

16 August 2017

Guaranty Trust Bank Plc. | Earnings Report
Earnings advance on lean provisioning
(OVERWEIGHT: ₦42.04)

- Yesterday, Guaranty Trust Bank Plc. (GTB) released audited H1 2017 results, wherein earnings came in stronger at ₦83.7billion (YoY: 17% YoY) with EPS of ₦2.84. In addition, the bank raised interim dividend pay-out to 30kobo relative to trend pay-out of 25kobo which translates to a dividend yield of 1% on current pricing. Though the higher than expected pay-out hints at a strong earnings outlook, GTB is roughly on track to meet our expectations as H1 17 EPS amounts to 50% of our FY 17 estimate of ₦5.97.
- As in Q1 17, core earnings performance continued to reflect robust contribution of higher asset yields to interest income as GTB's favorable balance sheet dynamics (high CASA mix and asset tilt to treasury bills) shone through the numbers. Furthermore, the sizable loan loss provision (collective) in 2016 provided the bank legroom to scale back materially on this item in the current period. For context, despite a 27bps YoY increase in funding cost (WACF: 3.0%), asset yield growth (+272bps YoY to 12.4%) drove similar expansion in NIMs (+270bps YoY to 9.7%). Likewise, following ₦65.3billion loan loss provision booked in 2016 (78% collective), the bank booked just ₦7.2billion in the period (-81% YoY) with annualized Cost of Risk at 1.0%. That said, specific

Income Statement Data			
	2017 – 6M'm	2016 – 6M'm	%chg
Gross Earnings	213,132	208,604	2.17%
PBT	101,101	85,688	17.99%
PAT	83,679	71,768	16.60%
EPS	2.84	2.44	16.60%

Balance Sheet Data			
	2017- 6M 'm	2016 -Dec 'm	%chg
Loans	1,489,958	1,589,430	-6%
Total Assets	3,232,238	3,116,393	4%
Deposits	1,966,376	1,986,246	-1%
Total liabilities	2,694,240	2,611,491	3%
Net Assets	537,998	504,903	7%
BVPS	18.28	17.16	7%

Stock Data	
Price	₦39.00
52-week range	₦20.33– ₦42.00
Market Cap. (N'Bn)	1,145
1-month Avg. Vol	1,694,604
Curr. PE	7.9x
Bloomberg Ticker	GUARANTY:NL

GTB Plc- Share Price Trend

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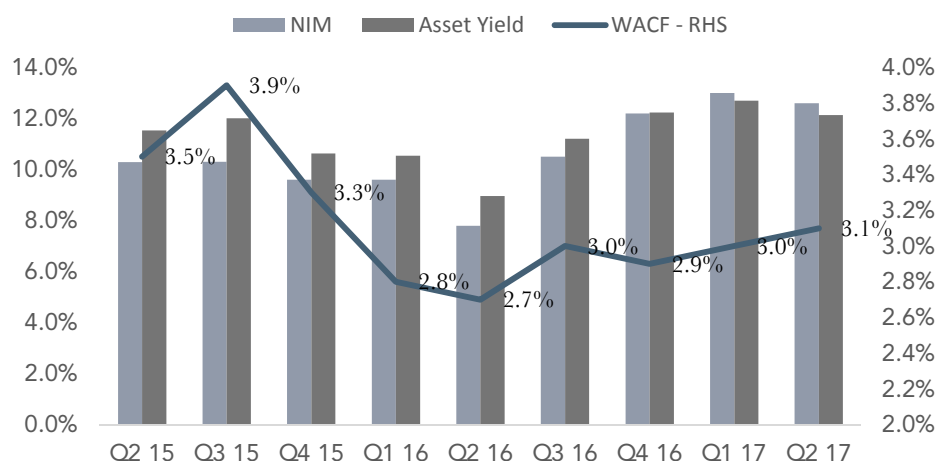
impairment increased 38% YoY to ₦14.4billion¹ which we think reflects asset quality deterioration.

- On the other side, despite higher trading income (+141% YoY), softer FX revaluation gains (-90% YoY) as well as lower fee income (-22% YoY) drove the 52% contraction in Non-Interest Revenue (NIR). Elsewhere, similar to Zenith, change in the treatment of AMCON levy, which entails the reporting of cost at the period incurred relative to accruals over the year, drove the increase in operating expenses (+25% YoY). Overall, lower NIR and higher operating expenses expanded cost to income ratio (CIR) by 7.9pps YoY to 38.7%.

Funding cost pressure in Q2 bolsters NIM contraction

- Breakdown of Q2 17 numbers revealed funding cost pressure in the period with annualized WACF tracking higher to 3.1% (+13bps QoQ). Pressures largely stemmed from existing Eurobond² as well as Treasury bills short positions even CASA tracked marginally lower to 81% (Q1 17: 82%). Also, interest income declined 3% QoQ to ₦81.8billion due to decline in interest income on loans (-2% QoQ) and investment securities (-6% QoQ). Consequently, asset yields declined 56bps QoQ to 12.1% with NIM following suit (-42bps QoQ) to 12.6%.

Figure 1: Trend in Funding cost, Asset Yield, and NIM



Source: Company financials, ARM Research

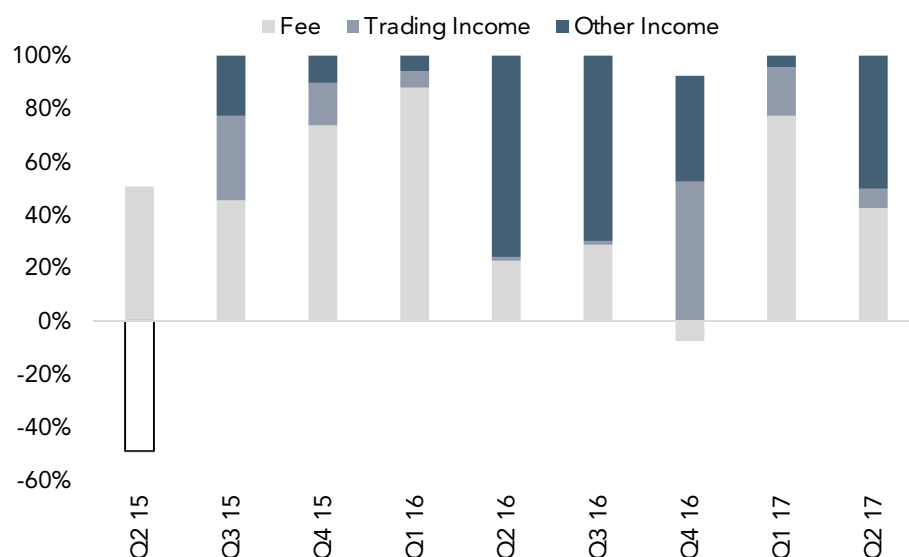
¹ Write-back in collective (₦3.4billion) and loan recovery (₦3.7billion) drove the sizable contraction in overall provision

² Amortized cost of Eurobond

Lower trading income takes shine of NIR in Q2 17

- After a brisk pace over Q1 17 (+67% QoQ), NIR slowed over Q2 17 after GTB booked lower trading income (-46% QoQ) largely reflecting losses on its bond position (₦157million) as well as softer income on FX trading position (-75% QoQ). In addition to this, lower FX revaluation gains of ₦5.6billion combined with declines in credit fees (-20% QoQ), COT (-18% QoQ) and higher transfer-related charges (₦720million) to drive softer NIR over the quarter. The foregoing alongside higher operating expenses (+15% QoQ) scaled up CIR in the review quarter to 40.3% (+3.3pps QoQ). However, reflecting lower loan loss provision (-11% QoQ) in the quarter, EPS printed at ₦1.43 (Q1: ₦1.41).

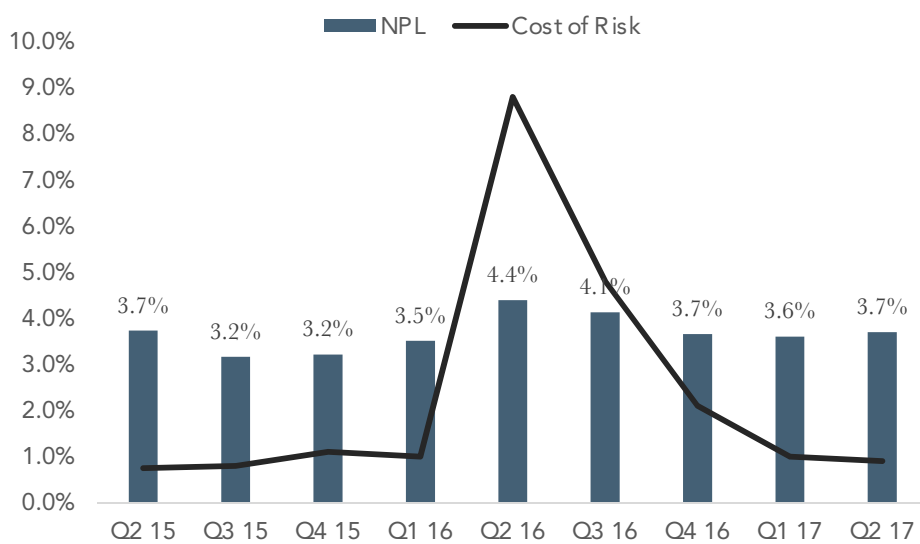
Figure 2: Attribution Analysis of Non-Interest Revenue



Source: Company financials, ARM Research

- Overall, GTB's ROAE rose 87bps to 31% despite the pressures in the macroeconomic landscape. This was on account of favourable balance sheet positioning to benefit from the elevated interest rate environment coupled with high provisioning base in 2016, which provided legroom for write-backs. The sturdy performance helped drive Capital Adequacy Ratio (CAR) well clear of regulatory thresholds of 16% to 22.2%.

Figure 3: NPL and Cost of Risk



Source: Company financials, ARM Research

Liquid balance sheet provides stage for solid FY 17

- On the interest income side, the decline in loan book as well as a still elevated interest rate environment suggest that management will continue to deploy balance sheet liquidity towards its securities portfolio. Thus, going by quarterly trend, we see room for strong growth in interest income over H2 17 and thus retain our FY 17E of ₦325billion (+24% YoY). On funding cost, despite pressures on deposit stemming from attractive Treasury Bills and improved dollar liquidity, we think GTB's CASA (81%) will keep funding cost moderated over the period with FY 17E WACF at 3.0% (H1 17: 3.0%). Consequently, we forecast net interest income to rise 27% YoY to ₦248.5billion with NIM of 9.4% (H1 17: 9.7%).
- On NIR, after the one-off transfer related charges and improved dollar liquidity, we expect fee income to reverse to quarterly trend of ₦14billion--~~₦15billion~~. Furthermore, trading income on FX and Treasury bills is expected to remain upbeat over the period. However, given impact of FX gains in prior year, NIR of ₦109billion is down 27% YoY.

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- Elsewhere, the one-off impact of AMCON levy guides to moderated growth in operating expenses in coming quarters with FY 17E operating expenses printing at ₦131billion (+15% YoY). On balance, reflecting softer NIR and increase in operating expenses, CIR of 36.6% is 3.6pps higher YoY.
 - In terms of asset quality, while concerns on specific loans suggest higher NPL, we feel the scale of GTB's collective provisioning over 2016 raises sizable scope for more write-backs over the rest of the year. Given our forecast for coverage ratio and cost of risk of 100% and 1.0% respectively (2016: 229% and 4.1%), we forecast loan loss charges to decline 77% to ₦15.3billion in FY 17E.
 - Cumulative impact of our estimates results in FY 17E EPS of ₦5.97 (+33% YoY) which largely reflects the strength in our net interest income projections and our views regarding softer impairment charges. The stock currently trades at a current P/E and P/B of 7.9x and 2.1x vs. Bloomberg Nigerian peer average at 7.4x and 0.5x respectively-- a justified premium in the light of GTB's best-in-class ROAE relative to the rest of the sector. We have an **OVERWEIGHT** rating on the stock with FVE at **₦42.04**.
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Summary of Results and Forecasts - Naira (₦)

ANNUAL					
Income Statement (₦'000) *	FY 2015A	FY 2016A	FY 2017F	FY 2018F	FY 2019F
Gross earnings	298,771	411,159	434,534	460,104	493,289
Interest Income	229,237	262,494	325,352	334,241	356,253
Interest Expense	(69,290)	(67,094)	(76,768)	(85,293)	(98,717)
Net interest income	159,947	195,400	248,584	248,948	257,536
Non-Interest Revenue	69,534	148,665	109,182	125,863	137,036
OPEX	(96,378)	(113,639)	(130,954)	(144,902)	(160,006)
Provisions	(12,408)	(65,290)	(15,263)	(10,142)	(3,732)
PBT	120,695	165,137	211,550	219,767	230,834
Tax	(21,258)	(32,856)	(35,963)	(37,360)	(39,242)
PAT	99,437	132,281	175,586	182,407	191,592
Balance Sheet (₦ '000) *					
Assets					
Cash & Short-term funds	254,633	455,863	501,450	551,595	606,754
Net Loans	1,371,926	1,589,430	1,526,284	1,690,256	1,865,905
Fixed Assets	87,989	93,488	101,533	112,331	121,997
LT investment	455,543	576,429	593,722	611,533	629,879
Other Assets	303,111	373,038	669,291	757,601	862,048
Total Assets	2,524,594	3,116,393	3,421,399	3,753,237	4,117,099
Liabilities					
Deposits	1,610,350	1,986,246	2,187,391	2,410,004	2,656,655
Taxation	17,740	17,928	17,928	17,928	17,928
Borrowings	345,240	345,871	356,248	366,935	377,943
Total liabilities	2,111,032	2,611,491	2,826,764	3,066,505	3,333,632
Shareholders' fund	413,562	504,903	594,635	686,732	783,467
Key Ratios					
EPS	3.38	4.49	5.97	6.20	6.51
DPS	1.77	2.00	2.95	3.07	3.22
BVPS	14.05	17.16	20.20	23.33	26.62
ROE	24.4%	28.8%	31.9%	28.5%	26.1%
ROA	4.0%	4.7%	5.4%	5.1%	4.9%
Financial leverage	6.10	6.17	5.75	5.47	5.25
Loan to Deposits	85%	80%	70%	70%	70%
Cost to income	42%	33%	37%	39%	41%
Liquidity ratio	40%	49%	48%	46%	45%
WACF	3.6%	3.0%	3.0%	3.1%	3.2%
Cost of risk	0.9%	4.1%	1.0%	0.6%	0.2%
NPL	3.2%	3.7%	3.8%	3.5%	3.3%

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
STRONG BUY	>20%	BUY	>20%
OVERWEIGHT	10% — 20 %	NEUTRAL	5% — 20 %
NEUTRAL	0% — 10 %	SELL	<5%
UNDERWEIGHT	-5% — 0%		
SELL	<-5%		

RECOMMENDATION KEY	
Rating	Recommendation
BUY	Accumulate security to a substantial extent constrained only by portfolio diversification considerations
OVERWEIGHT	Accumulate security to an extent moderated by cognizance of its benchmark weight
NEUTRAL	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
UNDERWEIGHT	Minimise exposure to security taking cognizance of its index weighting
SELL	Sell-off security completely from portfolio

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