

Price	₦0.95
FVE (last communicated)	₦1.39
52-week range	₦0.95 – ₦3.73
Market Cap. (₦mn)	22,002
1-month Avg. Vol	7,652,552
Curr. P/B	0.11x

#### DIAMONDBNK:NL - Share Price Trend



#### Analyst(s)

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## Diamond Bank Plc. (DIAMONDBNK.NL)

### Equity Commentary

#### Overblown fright or Justified concerns?

- Last week, global rating agency S&P lowered its issuer rating of Diamond Bank by one notch to CCC+ from B- majorly due to two concerns. Firstly, the rating agency expressed concerns on the possibility of higher provisioning which will put pressure on the bank's capitalization. Furthermore, S&P believes the bank's foreign-currency liquidity position remains vulnerable largely due to its maturing Eurobond in May 2019. The impact of this downgrade saw investors sell-off the bank's Eurobond with yields spiraling to over 30% (+1500bps MTD).
- The rating downgrade also comes after a corporate governance racket which saw the resignation of four non-executive directors – including the Chairman – without concrete reasons. However, market feelers suggest the development was related to the difference among the board on recapitalization plans. Information suggest that the bank was in the process of either accepting capital injection from a major shareholder or being taken over by a bigger bank, who aims to leverage on Diamond bank to penetrate the retail market for cheap deposit. While this news has been canned by Diamond Bank, the saying that there is no smoke without a fire now keeps us on the observer mode, awaiting the end of the twist.

**Table 1: Major Shareholders of Diamond Bank**

Shareholder	Stake
<b>Carlyle Group</b>	17.80%
<b>Kunoch Holdings</b>	9.30%
<b>Diamond Partners Ltd</b>	6.10%

Source: Bloomberg, ARM Research

- Eurobond redemption...any cause for concern?*** Diamond Bank is faced with \$200 million maturity of its Eurobond in May 2019. Based on recent engagement with management, the bank plans to fully redeem the bond as against refinancing. Management expects to redeem the bond via proceeds of the sale of the UK business, repayments of FCY loans (45% of total loans) and FX flows from bilateral agreements. As at FY 2017, Diamond bank had a net-long FCY position of \$95 million while S&P suggest the bank has \$70 million set aside for repayment of maturing Eurobond. The balance is expected to come from the proceed of the sale of UK business. In trying to estimate the expected proceeds, we use average P/B of comparable banks listed in the UK (0.98x) with the book value of Diamond Bank UK (\$156 million), which brings expected market value of \$153 million. Hence, we believe Diamond Bank is in a fair position to redeem its maturing Eurobond.
- We see bargain opportunity in buying into the Eurobond now following the sell-off which has seen yields spiked to over 30%, as we believe the recent selloff is largely driven by the downgrade in ratings, which has now put the bond below minimum investment criteria for institutional funds.

**Table 2: Yields of Comparable Eurobonds with similar Credit Rating**

Security	Price	Yield (%)	Z-Spread (bps)
<b>Avg of Comparables</b>		<b>13.13</b>	<b>1015</b>
<b>DIAMBK 8 ¾ 05/21/19</b>	<b>90</b>	<b>31.15</b>	<b>2842</b>
ALBRK 10 ½ 11/30/25	89.14	17	1391
GALIAR 8 ¼ 07/19/26	93.07	11.31	818
ECOTRA 8 ¾ 08/14/21	99.57	9.32	647
ACCESS 9 ¼ 06/24/21	100.09	9.07	628
BANBRA 6 ¼ PERP	87.37	9.27	611
BANVOR 8 ¼ PERP	98.91	8.57	543
FBNNL 8 07/23/21	99.96	8.03	521
BANBRA 9 PERP	103.58	8.19	504
BCGBK 6 ¾ 03/15/23	97.74	7.36	422
BANBRA 9 ¼ PERP	107.61	7.2	406

Source: Bloomberg, ARM Research

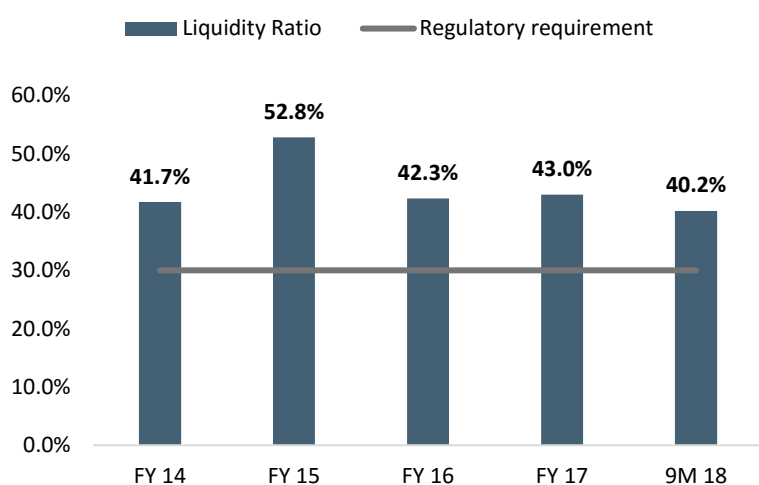
- Recapitalization or License Conversion?*** Diamond bank's capital adequacy ratio (CAR) currently stands at 16.3%, largely supported by the sale of Diamond Bank S.A<sup>1</sup>. Earlier in 2016, the bank almost saw its CAR fall below the minimum regulatory requirement, printing at 15.01%. Going forward, we expect higher provisioning to put pressure on the bank's CAR. Specifically, factoring our expectation of higher provisioning over Q4 18 (₦21.0 billion), we believe the bank's CAR could fall to 15.0% - 15.5%. Consequently, Diamond Bank may struggle to maintain a regulatory requirement for banks with

<sup>1</sup> It's West African business operation. Without the sale, CAR would have printed at 15.6%

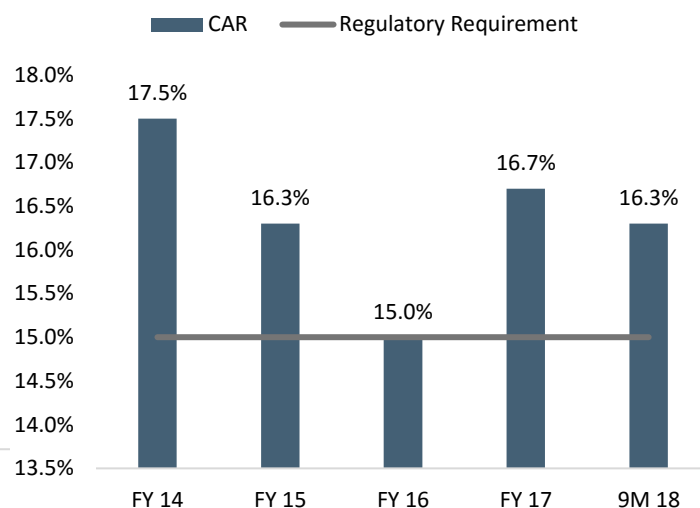
international operations (CAR of 15%). Thus, we expect the bank to either recapitalize or convert its license to a national banking license from international banking license following the sale of its UK business.

- Diamond bank has already received an offer of capital injection from a major shareholder. We believe the shareholder is Carlyle Group who currently owns about 18% stake in Diamond bank. Additional capital from Carlyle Group could see them having more control in the bank. Also, another option for the bank is to be acquired by a larger bank with potential synergy benefits. However, this option looks less likely as we expect some kick-backs by selected key shareholders. Irrespective, we are of the view that the bank will switch from its international banking license to a national banking license, post completion of UK divestment. This would bring regulatory capital requirement down to 10% from 15%. Thus, we expect an ease to capital adequacy issue in the coming period.
- Overall, we are of the view that the pending concerns on Eurobond repayment and Recapitalization will be short-lived as our analysis suggest no cause for alarm. However, we are still negative on profitability with our FY 2018 estimate, translating to a loss after tax of ₦2.6 billion (compared to a loss of ₦12.9 billion in 2017) on the back of funding cost pressure. Following a massive sell-off over the past few days (-32% MTD), current price (₦0.95) of the stock now translates to a **BUY** rating given our FVE of **₦1.39**.

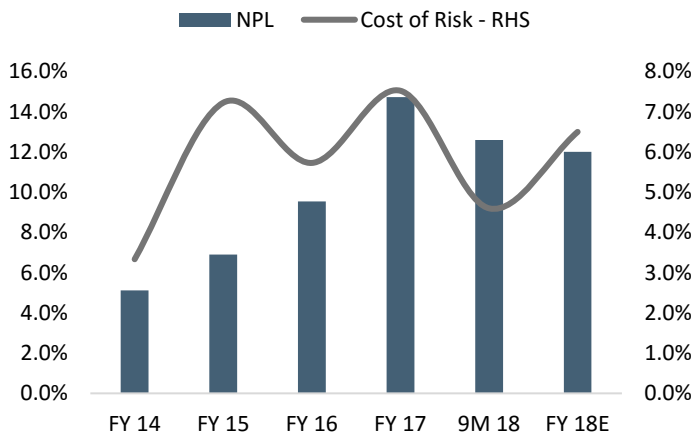
**Figure 1: Trend in Liquidity Ratio**



**Figure 2: Trend in Capital Adequacy Ratio**

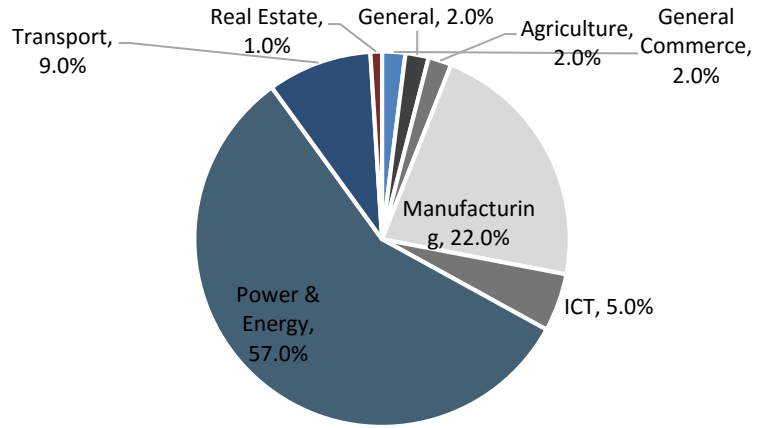


**Figure 3: Trend in NPL ratio and Cost of Risk**



Source: Company Financials, ARM Research

**Figure 4: Composition of NPL**



## Summary of Results and Forecast

Balance Sheet	2017	2018E	2019E	2020E	2021E
<b>Assets</b>					
Inv. Securities	357,843	368,578	405,436	433,817	446,831
Net loans	755,503	710,389	737,220	802,324	895,549
Gross loans					
Interest-earning assets	1,447,899	1,286,245	1,356,224	1,417,916	1,503,785
<b>Total assets</b>	<b>1,714,807</b>	<b>1,555,675</b>	<b>1,630,365</b>	<b>1,700,003</b>	<b>1,795,568</b>

<b>Liabilities</b>					
Interbank	10,959	19,178	21,096	22,151	23,258
Borrowings	231,812	173,859	199,938	206,936	214,179
Deposits	1,161,594	1,115,477	1,151,840	1,189,633	1,239,249
Interest-bearing liabilities	1,404,365	1,308,515	1,372,874	1,418,720	1,476,686
Total liabilities	1,455,630	1,359,779	1,424,139	1,469,985	1,527,951
<b>Shareholders Equity</b>	<b>259,177</b>	<b>195,895</b>	<b>206,226</b>	<b>230,018</b>	<b>267,618</b>

Income Statement	2017	2018E	2019E	2020E	2021E
Interest Income	145,323	145,762	146,337	150,167	155,720
Interest Expense	(47,038)	(54,460)	(51,183)	(49,494)	(46,671)
Net Interest Income	98,284	91,302	95,154	100,673	109,048
Non-Interest Revenue					
Gross Earnings	181,169	184,768	188,669	198,441	209,719
Staff Costs	23,788	24,506	25,246	26,523	27,866
Other Costs	65,060	62,514	63,368	65,201	67,479
Total Costs	88,847	87,019	88,614	91,725	95,345
PBT	(11,547)	(2,887)	4,638	23,203	40,836
Provision Charge	(56,830)	(46,175)	(44,233)	(34,019)	(26,866)
Tax	(1,350)	289	(557)	(3,016)	(5,309)
Minorities					
Net Profit	(12,897)	(2,598)	4,082	20,187	35,528
Dividend Paid	0	0	0	(2,644)	(4,178)

Key YoY growth rates (%)	2017	2018E	2019E	2020E	2021E
Loans	-24.1%	-6.0%	3.8%	8.8%	11.6%
Interest Earning Assets	-23.4%	-11.2%	5.4%	4.5%	6.1%
Deposits	-18.5%	-4.0%	3.3%	3.3%	4.2%
Interest Bearing Liabilities	-20.1%	-6.8%	4.9%	3.3%	4.1%
Assets	-16.3%	-9.3%	4.8%	4.3%	5.6%
Gross Earnings	3.4%	2.0%	2.1%	5.2%	5.7%
Costs	6.3%	-2.1%	1.8%	3.5%	3.9%
PBT	-442.8%	-75.0%	-260.7%	400.2%	76.0%
PAT	-744.7%	-79.9%	-257.1%	394.6%	76.0%
EPS	-744.7%	-79.9%	-257.1%	394.6%	76.0%

Per-share data (N)	2017	2018E	2019E	2020E	2021E
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No of common shares (mn)	23,160,389	23,160,389	23,160,389	23,160,389	23,160,389
EPS	(0.56)	(0.11)	0.18	0.87	1.53
DPS	0.00	0.00	0.00	0.11	0.18
BVPS	11.19	8.46	8.90	9.93	11.55

Balance-sheet ratios (%)	2017	2018E	2019E	2020E	2021E
Loan/Assets	44.1%	45.7%	45.2%	47.2%	49.9%
Deposit/Liabilities	79.8%	82.0%	80.9%	80.9%	81.1%
Loans/Deposits	65.0%	63.7%	64.0%	67.4%	72.3%
Assets/Equity	6.6	7.9	7.9	7.4	6.7

Asset Quality	2017	2018E	2019E	2020E	2021E
NPLs	119,976	91,861	78,847	59,056	46,401
NPLs/Gross Loans (%)	14.7%	12.0%	10.0%	7.0%	5.0%

Credit change (%)

Margins (%)	2017	2018E	2019E	2020E	2021E
Asset Yield	8.7%	10.7%	11.1%	10.8%	10.7%
WACF	3.0%	4.0%	3.8%	3.5%	3.2%
NIM	5.9%	6.7%	7.2%	7.3%	7.2%

Costs (%)	2017	2018E	2019E	2020E	2021E
Cost/Income	66.2%	66.8%	64.5%	61.6%	58.5%
Effective tax rate	-11.7%	10.0%	12.0%	13.0%	13.0%

Profitability ratios (%)	2017	2018E	2019E	2020E	2021E
RoAE	-5.3%	-1.1%	2.0%	9.3%	14.3%
RoAA	-0.7%	-0.2%	0.3%	1.2%	2.0%

## 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>	Minimize exposure to security taking cognizance of its index weighting
<b>SELL</b>	Sell-off security completely from portfolio
<b>RESTRICTED</b>	In certain circumstances, Asset & Resource Management ("ARM") Group policy and/or applicable law and regulations preclude certain types of communications, including an investment recommendation, during the course of ARM Securities' and/or ARM Group's engagement in an investment banking transaction and in certain other circumstances.

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