

**Diamond Bank Plc. | Earnings Report**

9 months ended 30<sup>th</sup> September, 2016

**Impairment spike drives Q3 16 loss**
**(SELL: ₦1.00)**

- Diamond Bank Plc. (Diamond) released unaudited 9M 2016 results, wherein PBT and PAT plunged 79% and 78% YoY to ₦3.9 billion and ₦3.5 billion respectively. The results reflect sizable deterioration over Q3 16 with Diamond posting a ₦5.5 billion loss during the period due to an elevated loan loss charge of ₦21 billion. The high impairment charge in Q3 16 underpinned underperformance of Diamond's results relative to estimates.

*Deterioration in O&G book drives upswing in impairment charge*

- Extending the pattern in H1 16, impairment charges climbed for the third consecutive quarter, rising three-fold YoY to ₦21.3 billion (doubled QoQ) with annualized cost of risk surging 400bps QoQ to 7.5% (9M 16: 5.2%). The Q3 16 reading which tracked well ahead of our forecasts of ₦18.5 billion for the quarter, emanated from higher specific impairments (+87% QoQ) which the bank links to oil and gas (37% of loan book). In addition, we think Diamond's sizable exposure to sectors of the economy facing headwinds (general commerce and power) leave the bank susceptible to higher NPLs.

Income Statement Data			
	2016 – 9M'm	2015 – 9M'm	%chg
<b>Gross Earnings</b>	144,983	149,950	-3.3%
<b>PBT</b>	3,892	18,595	-79.1%
<b>Tax</b>	381	2,628	-85.5%
<b>PAT</b>	3,511	15,967	-78.0%

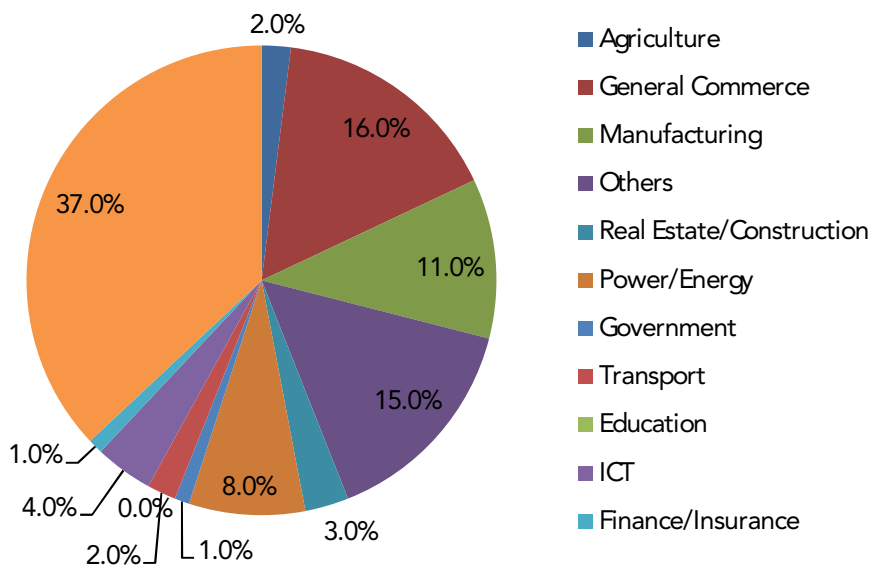
Balance Sheet Data			
	2016-Sep 'm	2015 -Dec 'm	%chg
<b>Cash</b>	318,564	361,167	-11.8%
<b>Loans</b>	1,041,227	763,635	36.4%
<b>Deposits</b>	1,400,978	1,233,591	13.6%
<b>Fixed Asset</b>	67,068	62,396	7.5%
<b>Net Assets</b>	227,976	214,609	6.2%

Stock Data	
<b>Price</b>	₦1.04
<b>52-week range</b>	₦1.02 – ₦2.88
<b>Market Cap. (N'm)</b>	25,244
<b>1-month Avg. Vol</b>	16,191,826
<b>Curr. PE</b>	N/A
<b>Bloomberg Ticker</b>	DIAMONDB:NL

**Diamond Bank Plc- Share Price Trend**

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**Figure 1: Loan book**



Source: Company financials, ARM Research

### *Higher asset yields buoy net interest income*

- In line with the pattern across coverage banks in Q3 16, tighter monetary policy provided scope for higher asset yields (+190bps QoQ). Though net loans expanded 6% QoQ, we believe this reflects translation impact of NGN weakness (-12% QoQ) on Diamond's FCY loan book (49% of loans) during the period. On the funding side, Diamond experienced pressures with annualized WACF rising 90bps QoQ to 2.5%. Given that deposit mix improved with CASA share of funding rising 40bps QoQ to 83%, interest expense pressures stemmed from more expensive borrowings which rose 31% QoQ to ₦246 billion. Despite the funding pressures, the gains on interest income helped drive improvement in net interest income (+15% QoQ). Nonetheless, lower trading (-5% QoQ) and other income (-8% QoQ) drove NIR lower (-10% QoQ). Overall, the loss over Q3 16 and weak earnings outlook raise prospects of further declines in earnings. Though CAR held flat at 15.6% -- the reading is now below CBN's threshold for systemically important banks and raises scope for additional capital raising.

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### *Asset quality pain to swing earnings negative in Q4 16*

- The weak Q3 16 result drives some revisions to our FY 16 estimates. First, we raise our loan growth estimates to match the 9M 16 run rate which results in 2016E net loan growth of 40% YoY. Over Q4 16, we think currency concerns should result in a retention of CBN's tight monetary policy stance which should continue to support asset yields. Thus, we forecast ₦37 billion interest income over Q4 16 with FY 16 reading at ₦151 billion (-6.7% YoY). On interest expense, Diamond's resort to borrowings amid tight monetary policy drives our Q4 16E forecast of ₦12.5 billion.
  - On asset quality, given the fresh NPL pressures from O&G and Diamond's historically higher cost of risk relative to peers, we see sizable scope for the bank to report higher loan loss charges in a weak macro environment in the last quarter. Thus, we forecast ₦23 billion impairment charges over Q4 16, which brings 2016E to ₦64 billion (+16% YoY) with annualized cost of risk at 6%.
  - Largely reflecting elevated impairment reading for Q4 16, we estimate that Diamond should report pre-tax and post-tax losses of ₦6.4 billion and ₦5.8 billion respectively in the last quarter which should swing FY 16 earnings into the red. Consequently, our FVE for the stock declines to **₦1.00** (previously ₦1.20). Diamond currently trades at P/B of 0.11x which is at discount to peer average of 0.4x. In view of the depressed earnings outlook, we reiterate our **SELL** rating on Diamond.
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## Summary of Results and Forecasts - Naira (₦)

### QUARTERLY

Income Statement  
(₦'000)\*

	Q1 2016A	Q2 2016A	Q3 2016A	Q4 2016E
Gross earnings	49,847	44,389	50,746	52,424
Interest Income	35,709	32,055	39,595	40,002
Interest Expense	(10,444)	(7,352)	(11,147)	(12,499)
Net interest income	25,264	24,703	28,448	27,503
Non-Interest Revenue	14,139	12,334	11,152	15,590
OPEX	(23,897)	(23,059)	(24,930)	(25,729)
Provisions	(8,812)	(10,186)	(21,263)	(23,838)
PBT	6,694	3,792	(6,593)	(6,474)
Tax	(934)	(499)	1,051	639
PAT	5,760	3,293	(5,543)	(5,835)

### ANNUAL

Income Statement  
(₦'000)\*

	FY 2014A	FY 2015A	FY 2016F	FY 2017F	FY 2018F
Gross earnings	205,308	208,265	200,574	211,791	226,178
Interest Income	161,130	157,860	147,360	152,752	161,906
Interest Expense	(51,553)	(48,454)	(41,442)	(40,945)	(51,709)
Net interest income	109,576	109,406	105,918	111,807	110,196
Non-Interest Revenue	44,178	50,404	53,215	59,039	64,272
OPEX	(99,282)	(97,546)	(97,615)	(99,585)	(103,310)
Provisions	(26,371)	(55,172)	(64,100)	(49,109)	(33,979)
PBT	28,101	7,093	(2,582)	22,152	37,180
Tax	(2,616)	(1,436)	258	(4,430)	(7,436)
PAT	25,485	5,657	(2,324)	17,722	29,744

Balance Sheet (₦'000)\*

Assets					
Cash & Short term funds	301,393	361,167	336,486	447,561	579,452
Net Loans	791,095	763,635	1,068,330	1,091,305	1,132,623
Fixed Assets	55,062	62,396	64,903	68,829	74,752
LT investment	446,232	439,438	475,183	489,438	504,121
Total Assets	1,933,123	1,753,232	2,046,360	2,200,997	2,397,335
Liabilities					
Deposits	1,493,081	1,233,591	1,414,541	1,562,250	1,720,737
Taxation	106,496	141,297	240,205	246,210	253,596
Borrowings	1,724,099	1,538,623	1,853,427	1,988,030	2,153,904
Total liabilities	209,025	214,609	192,933	212,967	243,431
Shareholders' fund	301,393	361,167	336,486	447,561	579,452
Key Ratios					
EPS	1.76	0.24	(0.10)	0.77	1.28
DPS	0.10	-	-	-	0.07
BVPS	14.44	9.27	8.33	9.20	10.51
ROE	14.7%	2.7%	-1.1%	8.7%	13.0%
ROA	1.5%	0.3%	-0.1%	0.8%	1.3%
Loan to Deposits	53.0%	61.9%	75.5%	69.9%	65.8%
Cost to income	64.6%	61.0%	61.3%	58.3%	59.2%
NPL	5.1%	6.9%	7.0%	5.0%	4.5%
Cost of risk	3.3%	7.2%	6.0%	4.5%	3.0%
WACF	3.4%	3.1%	2.5%	2.2%	2.6%
CAR	17.5%	16.3%	16.0%	16.4%	16.9%

Source: ARM Research \*unless otherwise stated

## ARM ratings and recommendations

ARM now employs a two-tier rating system which is based on systemic importance of the security under review and the deviation of our target price for the stock from current market price. We characterize systemic importance as a function of a stock's ranking among the group of top 20 stocks by NSE market capitalization over a trailing 6-month period (minimum) to the review date. We adopt a 5-point rating system for this category of stocks and a 3-point rating system for stocks outside this group. The choice of top 20 stocks arises from the consideration that this group of stocks constitutes >75% of overall market capitalization and stocks outside this group are generally less liquid and individually account for <<1% of market capitalization. For stocks in both categories, the basis for ratings subject to target price deviation is outlined below:

TOP 20		NON-TOP 20	
Rating	Deviation	Rating	Deviation
<b>STRONG BUY</b>	>20%	<b>BUY</b>	>20%
<b>OVERWEIGHT</b>	10% — 20 %	<b>NEUTRAL</b>	5% — 20 %
<b>NEUTRAL</b>	0% — 10 %	<b>SELL</b>	<5%
<b>UNDERWEIGHT</b>	-5% — 0%		
<b>SELL</b>	<-5%		

RECOMMENDATION KEY	
Rating	Recommendation
<b>BUY</b>	Accumulate security to a substantial extent constrained only by portfolio diversification considerations
<b>OVERWEIGHT</b>	Accumulate security to an extent moderated by cognizance of its benchmark weight
<b>NEUTRAL</b>	Maintain status quo for security with respect to current holding—i.e. keep if already holding and don't buy otherwise—subject to reasonable portfolio constraints
<b>UNDERWEIGHT</b>	Minimise exposure to security taking cognizance of its index weighting
<b>SELL</b>	Sell-off security completely from portfolio

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