notes, as retail investors seek returns closer to the average inflation rate of 17.6% in 2021. We believe the Group's structured finance loan, asset management and (new) trustee businesses will drive asset growth in the near term. However, we believe the Group's earnings will moderate in 2021 given that performance in 2020 was exceptional. Furthermore, we expect CSPG's liquidity and funding profile to remain good, supported by the Group's record in the Nigerian debt capital market, while CSPG's capitalisation is expected to provide adequate buffers as the businesses continue to grow.

Based on the above, we hereby attach a **stable** outlook to the rating.

Financial Summary

STATEMENT OF FINANCIAL POSITION AS AT	31-Dec-20		31-Dec-19		31-Dec-18	
	₦'000		₦'000		₦'000	
ASSETS						
Cash & bank balances	12,853,794	33.5%	2,215,965	8.3%	1,166,477	5.5%
Short term investments	13,693,086	35.7%	15,576,709	58.3%	12,168,336	57.5%
Direct loans & advances - net	2,437,144	6.4%	2,362,877	8.8%	1,371,328	6.5%
Advances under finance leases - net			-	0.0%	-	0.0%
Total loans (net)	2,437,144	6.4%	2,362,877	8.8%	1,371,328	6.5%
Total other assets	2,846,428	7.4%	2,518,647	9.4%	3,466,169	16.4%
Funds under management (FUM)	5,576,773	14.5%	3,192,491	11.9%	2,585,195	12.2%
Total other long term investments	250,000	0.7%	250,000	250,000	0	0.0%
Total fixed assets & intangibles	692,071	1.8%	615,603	2.3%	407,633	1.9%
TOTAL ASSETS	**38,349,296**	**100%**	**26,732,292**	**100%**	**21,165,138**	**100%**
LIABILITIES & EQUITY	₦'000		₦'000		₦'000	
Total interest bearing liabilities	10,263,867	26.8%	661,388	2.5%	609,677	2.9%
Total other liabilities	8,305,507	21.7%	5,604,788	21.0%	5,361,256	25.3%
Funds under management (FUM)	13,924,241	36.2%	16,143,549	60.4%	13,524,624	63.9%
Total liabilities	32,493,615	84.7%	22,409,725	83.8%	19,495,557	92.1%
Share Capital	317,842	0.8%	317,842	1.2%	250,000	1.2%
Share Premium	2,183,447	5.7%	2,183,447	8.2%	242,500	1.1%
Statutory Reserve	23,617	0.1%	2,934	0.0%	-	0.0%
Irredeemable Debentures	578,079	1.5%	458,667	1.7%	387,968	1.8%
Revaluation Surplus	15,714	0.0%	(5,174)	0.0%	(5,606)	0.0%
Bonus Issue Reserve		0.0%	-	0.0%	-	0.0%
Other Non-distributable Reserves	(38,560)	-0.1%	0	0.0%	0	0.0%
Revenue Reserve	2,775,542	7.2%	1,364,851	5.1%	794,719	3.8%
Shareholders' equity	5,855,681	15.3%	4,322,567	16.2%	1,669,581	7.9%
TOTAL LIABILITIES & EQUITY	**38,349,296**	**100%**	**26,732,292**	**100%**	**21,165,138**	**100%**

INCOME STATEMENT FOR THE YEAR ENDED	31-Dec-20		31-Dec-19		31-Dec-18	
	₦'000		₦'000		₦'000	
Portfolio Management	116,088	1.5%	38,653	0.9%	90,078	2.9%
Securities Trading & Dealing	2,930,889	38.8%	546,382	12.7%	(10,707)	-0.4%
Financial Advisory	236,877	3.1%	249,354	5.8%	117,431	3.8%
Fees & Commissions	460,303	6.1%	328,971	7.7%	374,939	12.3%
Other income	387,469	5.1%	178,266	4.1%	292,041	9.6%
Investment income	4,131,626	54.7%	1,341,626	31.2%	863,782	28.3%
Interest income	3,424,882	45.3%	2,955,747	68.8%	2,193,699	71.7%
Interest expense - clients	(1,805,687)	-23.9%	(1,330,940)	-31.0%	(1,094,021)	-35.8%
Net interest income	1,619,195	21.4%	1,624,807	37.8%	1,099,678	36.0%
Net earnings	**5,750,821**	**76.1%**	**2,966,433**	**69.0%**	**1,963,460**	**64.2%**
Staff costs	(1,201,431)	-15.9%	(818,172)	-19.0%	(702,161)	-23.0%
Depreciation expense	(115,380)	-1.5%	(70,921)	-1.7%	(66,612)	-2.2%
Other operating expenses	(1,161,944)	-15.4%	(783,342)	-18.2%	(580,972)	-19.0%
Total operating expenses	(2,478,755)	-32.8%	(1,672,435)	-38.9%	(1,349,745)	-44.1%
Profit (loss) before taxation	3,272,066	43.3%	1,293,998	30.1%	613,715	20.1%
Tax (expense)/benefit	(405,232)	-5.4%	(226,819)	-5.3%	(351,746)	-11.5%
Profit (loss) after taxation	**2,866,834**	**37.9%**	**1,067,179**	**24.8%**	**261,969**	**9%**
Non -operating income (expense) - net						
Statutory reserve	18,319	0.2%				
Capital redemption						
Proposed dividends	(1,271,369)	-16.8%	(400,000)	-9%	(400,000)	-13%
Script issues						
Other appropriations/adjustments	(202,650)	-2.7%	(97,047)	-2.3%	-184,120	-6%
Retained profit	**1,411,134**		**570,132**		**(322,248)**	
Profit retained b/fwd	1,364,408		794,719		(856,117)	
Profit retained c/fwd	2,775,542		1,364,851		(1,178,365)	
Gross earnings	7,556,508		4,297,373		3,057,481	

KEY RATIOS AS AT		31-Dec-20		31-Dec-19		31-Dec-18
PROFITABILITY						
Revenue Growth		93.9%		51.1%		-8.9%
Operating profit margin		43.3%		30.1%		20.1%
Operating expenses/ net earnings		43.1%		56.4%		68.7%
Return on average equity (pre-tax)		64.3%		43.2%		33.1%
Return on average assets (pre-tax)		10.1%		5.4%		3.2%
Gross earnings/Total assets & contingents (average)		23.2%		17.9%		15.9%
LIQUIDITY & FUNDING						
Liquid assets/total assets		84%		78%		75%
Liquid assets/short term IBD		457%		6288%		3568%
Liquid assets/Managed funds		231%		130%		117%
Adjusted capital & long term debt/illiquid assets		1021%		601%		478%
CAPITAL & LEVERAGE						
Adjusted capital/risk weighted assets		27%		30%		16%
Gross debt/equity (times)		2.3		1.5		3.6
Gross debt/Adjusted equity (times)		5.8		5.6		11.8
IBD (net of cash) as % of equity without revaluation		-208%		-302%		-760%
IBD (net of cash) as % of adjusted capital		-105%		-47%		-44%
Interest cover (times)		1.5		1.1		1.2
STAFF INFORMATION						
Average number of employees		143		145		112
Staff cost per employee (N'000)		8,402		5,643		6,269
Net earnings per staff (N'000)		40,216		20,458		17,531
Staff cost/Net earnings		21%		28%		36%
Staff costs/Operating expenses		48%		49%		52%
OTHER KEY INFORMATION						
Year operations started		2008		2008		2008
Age (in years)		12		11		10
Number of offices		6		6		6

Rating Definitions

Aaa	A financial institution of impeccable financial condition and overwhelming capacity to meet obligations as and when they fall due. Adverse changes in the environment (macro-economic, political and regulatory) are unlikely to lead to deterioration in financial condition or an impairment of the ability to meet its obligations as and when they fall due. In our opinion, regulatory and/or shareholder support will be obtained, if required.
Aa	A financial institution of very good financial condition and strong capacity to meet its obligations as and when they fall due. Adverse changes in the environment (macro-economic, political and regulatory) will result in a slight increase the risk attributable to an exposure to this financial institution. However, financial condition and ability to meet obligations as and when they fall due should remain strong. Although regulatory support is not assured, shareholder support will be obtained, if required.
A	A financial institution of good financial condition and strong capacity to meet its obligations. Adverse changes in the environment (macro-economic, political and regulatory) will result in a medium increase in the risk attributable to an exposure to this financial institution. However, financial condition and ability to meet obligations as and when they fall due should remain largely unchanged. In our opinion, shareholder support should be obtainable, if required.
Bbb	A financial institution of satisfactory financial condition and adequate capacity to meet its obligations as and when they fall due. It may have one major weakness which, if addressed, should not impair its ability to meet obligations as and when due. Adverse changes in the environment (macro-economic, political and regulatory) will result in a medium increase in the risk attributable to an exposure to this financial institution.
Bb	Financial condition is satisfactory and ability to meet obligations as and when they fall due exists. May have one or more major weaknesses. Adverse changes in the environment (macro-economic, political and regulatory) will increase risk significantly.
B	Financial condition is weak but obligations are still being met as and when they fall due. Has more than one major weakness and may require external support, which, in our opinion, is not assured. Adverse changes in the environment (macro-economic, political and regulatory) will increase risk significantly.
C	Financial condition is very weak. Net worth is likely to be negative and obligations may already be in default.
D	In default.

Rating Category Modifiers

A "+" (plus) or "-" (minus) sign may be assigned to ratings from 'Aa' to 'C' to reflect comparative position within the rating category. Therefore, a rating with + (plus) attached to it is a notch higher than a rating without the + (plus) sign and two notches higher than a rating with the - (minus) sign.

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