



<b>Current Price:</b>	N19.32k	<b>Fair Price:</b>	N16.40k
<b>Year High</b>	N32.00k	<b>Premium/ (Discount) to Valuation:</b>	22.00%
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### Business Summary

The Nigerian Aviation Handling company was incorporated in 1979 under the Nigeria Enterprise Promotion Decree. The federal government through the Federal Airport authority originally owned about 60 percent controlling shares in the company while foreign airline operators owned the remaining 40 percent. The company was privatized in 2005 and listed on the Nigerian Stock Exchange in 2006.

NAHCO controls over 75% of the aviation ground handling market in Nigeria, offering ground support services covering aircrafts handling, passenger/baggage handling, cargo handling and mail handling to a majority of about 40 airlines operating in the country. The company is a member of the international Alliance of Aviation Handlers.

### Investment Rationale

- NAHCO's post-privatization growth momentum in top line has been rather unimpressive averaging about 9 percent annually.
- Our assumed CAGR projections consistent with the past and most recent performance coupled with sector prospects, suggest that growth outlook does not support current pricing of the stock.
- Competitive pressures look likely to erode NAHCO's monopoly status in the aviation ground handling business as current reforms are luring ground handling companies into the country
- Due to the high degree of sensitivity of the aviation industry to policy changes, NAHCO's model could be negatively impacted by unexpected negative government regulations.
- Without leveraging its capital structure, the dilutive effect of the company's capital raising exercise and bonus issues in 2005 and 2006 respectively is expected to persist for the next 3 years; having failed to grow its earnings by a factor proportionate to its new equity base.

### Key Statistics and Financials

Key Metrics/Multiples	NAHCO	Peer Average
Trailing EPS (N)	0.66	0.59
Trailing PE (x)	29.06	30.64
Forward PE (x)	41.62	31.99
Earnings Yield %	3.44	3.27
Shares Outstanding (mn)	984	692
Shareholders' Funds (mn)	1222.6	1461.1
Market Cap	N19.01bn(\$162.49m)	N14.07bn(\$126.0m)
BVPS (x)	2.27	2.10
Turnover per share	5.48	4.60
ROE(%)	0.35	0.31
ROA(%)	0.12	0.14
PB ratio (x)	8.53	8.52
Price to sale (x)	3.96	4.31
Cost to turnover	0.41	0.50
Volatility (Beta)	1.1	0.71

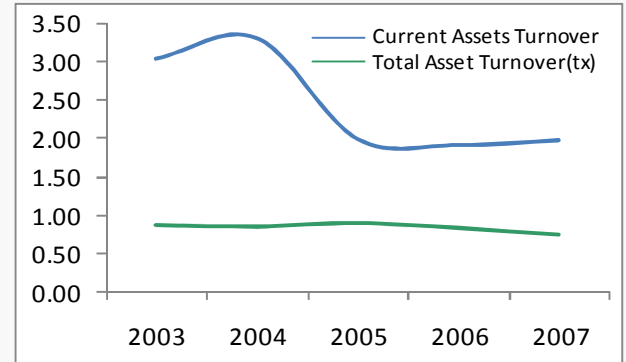
Financials	2006	2007	2008E	2009E	2010E
Turnover (N'bn)	3.2	3.7	4.8	6.4	8.3
Cost of Sales (N'bn)	2.0	2.1	2.9	4.0	5.3
PAT (N'mn)	434.1	590.0	687.2	665.8	976.3
Sales Per Share (NGN)	10.8	3.7	4.8	6.5	8.4
EPS(NGN)	1.4	0.8	0.9	0.9	1.3
DPS(NGN)	0.3	0.3	0.4	0.4	0.7
<b>Growth</b>					
Turnover Growth (%)	6.39	12.81	30.01	35.23	28.95
PAT (%)	36.63	35.90	16.00	35.00	29.00
EPS (%)	36.63	-45.64	16.49	-3.12	47.00
DPS (%)	0.00	0.00	22.00	21.00	47.00
Asset Growth (%)	14.19	25.09			
<b>Corporate Benefits</b>	<b>2003</b>	<b>2004</b>	<b>2005</b>	<b>2006</b>	<b>2007</b>
Bonus	1 for 5	nil	nil	nil	nil
Dividend (NGN)		0.24	0.30	0.30	0.30
Pay-out ratio (%)	nil	48.33	28.33	20.73	38.14
Dividend Yield (%)				2.5	1.11
Earnings Yield (%)				12.06	2.91

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## Analysis of financials

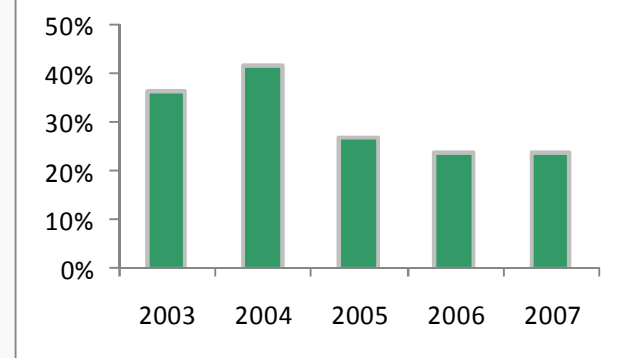
### Asset Management and Efficiency

NAHCo has maintained a stable level of efficiency in its asset utilization. This is reflected in the straight path of **total assets turnover ratio** which averaged 0.83 x in the past 5 years. This means that the company has been generating sales of 83 kobo for every naira of its asset base. Assets use efficiency is more commendable among the fixed assets class as the **current asset turnover** plunged from 3.04 x in 2003 to 1.98 x in 2007. This may suggest that the company is less efficient in the deployment of its liquid assets.



Though operational costs thread a narrow growth path of 15 percent CAGR, the company has demonstrated an impressive cost efficiency as **Operating Expenses to Sales (Opex-to-Sales)** ratio plummeted from 37 percent in 2003 to 24 percent in 2007. This is largely connected with government divestment as administrative expenses make up a disproportionately large part of operating expenses

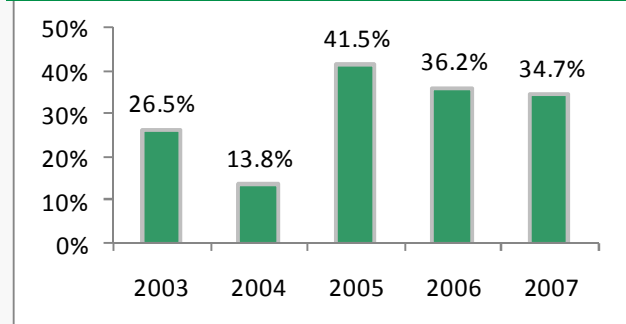
### NAHCO: Trend Opex to Sales Ratio



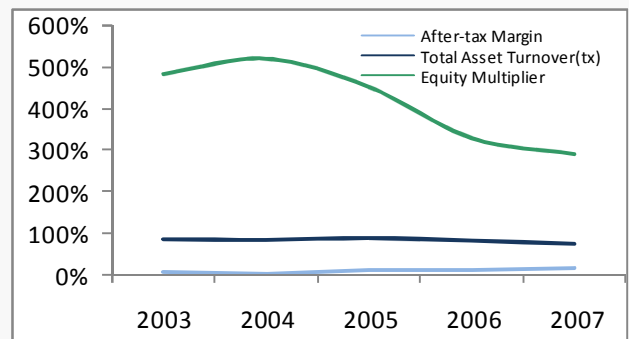
### DuPont Analysis of Profitability

NAHCo's record of 5 year average **return on equity (ROE)** of 31 percent shows a declining trend from 2003 to 2007. Despite **rising margins**, ROE dipped slightly from 36.19 percent in 2006 to 34.71 percent in 2007. Near constancy of asset turnover ratios and falling asset leverage have occurred side-by-side with a declining trend in ROE despite increased margins in the last 3 financial years. We believe that NAHCo's profitability can be improved if the company pays closer attention to its degree of asset leverage.

### NAHCO: Trend in ROE



A closer examination reveals that suboptimal combination of reserves and total assets employed is a contributory factor to worsening asset leverage. With respect to **return on total assets**, NAHCo has shown appreciable rise averaging 14 percent over a period of 5 years. This is accounted for by rising **pre-tax margin**.



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## Analysis of Financials

### Trends in Turnover and Earnings Growths

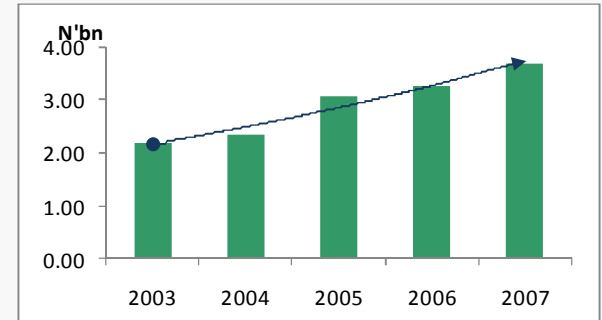
NAHCo has maintained a positive turnover growth trend in the last five years. The company grew its top line from N2.17bn in 2003 to N3.7bn in 2007, translating into a CAGR of 13.9 percent. Turnover growth path peaked in 2005 at 30.2 percent. This is regarded as an outlier which is directly connected to the successful divestment of government ownership. Subsequently, growth speed slowed down and the company was only able to achieve a 12.8 percent turnover growth in 2007 as against 17.0 percent forecast for the period. NAHCo transitioned from a profit after tax (PAT) of N139m in 2003 to N590m in 2007. This represents a 5-Year CAGR of 43.5 percent in PAT. This growth pattern is tracked by the upward trajectory of earnings per share (EPS) until 2006 when the company's EPS bowed to the dilutive effect of new equity issues of 125 million shares resulting from the dual effect of bonus and public offer. EPS nosedived from 106k in 2005 to 79k in 2007.

### Liquidity and Solvency

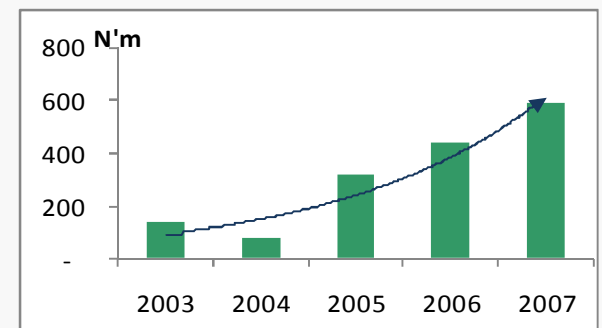
In terms of liquidity, NAHCo has maintained a significant improvement as shown in the upbeat recorded in its **current ratio** which moved from 0.69x in 2003 to 0.99x in 2007. This implies that the company's readily available assets cover 99 percent of current liabilities. However, there has been observable deterioration in the quality of net cash generated from operations. This is decipherable from the **downward trend of operating cash flow ratio (OCF)** which nosedived from 0.78x in 2003 to 0.57x in 2007. This suggests a weakening strength in the company's cash generating operations in covering its current liabilities. However, 2007 FYE suggests a rebound in coming year with operating cash ratio trending up from 0.45x to 0.57x.

Measures of **solvency** and **debt management** revealed appreciable improvement. **Equity multiplier** fell precipitously from 4.8x in 2003 to 2.9x in 2007. This indicates a significant reduction in financial leverage of about 50% as the company adjusted its capital structure by replacing part of its debt capital with equity.

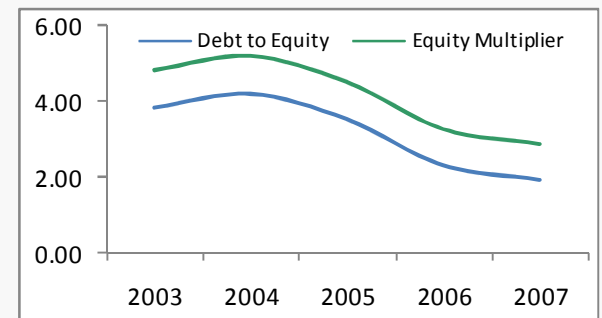
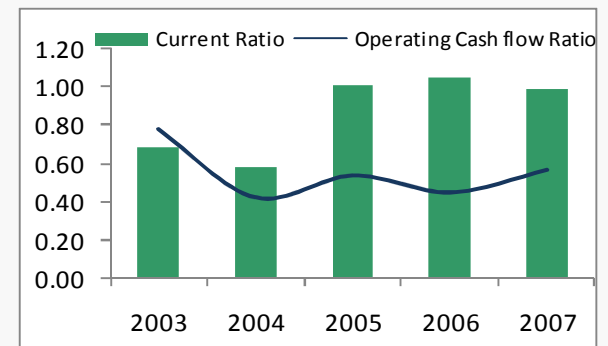
NAHCO: Trends in Turnover



NAHCO: Trends Profit After Tax (PAT)

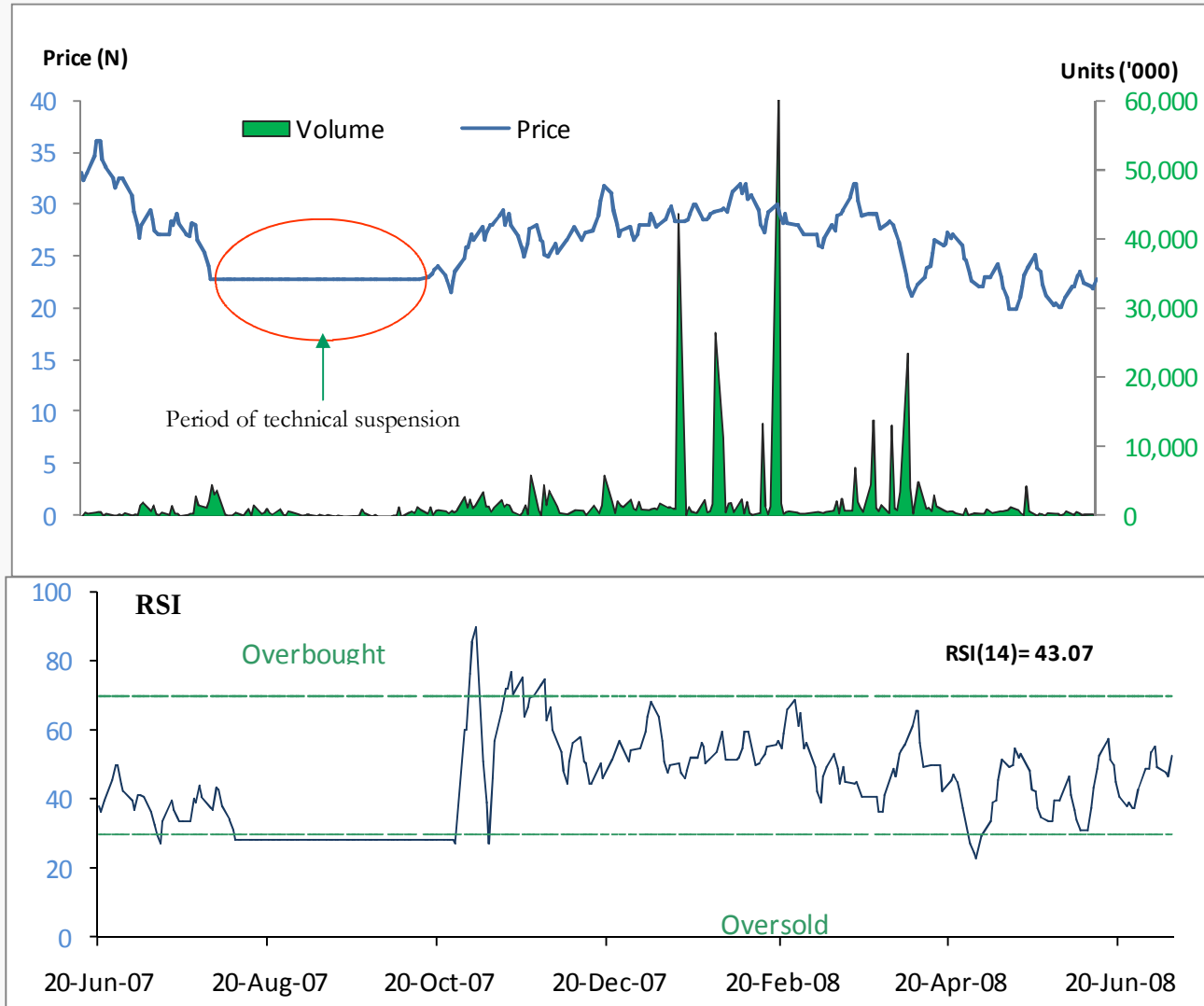


NAHCO: Trends in Liquidity and Solvency



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## Stock Price Trajectories and Returns



The historical price path of NAHCO has shown a track record of swings with an above-market volatility of 1.10. With an all time high of N70.05k on 11th May, 2007, the stock has been through the downward pressure of bearish momentum culminating in a 52- and 6 months returns of -29.08 percent and -23.08 percent as against corresponding market returns of 6.52 percent and -6.84 percent respectively.

Our momentum analysis using Relative Strength Index (RSI (14)) shows that NAHCo's price momentum exhibits extreme readings around the overbought region between October 2007 and February 2008. This is largely attributable to the impressive upbeat witnessed in the market during that period. Subsequently, however, the high volatility of NAHCo came to bear in explaining its downward trajectory resulting in extreme readings around the oversold region.



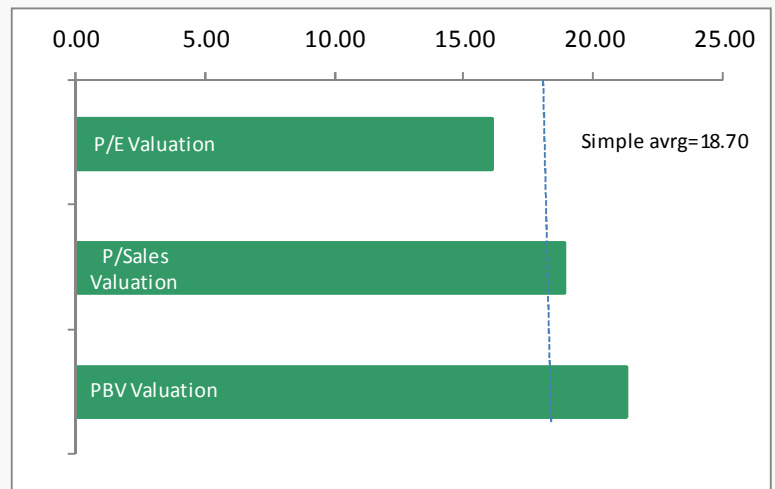
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### Valuation Methodologies and Summary

In the valuation of NAHCo, we employed different valuation methodologies. Based on comparable price multiples (**PE ratio, P/Sales and P/BV**) and our 12-month earnings, sales and net asset forecasts of 70k, 484k and 215k respectively, the 3 relative valuation methodologies yielded a simple average of N18.70k.

#### Valuations based on comparable price multiples

<b>P/E Valuation</b>	
Adopted P/E	23.00
12-Month Forecast EPS	0.70
<b>Valuation</b>	<b>16.06</b>
<b>P/Sales Valuation</b>	
Adopted P/Sales	3.89
12-Month Forecast Sales Per Share	4.84
<b>Valuation</b>	<b>18.82</b>
<b>PBV Valuation</b>	
Adopted P/BV	9.90
12-Month Forecast NAPS	2.15
<b>Valuation</b>	<b>21.24</b>



### Discounted Cash Flow Valuations

Further, we deployed the Discounted Cash Flow Models with a two-stage **Discounted Dividend, Residual Income** and **Free Cash Flow (FCF)** variants. We believe that our DCF assumptions are moderate. Our models employ a terminal growth rate of 7 percent (in line with long run economic growth rate) and CAPM-derived **cost of equity of 14.66 percent**.



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The input parameters for CAPM include 10.75 percent risk free rate on long term FG Bond, risk premium of 6.00 percent and an industry beta of 0.71 (as the company's beta of 1.1 seems too high and unrepresentative of the behaviour of the stock and the nature of the company's business).

**Based on DCF models, current pricing of NAHCo will be justified by a terminal growth rate of 13.00 percent. This justified growth rate in our fair opinion is unsustainable in the long run.**

Given the sensitivity of the adopted DCF models to terminal growth rate, we subjected these models to varying growth rates. The output of our sensitivity analysis reveals a price band of N7.22k at 5 percent terminal growth rate and N24.51k at 10 percent terminal growth rate.

Sensitivity Analysis						
Models	Growth rates					
	5%	6%	7%	8%	9%	10%
<b>DDM</b>	7.22	7.89	8.75	9.85	11.36	13.5
<b>FCF MODEL</b>	8.25	9.13	10.24	11.69	13.65	16.46
<b>RI MODEL</b>	14.68	15.73	17.06	18.8	21.14	24.51

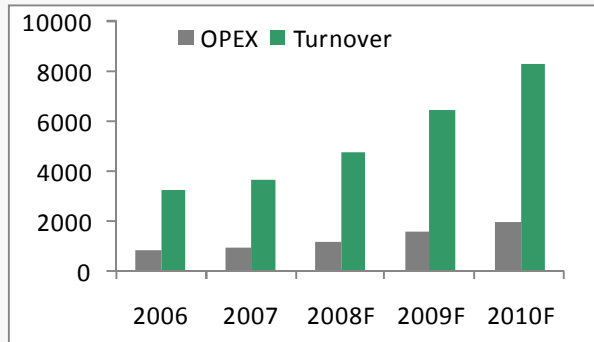
## Summary and Recommendation

Premised on the above analysis, coupled with appropriate consideration of comparable pricings, our **fair value for NAHCo gives N16.40k**. This implies that the current price is at a 22.0 percent **premium to valuation** and the **downside potential stands at 18.0 percent**.

We therefore place a **SELL** recommendation on NAHCo for both short term and long term investment horizons as the stock is currently overvalued.

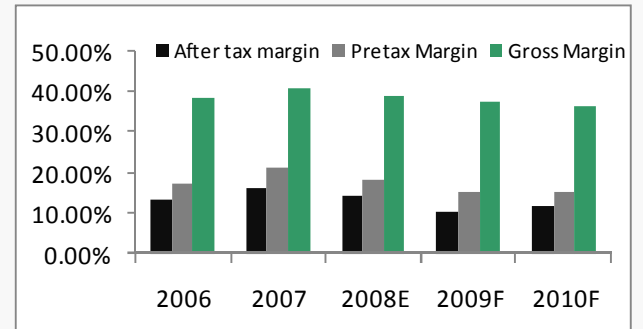
## Performance Charts

**Trend and Forecast: OPEX and Turnover (Nbn)**



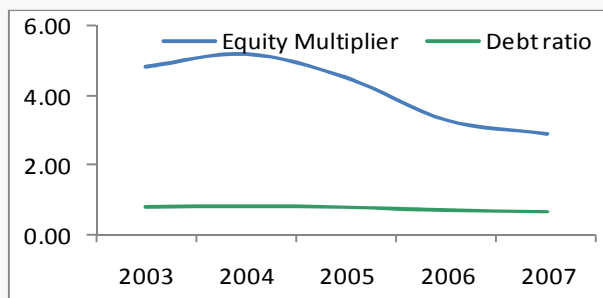
Source: Company Annual Reports, Meristem Research

**Profitability: Trend and Forecast**



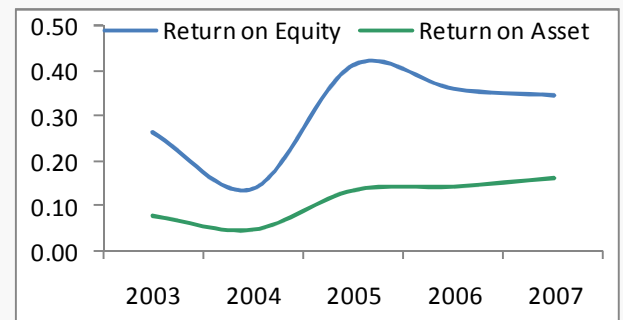
Source: Company Annual Reports, Meristem Research

**Trends in Solvency**



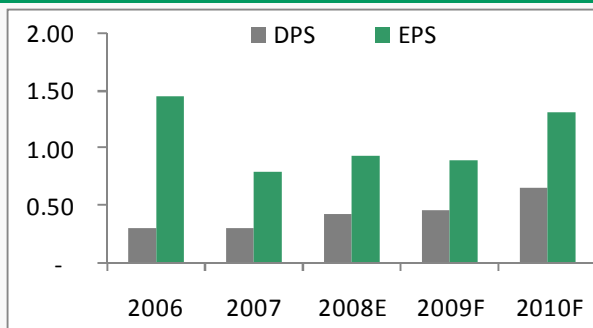
Source: Company Annual Reports, Meristem Research

**Trends in ROA and ROE**



Source: Company Annual Reports, Meristem Research

**Trends and Forecast: DPS and EPS (N)**



Source: Company Annual Reports, Meristem Research



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### NAHCo Abridged Financial Model and Assumptions

Projections (N)	2008	2009	2010	2011	2012
Turnover	4,759,657,500	6,425,537,625	8,288,943,536	10,775,626,597	14,008,314,576
Operating Costs	2,900,560,362	4,010,614,476	5,252,289,293	6,909,282,928	9,063,374,653
<b>Gross Profits</b>	<b>1,859,097,138</b>	<b>2,414,923,149</b>	<b>3,036,654,243</b>	<b>3,866,343,669</b>	<b>4,944,939,924</b>
Operating Expenses:					
<i>General / Admin. Exp.</i>	1,094,721,225	1,542,129,030	1,906,457,013	2,370,637,851	3,081,829,207
Total Operating Expenses	1,094,721,225	1,542,129,030	1,906,457,013	2,370,637,851	3,081,829,207
<b>Operating Profits</b>	<b>764,375,913</b>	<b>872,794,119</b>	<b>1,130,197,230</b>	<b>1,495,705,818</b>	<b>1,863,110,717</b>
Other income	142,789,725	192,766,129	276,021,820	377,146,931	420,249,437
EBIT	907,165,638	1,065,560,247	1,406,219,050	1,872,852,749	2,283,360,154
Interest income	47,596,575	64,255,376	82,889,435	107,756,266	140,083,146
Interest Expense	29,561,743	78,506,328	114,986,733	79,274,514	88,891,212
PBT	877,603,895	987,053,919	1,291,232,317	1,793,578,235	2,194,468,942
Taxes	190,386,300	321,276,881	314,979,854	452,576,317	532,315,954
<b>PAT</b>	<b>687,217,595</b>	<b>665,777,038</b>	<b>976,252,463</b>	<b>1,341,001,918</b>	<b>1,662,152,988</b>
Sales Per Share	4.84	6.53	8.42	10.95	14.23
EPS	0.70	0.68	0.99	1.36	1.69
DPS	0.31	0.34	0.50	0.68	0.84

Key Assumptions	2008	2009	2010	2011	2012
Sales Growth	30.00%	35.00%	29.00%	30.00%	30.00%
Cost of sales	60.94%	62.42%	63.37%	64.12%	64.70%
Selling expenses	0.00%	0.00%	0.00%	0.00%	0.00%
Administrative expenses	23.00%	24.00%	23.00%	22.00%	22.00%
Other operating income	3.00%	3.00%	3.33%	3.50%	3.00%
Exceptional Items	0.00%	0.00%	0.00%	0.00%	0.00%
Interest Income	1.00%	1.00%	1.00%	1.00%	1.00%
Interest expense	0.50%	0.70%	0.80%	0.90%	0.60%
Profit Margin	14.44%	10.36%	11.78%	12.44%	11.87%
Tax/sales	4.00%	5.00%	3.80%	4.20%	3.80%
Payout	45.00%	50.00%	50.00%	50.00%	50.00%

### IMPORTANT DISCLOSURES

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