Nigeria Mortgage Refinance Company Plc

Final Rating Report

Agusto&Co.

Research, Credit Ratings, Credit Risk Management

Nigeria Mortgage Refinance Company Plc

Ratings

Issue: ₦11 Billion Secured Series II Bond – $Aaa_{(NG)}$

The rating will be monitored throughout the tenure of the bond and is subject to an annual review.

Issuer: A+

Issue Date: 13 March 2018

Expiry Date: 30 June 2019

Industry:
Mortgage Banking

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RATING RATIONALE

Agusto & Co. has assigned a **"Aaa"** rating to the Nigeria Mortgage Refinance Company's ("NMRC" or "The Company") ₦11 billion, 15-year, Second Series Bond ("the Issue" or "the Bond"). The Bond is the second tranche under the Company's ₦440 billion debt issuance programme. The proceeds will be applied to refinance or purchase conforming mortgage loans created by eligible mortgage lenders. The Bond's coupon shall be paid quarterly, with principal also amortised quarterly. The Rating is supported by the unconditional and irrecoverable guarantee issued by the Federal Government of Nigeria for the due and punctual performance by the Issuer of all its payment obligations in relation to notes issued by the NMRC for an amount not exceeding ₦100 billion. The Bond will rank pari passu with present and future outstanding unsecured and unsubordinated obligations of the Issuer and the guarantor (the Federal Government of Nigeria).

Agusto & Co. has also assigned an **A+** Issuer rating to the Nigeria Mortgage Refinance Company. The standalone credit rating is supported by the Company's good financial position and business profile as the only mortgage refinance company registered in Nigeria. The rating reflects NMRC's good asset quality, strong capital adequacy, ample liquidity levels and satisfactory profitability. The Company's unfettered market access and shareholder support have also been factored into the rating.

With the proceeds of an initial bond issuance fully applied to purchase/refinance mortgage loans from eligible mortgage lenders in 2016, NMRC's credit strength has remained intact – with no delinquencies as at 31 December 2017. Achieving this during the recent period of economic stress partly reflects the Company's prudent management and an effective risk management framework. Though synonymous with the Industry at large, we note that the mortgage refinance portfolio is concentrated in two cities – Lagos and Federal Capital Territory, Abuja. Even though these are the most economically developed mortgage and real estate markets, the NMRC's national mandate, in our view, should eventually lead to a more diversified portfolio. Overall, we expect that the Company will increase lending significantly over the next two years, with low loss norms upheld by conservative underwriting standards

The NMRC's capitalisation is strong with a CAR of 126.0% as at FYE 2017 (2016: 95.5%). The Company's leverage ratio stood at 27.7%, higher than the 5% minimum prescribed by the Central Bank of Nigeria (CBN) (2016: 21.1%). The CAR has trended upwards in the last two years due to growth in equity. In 2017 specifically, shareholders' funds increased by ₦3.2 billion through accretion of reserves and injection of additional equity. In our opinion, the Company is well capitalised for the level of business risk undertaken, with significant capacity to take on additional risk assets in the near to medium term.

NMRC's management of liquidity is sound, aided by the high level of liquid assets the Company holds on its balance sheet – which translated to a liquidity ratio of 74.8% at FYE 2017 and a loan-to-funding ratio of 2.3 times (FYE 2016: 1.9 times). We recognise that the strong liquidity profile is supported by long term borrowings from the World Bank totalling ₦22.8 billion, with total borrowings funding 70.9% of total assets as at FYE 2017. These liquid assets comprise FGN bonds and treasury bills (rated Aaa nationally) and cash. The Company's debt service coverage ratio stood at 9 times, (FYE 2016: 10 times) – reflective of a strong ability to meet debt obligations maturing within the next 12 months. The debt coverage ratio is expected to weaken slightly in line with the anticipated rise in borrowings from the issuance of the series II Bond and a Sukuk in 2018. However, it should remain good in our view.

The Company's profitability is on the uptick, supported by higher yields on investments. Net earnings grew by 33% to ₦3.9 billion from the prior year – with a higher portion of 20% due to core refinancing activities. The cost profile is fairly heightened but was offset by higher earnings during the period. The Bank's cost-to-income ratio of 52% remains below the internal target of 60%, albeit high, given the current low base of operations. In the FYE 2017, NMRC's pre-tax return on average assets (ROA) and pre-tax return on average equity (ROE) rose to 4.6% (2016: 3.2%) and 18.6% (2016: 15.7%). Overall, profitability is expected to improve as the Company grows its portfolio of refinanced loans while keeping operating costs low. Elevated yields on government instruments also support our outlook for improved profitability. Overall, Agusto & Co is of the opinion that on a standalone basis the NMRC possesses adequate capacity to meet the short term obligations on its borrowings.

NMRC is yet to achieve its medium term goals mainly due to the economic stress Nigeria has experienced in the last two years and structural weaknesses in the mortgage and real estate market. Nonetheless, the Company is actively pursuing the mandate of developing the primary and secondary mortgage markets in Nigeria. In addition to raising long-term funds from the local capital market, a number of initiatives are underway to strengthen the weak structure surrounding mortgage lending in Nigeria and provide a pipeline of potential mortgages to be financed. The Company's impact on the mortgage industry in Nigeria should become more visible in the medium term as these initiatives come on-stream.

Figure 1: Strengths, Weakness and Challenges

Strengths
- Support from the Federal Government of Nigeria
- Strong capital adequacy
- Good asset quality
- Ample liquidity levels
- Good profitability
- Good governance structure
- Support from member mortgage banks

Weaknesses
- Low contribution to income from core business
- Geographical concentration within the mortgage refinance portfolio

Challenges
- Ensuring a sizeable pool of qualifying mortgage loans to refinance.
- Overcoming bottlenecks to land titling

Table 1: Background Information

Financial Information

Year Ended 31 December	2017	2016
Total Assets	₦42.6 billion	₦40.8 billion
Gross Earnings	₦6.3 billion	₦5.2 billion
Pre-tax return on average assets	4.6%	3.2%
Pre-tax return on average equity	18.6%	15.7%

Source: Nigeria Mortgage Refinance Company

Overview of the Nigerian Mortgage Banking Industry

The Nigerian Mortgage Industry has grown considerably since 2014, with gross loans recording a compound annual growth rate (CAGR) of 35%[1] between 2014 and 2017. The Industry recorded higher growth in 2014 and 2015 due to the recapitalization of mortgage banks in 2014 and the commencement of operations of the Nigeria Mortgage Refinance Company (NMRC) in 2015. However, industry growth slowed in 2016 and remained subdued in 2017, attributable to the weak macroeconomic climate - evidenced by a higher interest rate environment, inflationary pressures, rising unemployment and lower consumer purchasing power. The Industry's total assets stood at ₦363 billion in June 2017, a 5% dip from ₦384 billion as at December 2016[2].

Nigeria's mortgage finance as a share of GDP currently stands at 0.9%, a reflection of the country's low mortgage penetration rate of 0.6% - comparing less favourably to other emerging economies such as India (9%), Indonesia (10%), Kenya (3%) and South Africa (31%)[3]. We anticipate a moderate growth in the volume of mortgage loans in 2018, as improving macroeconomic conditions should have a positive impact on the Industry.

Currently, 36 Primary Mortgage Banks (PMBs) are licensed to grant mortgage loans and related services in Nigeria. Of the thirty-six PMBs, 26 are licensed to operate within single states, while 10 operate with a national license. Prior to 2010, PMBs were permitted to engage in a variety of non-core mortgage banking activities. Industry operators emphasized that the absence of long-term finance contributed to the lack of innovation in financial products to accommodate clients in the lower income segments. Accordingly, PMBs were limited in their ability to respond to market demand in that space and thus, focused on non-lending services. With industry operators currently prohibited from the aforementioned services, profitability and competitiveness within the Industry has been adversely impacted – given that commercial banks are allowed to engage in mortgage lending.

The establishment of the Nigeria Mortgage Refinance Company (NMRC) was expected to improve the fortunes of the Industry, through the introduction of mortgage refinancing. As at December 2017, NMRC had refinanced mortgages amounting to ₦8 billion, exhausting the first ₦8 billion bonds raised from the domestic market. However, the pool of refinanced mortgages remains low with total refinanced mortgages accounting for less than 5% of the Industry's loan portfolio. This is directly attributable to the limited number of eligible mortgage loans, with NMRC only refinancing loans that conform to the Company's uniform underwriting standards. Furthermore, only 20 PMBs are members, with less than half of these institutions currently amongst the Company's beneficiaries.

While we take cognizance of the activities of the NMRC, prevalent challenges within the Industry remain detrimental to the development of the mortgage lending in Nigeria. These include high cost of funds, expensive land titling procedures and low income levels. We believe these issues must be addressed to ensure sustainable growth and progression within the Industry.

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[1] Agusto & Co., CBN
[2] Agusto & Co Mortgage Banking Industry Report
[3] 'Unleashing the Housing Sector in Nigeria and in Africa' by Dr. Ngozi Okonjo-Iweala at the 6th Global Housing Finance Conference World Bank Headquarters, Washington, DC. Wednesday, 28th May, 2014

COMPANY PROFILE

The Nigerian Mortgage Refinance Company ('NMRC' or 'the Company') is a private sector driven mortgage refinance company with a public objective of promoting home ownership by providing long term funding to operators in the Nigerian mortgage industry. NMRC was incorporated on 24 June 2013, as a public limited liability registered with the Securities and Exchange Commission (SEC) with an approval in principle from the Central Bank of Nigeria. NMRC subsequently obtained a final operating license from the CBN on 18 February 2015 and commenced operations in the same year.

NMRC is a public private partnership arrangement between the Federal Government of Nigeria (FGN) and the private sector. The FGN through the Federal Ministry of Finance (FMOF) and the Nigerian Sovereign Investment Authority (NSIA) holds the single largest equity stake in the Company with a joint 36.5% shareholding as at November 2017, while the balance of 63.4% is held by 20 PMBs (52.3%), four commercial banks (9.8%) and one non-bank financial institutions (1.3%)[4].

Table 2: Shareholding Structure

S/N	Institution	% Shareholding
1	Nigerian Sovereign Investment Authority	20.91%
2	Ministry of Finance Incorporated	15.68%
3	Homebase Mortgage Bank Limited	13.07%
4	Trust Bond Mortgage Bank Plc	7.84%
5	FHA Homes Ltd	6.53%
6	Sterling Bank Plc	3.92%
7	Infinity Trust Mortgage Bank	2.98%
8	Abbey Mortgage Bank Plc	2.61%
9	Access Bank Plc	2.61%
10	Imperial Homes Bank Limited	3.45%
11	Heritage Bank Ltd	1.96%
12	Resort Savings & Loans	1.31%
13	Haggai Mortgage Bank Ltd	1.31%
14	Jubilee Mortgage Bank Ltd	1.31%
15	May Fresh Mortgage Bank Limited	1.31%
16	New Prudential Mortgage Bank Limited	1.31%
17	Nigeria Police Mortgage Bank	1.31%
18	Platinum Mortgage Bank Limited	1.31%
19	Refuge Home Savings & Loans Limited	1.31%
20	Stanbic IBTC Investment	1.31%
21	SunTrust Bank Nigeria Limited	1.31%

[4] NMRC's ownership base expanded from 21 as at 31 December 2017 to 27 shareholders as at November 2017 as an additional six PMBs invested in the Company.

22	FBN Mortgages	1.17%
23	Brent Mortgage Bank Limited	0.84%
24	Gateway Savings & Loans Limited	0.84%
25	Omoluabi Mortgage Bank Plc	0.84%
26	Lagos Building & Investment Co. Ltd	0.84%
27	Delta Mortgage Bank Limited	0.84%

Source: Nigeria Mortgage Refinance Company

Business Strategy

NMRC was established to bridge the funding cost of residential mortgages and promote the availability and affordability of good housing to Nigerians by boosting the liquidity of the mortgage industry through PMBs and commercial banks. The Company aims to develop the primary and secondary mortgage markets by raising long-term funds from the capital market and thus providing access to affordable housing finance in Nigeria.

NMRC's strategy involves working across the value chain, spearheading and advocating changes that will create a positive environment for mortgage lending and increased home ownership. Accordingly, the Company continues to strengthen and deepen its partnership with key stakeholders across the Industry including PMBs, Mortgage Warehouse Funding Limited (MWFL), Real Estate Developers Association of Nigeria (REDAN) and the Federal Mortgage Bank amongst others. NMRC plans to expand mortgage coverage in Nigeria, targeting 180,000 to 200,000 new mortgages by 2020 through increased capital access, improved competencies and operational efficiency within the Industry. As at FYE 2017, NMRC had refinanced 456 mortgage loans.

Key initiatives aimed at achieving the above-mentioned goals include the establishment of the Housing Market System comprising the Mortgage Market System and Hosing Market Information Portal (a web based software aimed at enhancing the efficiency of the mortgage industry and stakeholder integration), sensitization campaigns using adverts on radio stations and the development of underwriting standards for the informal sector.

Operations

NMRC aims to achieve its objectives by raising long term funds from the domestic debt capital market to refinance existing mortgage loans issued by PMBs and commercial banks. The Company purchases qualifying mortgage loans from participating PMBs and commercial banks, to provide mortgage lenders with longer tenured and relatively affordable funding to increase residential mortgage penetration. As at December 2017, NMRC had refinanced mortgages amounting to ₦8 billion, from the series I ₦8 billion bonds issued in 2015. NMRC's refinancing operations are currently restricted to member institutions, which has limited the pace at which the Company can refinance mortgage loans. In addition, NMRC has defined a set of uniform underwriting standards (UUS) which serve as the minimum acceptance criteria for qualification for refinancing mortgage loans. Thus, only qualifying residential mortgage loans (that have met this UUS) from participating institutions can be refinanced by the Company.

Business Structure

NMRC runs a simple business structure as the Company's operations are currently limited to mortgage refinancing within a restricted pool of participating mortgage lenders. The Company is structured along two core functions - Finance and Policy, Strategy & Partnerships, each of which is headed by an Executive Director. The Managing Director has direct oversight of the Company's Risk Management and Information Technology units, while the heads of support units; Company Secretariat/Legal and Internal Audit report directly to the Board of Directors (with dotted reporting lines to the Managing Director).

As at 31 December 2017, the NMRC had a staff strength of 30 individuals, a rise from 28 employees recorded in the previous year. NMRC has no subsidiaries or affiliates and the Company is headquartered at 18, Mississippi Street, Maitama, Abuja with one operating office in Victoria Island, Lagos.

NMRC is registered by SEC and regulated by CBN as a non-bank financial institution. The Company operates with a Mortgage Refinance license issued by the Central Bank of Nigeria.

Governance

NMRC is governed by a 13 member Board of Directors, comprising three executive directors and 10 non-executive directors. The Board is chaired by an independent member - Charles C. Okeahalam, PhD, who serves as the Managing Director and Chief Executive Officer at AGH Capital Group[5]. In addition to the Chairman, the Board has three independent non-executive directors.

The Federal Government has just two representatives on the Board of Directors. The Board has a good mix of executive and non-executive directors and a sufficient number of independent members. In addition, we believe members of the Board are qualified and have the requisite experience to foster effective governance of the Company's activities – with a number of members being senior executives of reputable financial institutions. The composition of the Board aligns with corporate governance best practice.

Table 3: NMRC Board of Directors

DIRECTORS	STATUS	DIRECT SHAREHOLDING
Charles C. Okeahalam, Phd	Chairman, Independent Member	Nil
Professor Charles Inyangete	CEO, NMRC – Managing Director	Nil
Mr Kehinde Ogundimu	CFO, NMRC – Executive Director	Nil
Dr Chika Akporji	Executive Director	Nil
Mr Herbert Wigwe	Non – Executive Director, Representing Access Bank	Nil
Mrs Fatima Wali-Abdurrahman	Non – Executive Director, Independent Member	Nil
Mr Adeniyi A. Akinlusi	Non – Executive Director, Representing Trust Bond Mortgage Plc	Nil
Dr. Femi Johnson	Non – Executive Director, Representing Home Base Mortgage Bank Limited	Nil

[5] An investment holding company with interests in the private equity, mining, marine and property sectors

Mr Charles Adeyemi Candide-Johnson	Non – Executive Director, Independent Member	Nil
Mr Uche Orji	Non – Executive Director, Representing Sovereign Investment Authority	Nil
Dr. Bakari Wadinga	Non – Executive Director, Representing Federal Ministry of Finance	Nil
Dr. Anino Emuwa	Non – Executive Director, Independent Member	Nil
Mr Razak Adeyemi Adeola	Non – Executive Director, Representing Sterling Bank Plc	Nil

Source: Nigeria Mortgage Refinance Company

Management Team

NMRC's management team is headed by Professor Charles Inyangete – the Managing Director of the Company. He has over 20 years' experience in banking, finance, capital market operations, economic reforms and risk management amongst others, gained both within and outside Nigeria. Prior to his appointment as Managing Director, Inyangete served as the founding chairman of Vertex Financial Services Limited, where he spearheaded the merger of Vertex with African Harvest.[6] He also served as a non-executive (independent) director and the chairman of the strategy and risk committee of Exim Bank[7] from 2001 to 2008. In 2003, Professor Inyangete developed regional benchmarks and a framework for Sovereign Assets and Liability Management for the ten-member states of the Eastern and Southern African Macro Economic & Financial Management Institute (MEFMI). He was also on a panel for developing a national housing and mortgage finance policy for Tanzania and the Chair of the Technical Working Group for the National Mortgage Finance Initiative of the National Social Security Fund (NSSF), which developed a framework for mortgage finance in Tanzania.

Professor Inyangete holds a PhD in Finance from the University of Strathclyde, Glasgow United Kingdom.

Other members of the Company's executive management team include:

- Mr Kehinde Ogundimu - Executive Director, Chief Financial Officer
- Dr Chika P. Akporji – Executive Director, Policy, Strategy & Partnerships

Correspondent Banks

NMRC maintains correspondent banking relationships with the following banks:

- Sterling Bank Plc. – *maintains a 3.92% equity stake*
- Access Bank Plc. – *maintains a 2.61% equity stake*
- Standard Chartered Bank Limited
- Stanbic IBTC Bank Limited

[6] A Johannesburg Stock Exchange (JSE) listed company

[7] Exim Bank, Tanzania

Information Technology

The Company uses the 'Fintrak' software for treasury operations, including transaction recording and monitoring. The software provides an end to end solution for NMRC's treasury function, from asset acquisition to disposal. NMRC recently acquired the Mortgage Market System (MMS), an internet based bespoke software for core mortgage refinancing activities. MMS provides an end-to-end solution for housing finance by enabling the seamless integration of all stakeholders in the housing finance system. MMS has been deployed to three participating mortgage lending institutions to enable seamless monitoring of refinanced loans. The ultimate objective is to have all participating mortgage banks and other stakeholders on the same platform with a mirror account with NMRC.

Track Record of Financial Performance

The Company's total assets have grown at a compounded annual rate of 4% in the last three years and stood at ₦42.6 billion as at 31 December 2017. NMRC's net earnings have grown significantly at a compounded annual rate of 41% over the same period. The Company's asset quality remains strong with no non-performing loans recorded in the last three years. NMRC recorded an average pre-tax ROA and pre-tax ROE of 3.3% and 13.6% respectively over the last three years.

THE ISSUE

Structure

The Issue is a ₦11 billion Fixed Rate Bond ("the Bond" or "the Issue"), the second tranche under the Company's ₦440 billion Debt Issuance Programme ("DIP"). The Issue will have a tenor of 15 years, with interest paid quarterly and principal repayment made on each coupon payment date. The Bond will rank pari passu with present and future outstanding unsecured and unsubordinated obligations of the Issuer and the guarantor (the Federal Government of Nigeria).

Purpose

NMRC's main purpose is to provide long-term funds to refinance conforming mortgage loans from member Mortgage Lending Banks (MLBs), with the goal of making the mortgage market liquid. The Company shall refinance eligible mortgage loans of member mortgage lenders by purchasing the cash flows from the mortgage loans with recourse, and obtaining a corresponding security interest on the mortgage properties securing the original loans - with 125% over-collateralization.

Repayment

Interest payments on the Bond shall be made on a quarterly basis throughout the tenure of the Bond. The principal repayment is on an amortized basis where principal repayment shall be made on each coupon payment date.

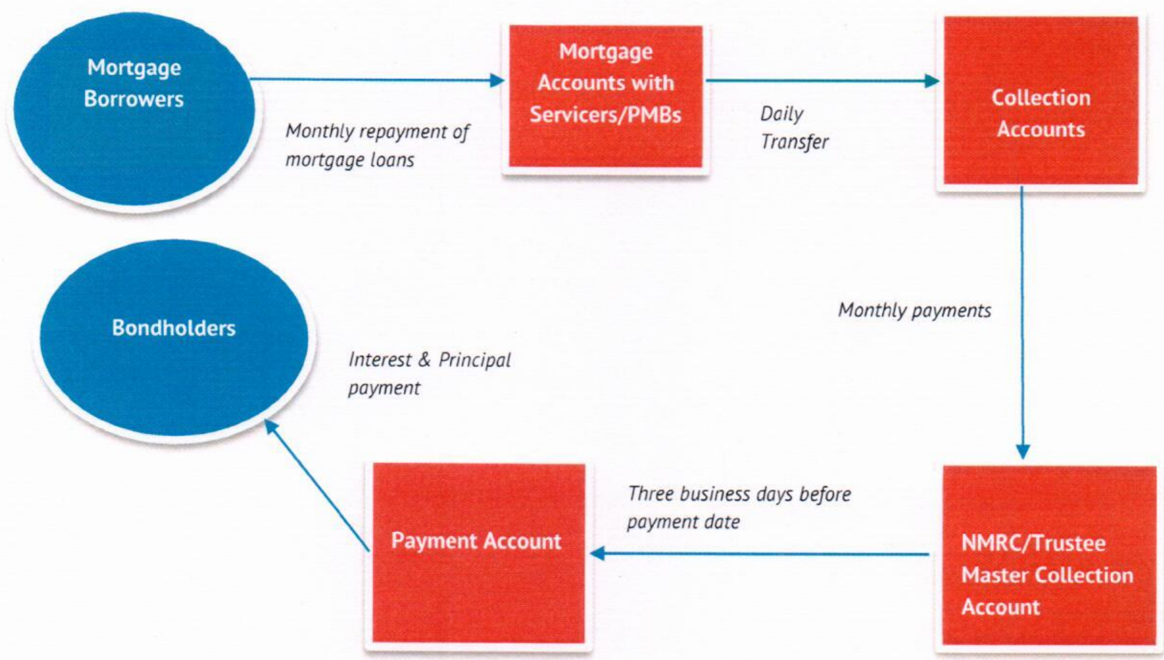
Covenants

NMRC shall, with or without formal demand, discharge the secured obligations in full and not create any charge, pledge, lien or other encumbrance upon, or permit any charge, pledge, lien or other encumbrance to be created on the trust property in accordance with the Trust Deed.

Guarantee

The Federal Government of Nigeria (FGN), through the Federal Ministry of Finance, guarantees NMRC's bond issuances up to ₦440 billion in accordance with the terms of the Deed of Guarantee. By the Deed of Guarantee, the irrevocable and unconditional obligations of the Guarantor shall extend to, and cover NMRC's payment obligations owed or promised to the Note Trustee under the Trust Deed, on a revolving basis, in respect of the Bonds issued under the Programme subject to the Guarantee Amount. The programme has an initial guarantee amount of ₦100 billion. Subsequent to this, a review of the programme's effectiveness and impact on the Nigerian mortgage market shall be conducted before any additional amount is extended by the FGN.

Figure 2: Overview of Flow of Funds/Transaction Structure



Source: NMRC

Transaction Parties

Dunn Loren Merrifield Advisory Partners Limited

Dunn Loren Merrifield Advisory Partners Limited (DLM) is the lead issuing house to the funding programme. DLM is a full-service investment house head-quartered in Lagos, Nigeria. It is an independent institution that provides an array of services including financial advisory, asset management, trusteeship and securities trading.

Stanbic IBTC Capital Limited

Stanbic IBTC Capital Limited (Stanbic IBTC Capital) is the joint issuing house to the Series II Bond. The Company, a subsidiary of Stanbic IBTC Holdings Plc, was registered with the Securities and Exchange Commission as an Issuing House and Underwriter in 2012. Stanbic IBTC Capital provides investment banking services to corporate clients and is a leading investment banking franchise in Nigeria with expertise in advisory, capital markets and financial arranging.

Stanbic IBTC Trustees Limited

Stanbic IBTC Trustees Limited (SITL) is the note trustees to the Bond. The Company is a wholly owned subsidiary of Stanbic IBTC Holdings Plc and was registered in 2009 by Nigeria's Securities and Exchange Commission (SEC) as trustees. SITL also received the South African Reserve Bank (SARB) approval in 2010. Stanbic IBTC Trustees provides institutional trust and loan agency services, as well as estate planning and inter-generational wealth transfer. SITL also provides trustee agency services in relation to debt issues and syndicated lending transactions, acting as a representative of the bond/other debt holders and group of banks/ financial institutions.

DLM Trust Company Limited

DLM Trust Company Limited (DLM Trust) is the joint note trustees to the Issue. DLM Trust is a subsidiary of DLM and provides trusteeship services to clients.

FBN Trustees Limited

FBN Trustees Limited ("FBN Trustees") is the security trustee to the Issue. FBN Trustees is a wholly owned subsidiary of FBN Holdings Plc. The Company acts as a custodian of assets for public, corporate and private entities. The Company acted as trustee in the Dangote Industries Limited US$3.5 billion Syndicated Loan Facilities and the UNICEM US$638 million Syndicated Loan Facility, amongst other deals.

Meristem Registrars & Probate Services Limited

Meristem Registrars & Probate Services Limited (Meristem) is the registrar for the programme. Meristem is a wholly owned subsidiary of the Meristem Group, a capital market conglomerate offering wealth management, stockbroking, trustees, corporate financing and registrar services.

Abraham & Co. (Solicitors, Advocates and Notary Public)

Abraham and Co. is the solicitor to the Issue. The firm was established in 2004 and specializes in a number of areas including corporate law & finance, dispute resolution, energy & natural resources, intellectual property and private equity & venture capital amongst others.

Olaniwun Ajayi Legal Practitioners

Olaniwun Ajayi is the solicitor to the offer. The firm was established in 1962 and has over 50 years' experience in the areas of commercial litigation, banking, finance, capital markets, corporate governance, intellectual property and taxation amongst others.

G. Elias & Co. Solicitors & Advocates

G. Elias & Co. is the solicitor to the note trustee. The firm was established in 1994 and offers a variety of legal services in areas such as mergers & acquisitions, capital markets, banking, intellectual property and taxation.

Standard Chartered Bank Limited

Standard Chartered Bank Limited (SCBL) is the account bank/paying agent for the bond programme. SCBL is a wholly owned subsidiary of Standard Chartered Bank Plc, headquartered in the United Kingdom. The Bank offers a wide range of products and services in retail, wealth management, commercial, corporate & Institutional; as well as private and transaction banking business.

Receiving Banks

- Access Bank Plc
- Sterling Bank Plc
- Stanbic IBTC Bank Limited

ISSUER'S FINANCIAL CONDITION

ASSET QUALITY

NMRC had a balance sheet footing of ₦42.6 billion as at 31 December 2017, reflecting marginal growth over the previous year. The Company's investment portfolio continues to dominate the asset base, accounting for 75% of total assets as at FYE2017. Refinance loans came a distant second, accounting for 19% of total assets (2016: 20%). Bank placements and other cash holdings jointly accounted for 5% of total assets. Agusto & Co. is of the view that the Company's investment guidelines should specify minimum credit ratings for its placements. This balance sheet structure could change moderately in 2018, with bond issuances slated for the period likely to increase the volume of refinanced loans.

NMRC is permitted to maintain a minimum of 50% of total investments in government securities and correspondingly, a maximum of 50% in bank placements. The Company is prohibited from investing in equities, corporate bonds, mutual funds, derivatives and foreign exchange securities. Federal Government securities accounted for the bulk of investment securities, upheld by the high interest rate environment that prevailed for most of 2017, with treasury bills yielding higher returns over most permissible money market instruments. In our view, the high volume of investments in government securities is likely to persist in the short to medium term.

Figure 3: Breakdown of Assets as at FYE 2017

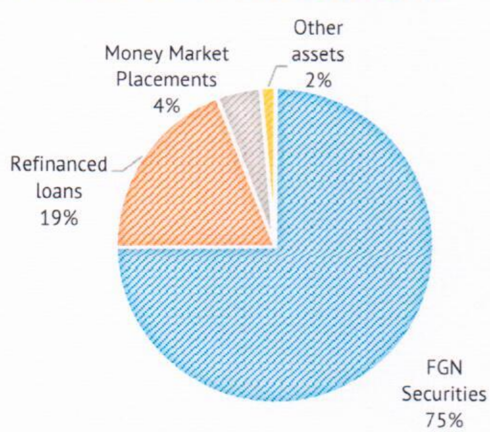
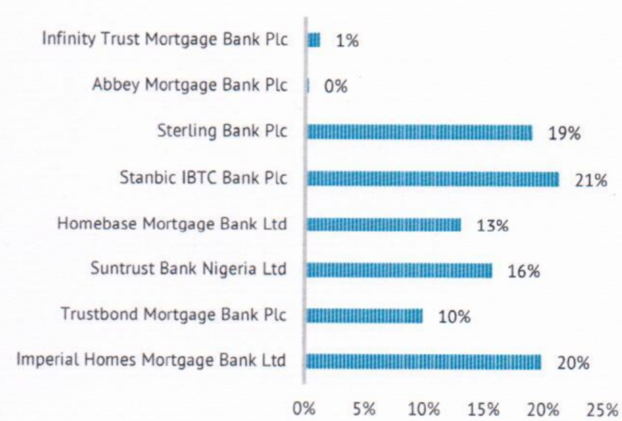


Figure 4: Distribution of NMRC Mortgage Refinance Loans



0Source: Nigeria Mortgage Refinance Company

NMRC's portfolio of refinanced mortgage loans (purchases with recourse, PWR) remained relatively unchanged from the prior year at ₦8.1 billion as at FYE 2017. NMRC purchases qualifying mortgage loans from participating PMBs and commercial banks. These mortgage loans must have met the UUS, which serves as a minimum acceptance criteria for refinancing. The Company's refinance portfolio is concentrated in eight mortgage institutions, with three institutions jointly accounting for 60% - but each within the single obligor limit. As at FYE 2017, NMRC had refinanced a total of 456 mortgage loans. The refinance mortgage portfolio currently has an average term to maturity of 13 years. The Company does not extend credit to any single lending institution equal to or above 20 times the value of the institution's MRC shares or 25% of its shareholders' funds unimpaired by losses.

Geographically, the Company's refinance portfolio is concentrated in Lagos and Abuja, with 79% and 19% of the total mortgage pool respectively. The balance is distributed across Ogun, Nassarawa, Kaduna and Bauchi. Although this concentration is synonymous with the Industry at large, NMRC is looking to expand the current geographical spread through advocacy for favourable land documentation and foreclosure laws across the country. Nonetheless, mortgage lending could remain skewed towards the aforementioned cities in the short to medium term, with only three of the Company's current member institutions based outside these locations. The fact that Lagos and Abuja are amongst the most economically developed mortgage and real estate markets in Nigeria also support this assertion.

The Company did not have any non-performing loans (NPLs) as at 31 December 2017, benefiting from refinancing loans with better credit quality from its borrowing member mortgage banks. Underpinning this low level of delinquency is NMRC's strategy to purchase only 'prime' residential mortgages and agreements with the member mortgage banks to have any delinquent mortgage loan replaced with a performing loan. The Company enters a master purchase, refinance and servicing agreement (MPRSA)[8] with each participating lending institution that includes a direct debit arrangement where the minimum monthly remittance[9] due to NMRC is paid directly into a collection account through the NIBSS[10] platform. The document also permits a direct debit of an institution's CBN account where there's a shortfall in the minimum monthly repayment to NMRC's collection account.

The direct debit instructions contained in the MPRSA is supported by active portfolio monitoring by the Company's risk management unit. The risk management team monitors the liquidity position of all obligors (participating lending institutions) every week and conducts an independent financial health assessment at least once a quarter. NMRC also insists on a loan to value ratio of less than or equal to 80%, with NPLs to refinanced loans ratio expected to be under 3.5% in any given year. If an exception is noted, NMRC gives the lending institution 90 days to correct the facility.

In our opinion, NMRC's mortgage refinance assets are of high quality and the Company has adequate policies and guidelines to forestall significant growth in NPLs while growing risk assets in the short term. Overall, asset quality is very good.

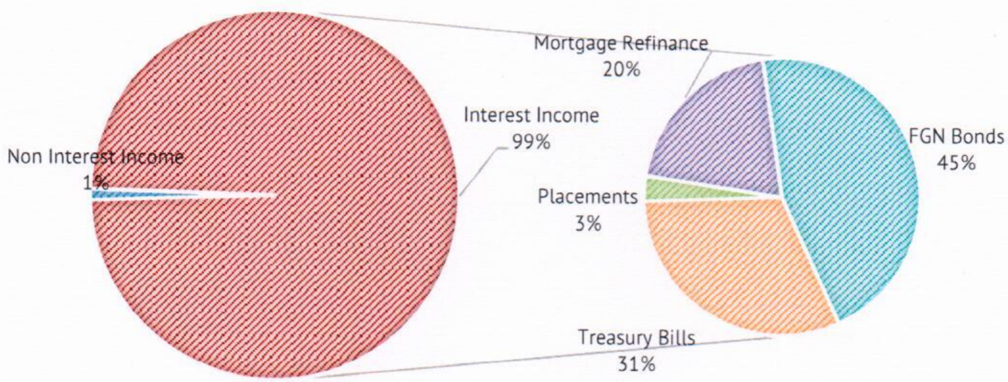
[8] Master purchase, refinance and servicing agreement
[9] The minimum amount as indicated in the Minimum Monthly Remittance Schedule to be paid by the participating lending institution into the Collection Account on or before a Remittance Date, including any Principal Prepayment
[10] Nigeria Interbank Settlement System

EARNINGS AND PERFORMANCE

Over the past three years, NMRC's net earnings have grown at a compound annual growth rate (CAGR) of 41%, rising by 33% to ₦3.9 billion in 2017 from ₦2.9 billion in 2016. The growth was primarily driven by higher yields on money market investments which contributed to a 22% increase in interest income to ₦6.3 billion.

Interest income accounted for over 99% of the Company's net earnings, while non-interest income, which comprises mainly fees, remained a relatively small contributor to net earnings at less than 1% (2016: <1%). Investment income from government securities accounted for the bulk of interest income at 76%, upheld by the prevailing high interest rate environment. NMRC's core business of mortgage refinancing which can only be funded through equity and the proceeds of bond issuances therefore accounted for just 20% of earnings. Income from placements with commercial banks and select participating mortgage banks accounted for 3% of interest income.

Figure 5: Breakdown of Earnings



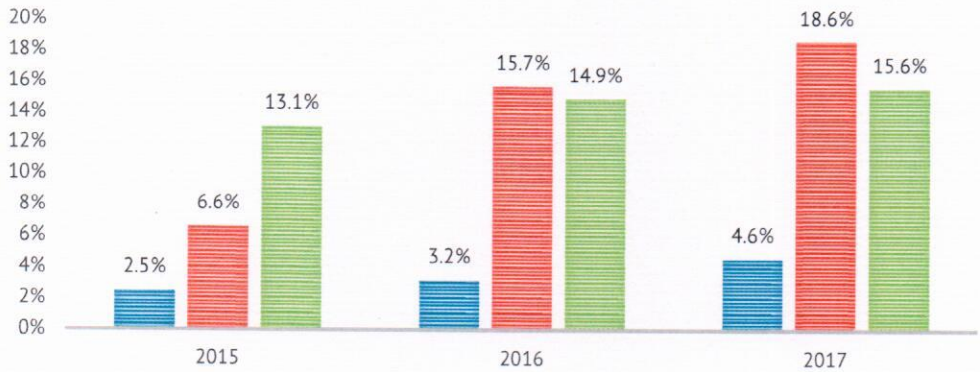
Source: Nigeria Mortgage Refinance Company

Despite the high inflationary pressures that persisted in 2017, NMRC's cost to income ratio improved to 52% (2016: 56.8%) due to a significant growth in net earnings as operating expenses actually increased by 22%. NMRCs cost-to-income is below the internal benchmark of 60%. However, this is high in our opinion, given the low scale of operations in comparison to commercial banks and mortgage banks. The company's cost–to-income ratio is also significantly higher than other emerging market peers such as Hong Kong Mortgage Corporation (HKMC) and Cagamas Berhad (the National Mortgage Corporation of Malaysia).

NMRC's profit before tax grew by 48% in 2017 to ₦1.9 billion (2016: ₦1.3 billion), reflecting significant growth in earnings, particularly from investment income. The Company recorded a pre-tax return on average assets (ROA) and pre-tax return on average equity (ROE) of 4.6% and 18.6% respectively (2016: 3.2%, 15.7%). The

Company's profitability compared favourably with the average return on 364-day Federal Government of Nigeria (FGN) Treasury Bills of 15.6% in 2017. Going forward, we expect investment income to remain a core contributor to the Company's earnings, and ROE to mirror trends in yields on FGN securities in the near term.

Figure 6: Profitability Indicators (2015 - 2017)

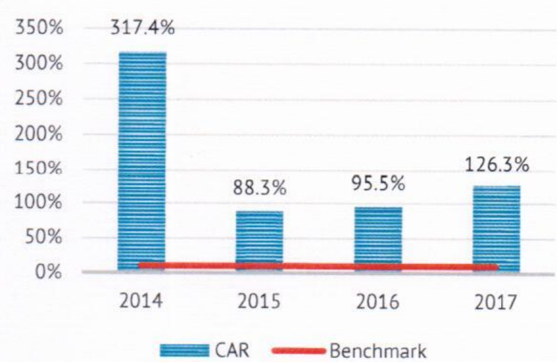


Source: NMRC and Agusto & Co Research

CAPITAL ADEQUACY

NMRC has an authorised capital of ₦7.8 billion which was fully paid-up as at 31 December 2017. The Company's shareholders' funds rose by 37.1% to ₦11.8 billion as at the same date (through the accretion of reserves), well above the ₦5 billion minimum requirement prescribed by the CBN for mortgage refinance companies. In addition, NMRC's leverage ratio (core capital to total assets ratio) of 27.7% was above the 5% minimum requirement prescribed by the CBN.

Figure 7: Capital Adequacy Ratio



The NMRC's capitalisation is strong, with a CAR of 126.3% as at FYE 2017 (2016: 95.5%). The CAR has trended upwards in the last two years due to growth in equity and retained earnings. The NMRC enjoys a lower risk weighting for the mortgage loans on its books (50% compared to 75% for commercial banks), a fact that has significantly enhanced the Company's CAR relative to other financial service operators, but is justifiable given the expected higher credit quality. Both the CAR and leverage ratios are in line with internal minimum benchmarks of 13% and 7% set by the NMRC. The Company's CAR is also higher than Agusto & Co.'s minimum benchmark.

In our view, the Company's capital is strong for the current level of business risks and is expected to remain adequate to support further growth in business volumes in the short to medium term.

Liquidity and Funding

NMRC is a non-deposit taking mortgage refinance institution. The Company's liquidity and funding profile is thus primarily supported by long-term capital comprising equity of ₦11.8 billion – which funded 28% of total assets and borrowings of ₦30.2 billion (which funded 70.9% of total assets) as at FYE 2017.

The Company's borrowings of ₦30.2 billion comprises net bond proceeds[11] of ₦7.4 billion and long term borrowings of ₦22.8 billion. Interest accrues on the bond at 14.9% per annum payable quarterly. The proceeds of the bond have been fully utilised for mortgage refinancing and set to mature in 2030. The long term borrowings comprises a 40 year International Development Agency (IDA)[12] facility granted to Nigeria and received by the Company through the CBN in 2014 (tranche I) and 2015 (tranche II). The facility represents a portion of the World Bank's $300 million loan to fund the Federal Government's housing finance programme and is not available for mortgage refinancing or loan repayment. Currently, the loan acts as a buffer for the Company's capital base and overall liquidity. The loan has an annual interest rate of 4.25% (including a CBN forex hedge of 3.5% per annum) and a moratorium period of 10 years on principal repayment.

NMRC's balance sheet is highly liquid, with a liquidity ratio (liquid assets to total assets) of 74.8% as at FYE 2017 (2016: 72.1%). NMRC's debt coverage ratio, which relates the sum of short-term debt and long-term debt maturing or amortizing over the next 12 months to liquid assets declined slightly to 9 times from 10 times in the prior year, but remains strong. Excluding the IDA facility, the Company's debt service coverage ratio worsens to 2.5 times, but remains adequate. Furthermore, NMRC's profit before taxation in 2017 provided 0.9 times coverage of maturing annual debt (2016: 0.6 times). When we consider anticipated issuances and the expected additional $50 million drawdown from the IDA facility in 2018, coverage remains adequate.

Though the Company has accessed the market for funding only once, we view the NMRC's ability to raise funding to be good, bolstered by the fact that the Issuer's borrowings are guaranteed by the Federal Government of Nigeria. In July 2015, the Company issued ₦8 billion fixed rate bond at 14.9% with a tenor of 15 years. NMRC is likely to raise additional funds from the debt issuance programme in 2018. As of end-December 2017, total securities outstanding stood marginally lower at ₦7.41 billion (2016: ₦7.54 billion), matching the contracted loan base, with the loan-to-funding ratio improving slightly to 2.3 times (FYE 2016: 1.9 times).

[11] This represent the ₦8 billion, 14.9% series 1 fixed rate bonds issued on 29 July 2015.
[12] A World Bank Agency

Overall, we consider NMRC's liquidity profile to be very good.

OWNERSHIP & GOVERNANCE

NMRC is a non-deposit taking, limited liability company that provides mortgage refinancing services to participating lending institutions. The Company had 1.9 billion ₦1 shares in issue, held by 27 institutions. The Federal Government through the Ministry of Finance Incorporated (MOFI) and NSIA have the highest shareholding with a 36.6% equity stake and the balance spread out amongst 25 financial institutions.

NMRC is governed by a 13-member board of directors comprising, three executive directors and 10 non-executive directors (including four independent directors). The Company's Board is chaired by an independent non-executive director – Charles C. Okeahalam. The directors on the Company's Board are representatives of the institutional investors and have no personal interest(s) in the Bank. These institutional investors provide oversight on the Bank's operations through board representations and standing committees. In addition to the statutory audit committee, the Board has six standing committees:

- Board Audit Committee
- Board Credit & Investment Committee
- Board Finance and General Purpose Committee
- Board Governance and Nominations Committee
- Board Risk Management Committee
- Board Remuneration Committee

NMRC's management team is led by Professor Charles Inyangete, the Managing Director/Chief Executive Officer. Prof. Inyangete is a seasoned financial services practitioner, with over 20 years of experience. The Managing Director/CEO is supported by two executive directors who in our opinion have relevant qualifications and adequate experience in the finance and mortgage banking industry.

NMRC has a total staff strength of 30 employees comprising three executive management staff, 15 middle management staff and 12 non-management staff. The Company's staff productivity measured by net earnings per staff improved to ₦132 million in 2017 from ₦106 million in 2016. We consider staff productivity to be good, with productivity expected to improve once the volume of operations increases.

OUTLOOK

While the potential for mortgage loans in Nigeria is high, the growth and development of the mortgage industry remains constrained by numerous challenges. Over the last two years, business activities have suffered from the nation's weak macroeconomic climate, primarily driven by the dip in crude oil prices and the country's high dependence on the product. Although the economy has begun showing signs of recovery, many challenges still persist, which continue to hinder the progression of the Industry. The poor access to long term financing, the high interest rate environment (driven by inflationary pressures), unemployment and other bottlenecks associated with property registration and acquisition remain major impediments to mortgage lending in the country. Despite this, NMRC remains committed to promoting home ownership in Nigeria and pushing reforms aimed at increasing mortgage lending activities.

To address the challenges facing the Industry, the Company has undertaken a number of strategic initiatives. The establishment of the Mortgage Market System (MMS) is aimed at enhancing the efficiency of processes within the entire Nigerian housing finance ecosystem, including land and titling, construction finance, primary mortgage origination and secondary mortgage market refinancing. NMRC, alongside DLM and several PMBs, have sponsored the Mortgage Warehouse Funding Limited (MWFL), a special purpose vehicle established to provide short term liquidity to member PMBs for the origination of eligible mortgage loans. In an effort to reach the underserved populace, the Company (alongside industry stakeholders) has developed and launched uniform underwriting standards for workers in the informal sector. Furthermore, NMRC has commenced advertising on radio stations in a bid to sensitize the general public about mortgage loans. Although we view positively, the aforementioned, we recognize that the impact of these initiatives are medium to long term in nature and thus, do not anticipate material improvement in outreach in the near term.

In our opinion, the addition of more member mortgage banks to NMRC is crucial to NMRC's strategic goals. As the Issuer grows its refinancing loan portfolio, overall outreach will be positively impacted. However, adherence to NMRC's underwriting standards remains a limiting factor for many PMBs and thus, restricts the number of eligible mortgage loans. Nonetheless, the MWFL is expected to fund the origination of mortgages in conformance with the NMRC Uniform Underwriting Standards. Currently, the bulk of NMRC's earnings stem from investments in government securities. Accordingly, we expect profitability to remain good going forward.

We attach a stable outlook to the rating of both the Issuer and the ₦11 billion secured series II bond. Our stable outlook reflects Agusto & Co.'s expectation that the management will be able to uphold the Company's good financial condition as they increasingly fulfil NMRCs mandate of developing the primary and secondary mortgage markets and promoting affordable home ownership in Nigeria, with the Federal Government of Nigeria providing adequate support.

FINANCIAL SUMMARY

Nigeria Mortgage Refinance Company Plc						
BALANCE SHEET AS AT	**31-Dec-17**		**31-Dec-16**		**31-Dec-15**	
	=N='000		**=N='000**		**=N='000**	
ASSETS						
Cash & equivalents	420	0.0%				
Government securities	31,917,002	74.8%	29,391,930	72.1%	15,322,023	39.2%
Liquid assets	31,917,422	74.8%	29,391,930	72.1%	15,322,023	39.2%
Balances with Nigerian banks	1,920,361	4.5%	2,637,765	6.5%	20,717,525	53.0%
Total mortgage assets	8,243,971	19.3%	8,185,160	20.1%	1,908,295	4.9%
Less: Cumulative loan loss provision	(82,294)		(80,914)	-0.2%	(42,447)	-0.1%
Total loans & advances - net	8,161,677	19.1%	8,104,246	19.9%	1,865,848	4.8%
Interest receivable	-		64,424	0.2%	809,027	2.1%
Other prepayments	233,554	0.5%	251,509	0.6%	120,711	0.3%
Other accounts receivables	36,030	0.1%	56,036	0.1%	14,571	0.0%
Other long-term investments	10,000	0.0%	-		-	
Fixed assets & intangibles	363,164	0.9%	282,703	0.7%	209,710	0.5%
Total assets & contingents	**42,642,208**	**100%**	**40,788,613**	**100%**	**39,059,415**	**100%**
CAPITAL & LIABILITIES						
Shareholders' funds	11,827,366	27.7%	8,625,122	21.1%	7,776,802	19.9%
Specialized funding	22,816,413	53.5%	24,268,660	59.5%	23,303,888	59.7%
Bank borrowings						
Debt securities issued and other borrowings	7,410,894	17.4%	7,542,865	18.5%	7,760,373	19.9%
Other liabilities	587,535	1.4%	351,966	0.9%	218,352	0.6%
Total capital, liabilities & contingents	**42,642,208**	**100%**	**40,788,613**	**100%**	**39,059,415**	**100.0%**

Nigeria Mortgage Refinance Company Plc						
INCOME STATEMENT FOR THE YEAR ENDED	**31-Dec-17**		**31-Dec-16**		**31-Dec-15**	
	=N='000		**=N='000**		**=N='000**	
Interest income	6,298,372	99.8%	5,176,768	100.0%	3,132,729	100.0%
Interest expense	(2,339,939)	-37.1%	(2,153,901)	-41.6%	(1,104,822)	-35.3%
Loan loss expense	-		(38,467)	-0.7%	(42,447)	-1.4%
Net-interest income	3,958,433	62.7%	2,984,400	57.6%	1,985,460	63.4%
Non-interest income	10,406	0.2%	6	0.0%	772	0.0%
Net Earnings	**3,968,839**	**62.9%**	**2,984,406**	**57.6%**	**1,986,232**	**63.4%**
Staff costs	(801,417)	-12.7%	(882,562)	-17.0%	(618,223)	-19.7%
Depreciation expense	(132,296)	-2.1%	(92,558)	-1.8%	(47,774)	-1.5%
Other operating expenses	(1,131,245)	-17.9%	(719,849)	-13.9%	(832,885)	-26.6%
Total operating expenses	(2,064,958)	-32.7%	(1,694,969)	-32.7%	(1,498,882)	-47.8%
Profit (loss) before taxation	1,903,881	30.2%	1,289,437	24.9%	487,350	15.6%
Tax (expense) benefit	(19,058)	-0.3%	(12,767)	-0.2%	(4,825)	-0.2%
Profit (loss) after taxation	1,884,823	29.9%	1,276,670	24.7%	482,525	15.4%
Gross Earnings	**6,308,778**	**100.0%**	**5,176,774**	**100.0%**	**3,133,501**	**100.0%**

KEY RATIOS	31-Dec-17	31-Dec-16	31-Dec-15
Profitability & Earnings			
Net interest margin	62.8%	57.6%	63.4%
Loan loss expense/Interest income		0.7%	1.4%
Operating expenses/Net earnings	52.0%	56.8%	75.5%
Return on average assets (pre-tax)	4.6%	3.2%	2.0%
Return on average equity (pre-tax)	18.6%	15.7%	6.6%
Net interest income/average earning assets	3.0%	2.2%	2.1%
Earnings Mix			
Net interest income	99.7%	100.0%	100.0%
Non-interest income	0.3%		
Growth Ratios			
Net interest income	32.6%	50.3%	249.4%
Operating revenue	33.0%	50.3%	222.6%
Non interest Expense	21.8%	13.1%	229.1%
Profit Before Taxation	47.7%	164.6%	204.3%
Liquidity & Funding			
Total loans - net/Total borrowings	-10.9%	-0.7%	-18.4%
Refinanced loans/Total Assets	19.1%	20.1%	4.9%
Refinanced loans/Total borrowings	27.0%	25.7%	6.1%
Liquid Assets/Total Assets	74.8%	72.1%	39.2%
Weighted Average Cost of Funds (WACF)	7.5%	6.9%	7.1%
Loan to Funding Ratio	2.3	1.9	8.4
Debt Service Coverage Ratio - (Short term borrowings + Current portion of long term borrowings)/Liquid assets	8.8	9.9	7.8
Asset Quality Ratios			
PERFORMING LOANS	8,243,971	8,185,160	1,908,295
Loan loss provision/Total loans - Gross	1.0%	1.0%	2.2%
Loan loss provision/Non-performing loans & mortgages	100.0%	100.0%	100.0%
Capital Adequacy & Leverage Ratios			
Risk-weighted assets/Total assets & contingents	26.9%	27.3%	23.7%
Adjusted capital/risk weighted assets	126.3%	95.5%	83.3%
Core capital/total assets - leverage	27.7%	21.1%	19.8%
Interest Cover	1.8	1.6	1.4
Staff Information			
Average number of employees	30	28	19
Staff cost per employee (N'000)	26,714	31,520	32,538
Net earnings per staff (N'000)	132,295	106,586	104,539
Staff cost/Net earnings	20.2%	29.6%	31.1%
Staff costs/Operating expenses	38.8%	52.1%	41.2%
Average staff per branch	15	28	19
Other Key Information			
Age (in years)	4	3	2
Number of offices	2	1	1
Legal lending limit (N'000)	5,913,683	4,312,561	3,888,401

RATING DEFINITIONS

ISSUER RATING

Aaa	An 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	An 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 in the risk attributable to an exposure to this bank. However, financial condition and ability to meet obligations as and when they fall due should remain strong.
A	An 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 bank. However, financial condition and ability to meet obligations as and when they fall due should remain largely unchanged.
Bbb	An 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 mortgage bank.
Bb	Financial condition is satisfactory and ability to meet obligations as and when they fall due exists. The mortgage bank 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.

ISSUE RATING

Aaa	This is the highest rating category. The Bond is adjudged to offer highest safety of timely payment of interest and principal.
Aa	The Bond is adjudged to offer high safety of timely payment of interest and principal.
A	The Bond is adjudged to offer adequate safety of timely payment of interest and principal; however, changes in circumstances can adversely affect such issues more than those in the higher rated categories.
Bbb	The Bond is adjudged to offer sufficient safety of timely payment of interest and principal for the present; however, changing circumstances are more likely to lead to a weakened capacity to pay interest and repay principal than for bonds in higher rated categories.
Bb	The Bond is adjudged to carry inadequate safety of timely payment of interest and principal; while they are less susceptible to default than other speculative grade bonds in the immediate future, the uncertainties that the issuer faces could lead to inadequate capacity to make timely interest and principal payments.
B	The Bond is adjudged to have greater susceptibility to default; while currently interest and principal payments are met, adverse business or economic conditions would lead to lack of ability or willingness to pay interest or principal.
C	The Bond is adjudged to have factors present that make them vulnerable to default; timely payment of interest and principal is possible only if favourable circumstances continue.
D	The Bond is in default and in arrears of interest or principal payments or are expected to default on maturity.

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