

Guaranty Trust Bank Plc

Nigeria | Equities | Financial Services | April 09, 2018

PAC RESEARCH

Core Business Operations Improve Earnings

INVESTMENT SUMMARY

Guaranty Trust Bank, which is one of the leading financial institutions in Nigeria, continues to grow in terms of profit and asset base. The recent FY'17 audited accounts released by the bank shows a marginal growth of 1.11% YoY in its gross earnings as it rose to ₦419.23 billion (vs. ₦414.62 billion in FY'16). The growth in gross earnings was majorly triggered by interest income as it increased by 24.70% to ₦327.33 billion in FY'17 from ₦262.49 billion in FY'16. Interest Expenses rose by 20.23% to ₦80.67 billion in FY'17 from ₦67.09 billion in FY'16. Impressively, loan impairment charges largely reduced by 81.36% to ₦12.17 billion in FY'17 (vs. ₦65.29 billion in FY'16) having created huge collective impairment reserves in 2016 to act as a buffer against future credit losses. During the period, the company grew its net fees and commission income by 13.31% to ₦40.73 billion in FY'17 from ₦35.95 billion in FY'16. The bank was able to grow its customer deposits by 3.82% to ₦2.06 trillion in FY'17 from ₦1.99 trillion in FY'16 while loans and advances reduced by 8.85% to ₦1.45 trillion in FY'17 from ₦1.60 trillion in FY'16.

On the back of impressive returns from earnings assets, complimented by growth in fees and commission income, profit before tax increased by 21.26% to ₦200.24 billion in FY'17 (vs. ₦165.14 billion recorded in FY'16) while profit after tax increased by 28.87% to ₦170.47 billion in FY'17 from ₦132.28 billion in FY'16. EPS increased by 28.87% to ₦5.79 in FY'17 (vs. ₦4.49 recorded in FY'16) and as a result, the bank rewarded shareholders as it declared final dividend of ₦2.40 per share in FY'17 (vs ₦1.75 in FY'16). In addition to the interim dividend of ₦0.30 paid in 2017 (vs ₦0.25 in 2016), the dividend per share increased by 35.00% to ₦2.70 in FY'17 from ₦2.00 recorded in FY'16.

Based on the recent figure released by the company, we recommend a **HOLD** on the company shares at current price as present forward estimates places the company share price at ₦47.70

Fig. 1: Quarterly results highlights

	4Q2017	3Q2017	4Q2016	Q/q Δ	Y/y Δ
Net Int. Income (₦mn)	57,097	60,029	62,652	-4.88%	-8.87%
PBT (₦mn)	50,209	48,932	27,154	+2.61%	+84.96%
Net profit (₦mn)	44,892	41,898	15,199	+7.14%	+195.35%

Source: NSE, PAC Research

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Price:

- Current	₦43.50
- Target	₦47.70
Recommendation:	HOLD

* As at Monday April 9, 2018

Fig. 2: Stock data

FYE	December
Price Mov't: YtD / 52wk	+6.75%/+74.00%
52-week range	₦24.26 - ₦57.00
30-day Average vol.	21,480,270
Shares Outstanding ('mn)	29,431.18
Market Cap. (₦bn)	1,280.26
EPS (₦) - 12months trailing	5.79
DPS (₦) - FY2017	2.70

Source: NSE, Bloomberg, PAC Research

Fig. 3: Key ratios

	FY'17	FY'16
Net Interest Margin	58.84%	47.13%
Net profit margin	40.66%	31.90%
Equity multiplier	5.36x	6.17x
Cash/ total Assets	19.16%	14.63%

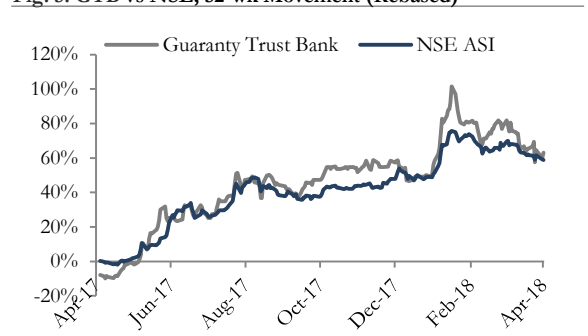
Source: NSE, PAC Research

Fig. 4: Valuations

	FY2016	FY2017	FY2018F	FY2019F
P/E	9.68x	7.51x	6.83	6.01x
P/B	2.54x	2.05x	1.83x	1.74x
Div Yield (%)	4.60	6.21	6.55	7.13
Payout Ratio	44.50%	46.61%	44.78%	42.83%
Ev/Revenue	2.87%	2.31%	2.04%	1.77%
Rev per share	14.09	14.24	15.48	16.75
ROE	26.20%	27.27%	26.73%	28.99%
ROA	4.24%	5.09%	5.19%	5.35%

Source: NSE, PAC Research

Fig. 5: GTB vs NSE, 52-wk Movement (Rebased)

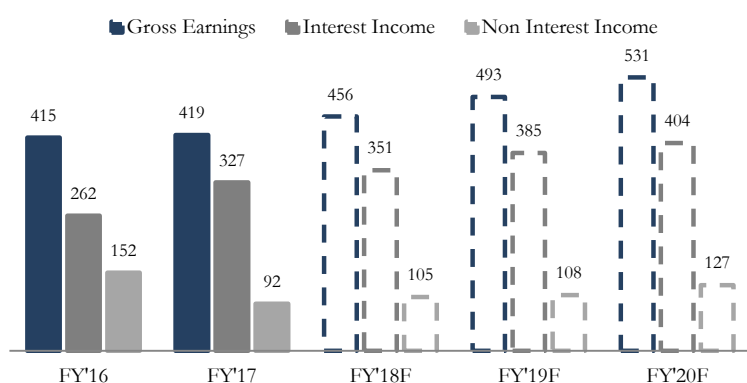


Source: Bloomberg, PAC Research

Gross earnings recorded a sluggish growth of 1.11% YoY as non-interest income dropped by 39.59%: Guaranty Trust Bank managed to improve its gross earnings as drop in non-interest income was offset by improvement in interest income. Gross earnings in FY'17 increased by 1.11% to ₦419.23 billion (vs ₦414.62 billion in FY'16) and this was majorly boosted by interest income as it grew by 24.70% to ₦327.33 billion in FY'17 (vs. ₦262.49 billion recorded in FY'16). However, non-interest income declined by 39.59% to ₦91.89 billion in FY'17 from ₦152.12 billion reported in FY'16. The decrease in non-interest income was majorly triggered by 64.99% dip in Other Income as it decreased to ₦37.63 billion in FY'17 (vs. ₦107.50 billion recorded in FY'16). Due to exchange rate stability during the period, FX revaluation gain dropped by 70.74% to ₦25.54 billion (vs. ₦87.29 billion in FY'16) while mark-up income dropped by 83.89% to ₦1.43 billion (vs. ₦8.88 billion in FY'16). Fee and commission income improved by 8.93% to ₦42.92 billion in FY'17 (vs. ₦39.40 billion in FY'16), due to improvement in account maintenance fees, commission on foreign exchange deals among others.

Gross earnings in FY'17 increased by 1.11% to ₦419.23 billion (vs ₦414.62 billion in FY'16) and this was majorly boosted by interest income as it grew by 24.70% to ₦327.33 billion in FY'17...

Fig. 6: Gross Earnings, Int. Income and Non Int. Income - FY'16-FY'20F (Billion NGN)



Source: NSE, PAC Research

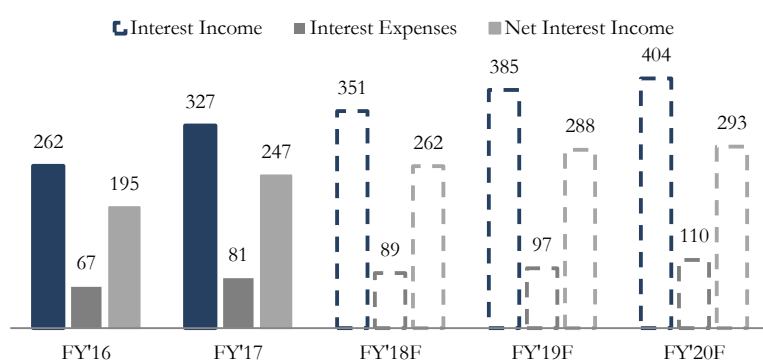
Interest income continues to impress but interest expenses surge: In full year 2017, interest income increased by 24.70% to ₦327.33 billion (vs. ₦262.49 billion in FY'16). The improvement in interest income can be partly attributed to the high yielding Treasury Bills as well as maintenance of appropriate Naira liquidity which resulted in improvement in interest income earned on investment securities and placements. Interest earned on investment securities increased by 86.35% to ₦100.14 billion in FY'17 (vs. ₦53.74 billion in FY'16) while interest income from cash and cash equivalents increased by 68.86% to ₦10.29 billion in FY'17 (vs. ₦6.09 billion in FY'16). Interest income from assets pledged as collateral is another key factor that contributed to the improvement in interest income as it increased by 110.36% to ₦11.14 billion in FY'17 from ₦5.29 billion reported in FY'16.

The improvement in interest income can be partly attributed to the high yielding Treasury Bills as well as maintenance of appropriate Naira liquidity...

There was a sluggish growth in interest income from loans and advances (which is the major contributor of the total interest income) as it increased by 3.61% to ₦203.23 billion in FY'17 from ₦196.15 billion reported in FY'16.

However, interest expenses increased by 20.23% to ₦80.67 billion in FY'17 (vs. ₦67.09 billion in FY'16) due to the tight monetary environment in 2017. Interest expenses of ₦60.61 billion in FY'17 on total deposit accounted for 75.13% of the total interest expenses, closely followed by interest expenses on other borrowed funds (FY'17: ₦10.77 billion) which accounted for 13.36% of total interest expenses. Thus, net interest income increased by 26.23% to ₦246.66 billion in FY'17 (vs. ₦195.40 billion in FY'16)

Fig. 7: Int. Income, Int. Expenses and Net Int. Income: FY'16-FY'20F (Billion NGN)



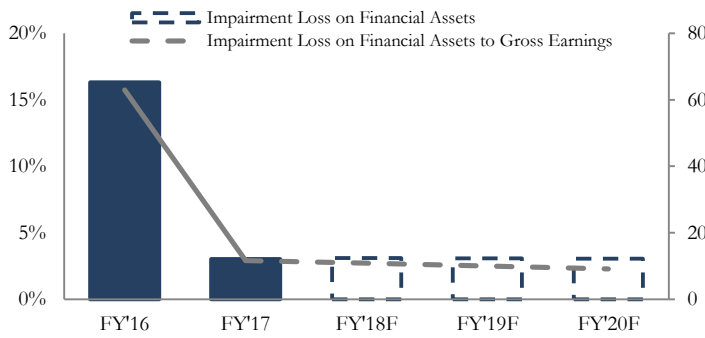
Source: NSE, PAC Research

Moderate Loan Impairment charges due to adequate provision in the previous financial year:

Impressively, loan impairment charges largely reduced by 81.36% to ₦12.17 billion in FY'17 (vs. ₦65.29 billion in FY'16) having created huge collective impairment reserves in 2016 to act as a buffer against future credit losses. Impairment charges on loans and advances to the bank reduced by 40.61% to ₦0.51 million (vs. ₦0.86 million in FY'16) while impairment on loans and advances to the customers reduced by 81.36% to ₦12.17 billion in FY'17 (vs. ₦65.29 billion in FY'16). The reduction in total loan impairment charges is largely attributed to the reversal in collective impairment of ₦18.82 billion in FY'17. Though the company was able to monitor its loans and advances to the customers as it reduced it by 8.85% to ₦1.45 trillion in FY'17 (vs. ₦1.59 trillion in FY'16) the non-performing loans to total loans continued to increase. Non-performing loans to total loans increased to 7.66% in 2017 from 3.66% in 2016 in FY'16. Of the total loans to the customers in FY'17, upstream sector accounted for 20.00%, closely followed by manufacturing sector (17.00%) and midstream sector (14%).

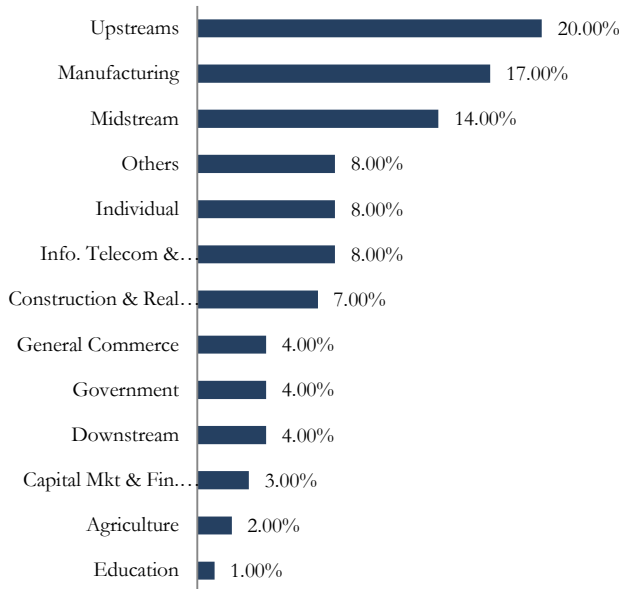
Impressively, loan impairment charges largely reduced by 81.36% to ₦12.17 billion in FY'17 (vs. ₦65.29 billion in FY'16) having created huge collective impairment reserves in 2016 to act as a buffer against future credit losses

Fig. 8: Impairment Loss on Financial Assets to Gross Earnings (FY'16-FY'20F)



Source: NSE, PAC Research

Fig. 9: Loan by Sectors - 2017



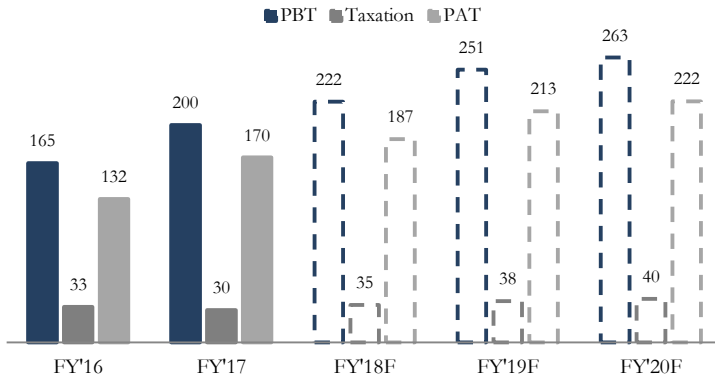
Source: NSE, PAC Research, GTB's Presentation

Strong profit before tax resulting from impressive returns from earnings assets: Non-interest income almost pose a threat to the profit of the company as it reduced by 39.59% to ₦91.89 billion in FY'17 (vs. ₦152.12 billion in FY'16). However, interest income offset the effect of non interest income on the profit of the company as it grew by 24.70% to ₦327.33 billion in FY'17 (vs. ₦262.49 billion in FY'16). Strong growth in profit before tax was driven largely by impressive returns from earning assets, complimented by growth in fees and commission income which was strong enough to moderate growth in cost of funds and operating expenses. Even with non-reoccurrence of huge FX revaluation gains (which drove PBT in FY'16), PBT grew by 12.26% to ₦200.24 billion in FY'17 (vs. ₦165.14 billion in FY'16).

Strong growth in profit before tax was driven largely by impressive returns from earning assets, complimented by growth in fees and commission income....

The provision for tax reduced by 9.38% to ₦29.77 billion in FY'17 (vs. ₦32.86 billion paid in FY'16) and as a result PAT surged to ₦170.47 billion in FY'17 from ₦132.28 billion recorded in FY'16, representing an increase of 28.87%.

Fig. 10: Profit before Tax, Taxation and Profit after Tax (FY'16-FY'20F) (Billion NGN)



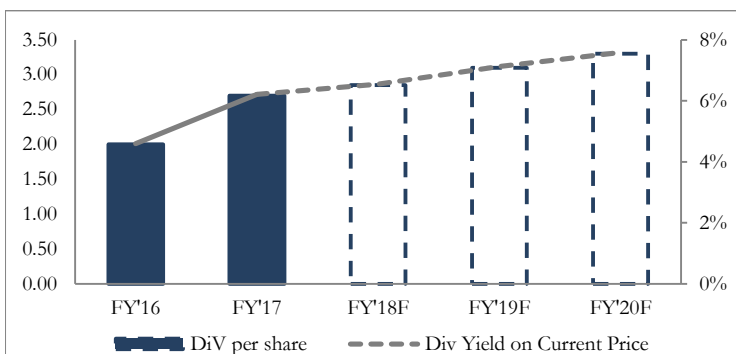
Source: NSE, PAC Research

High quality capital position of the bank gives room for improved dividends:

As at September 2017, the banking industry's NPLs was 15.18% and as a result, the Central Bank of Nigeria stopped the payment of dividends to shareholders by Deposit Money Banks and discount houses with huge bad loans and low capital base. GTB's NPL ratio grew to 7.66% in FY'17 from 3.66% in FY'16 and this is below the ratio of 10% dictated by the CBN. Also, Liquidity and Capital Adequacy Ratio of the bank are well above industry requirements of 30% for liquidity and 15% for capital adequacy ratio. Liquidity and capital adequacy ratio of the bank in FY'17 are 47.56% (FY'16: 42.19%) and 25.68% (FY'16: 19.79%) respectively. During the period, the company increased its net asset by 23.82% to ₦625.17 billion in FY'17 from ₦504.90 billion in FY'16 as the NAPS increased by 23.81% to ₦21.24 in FY'17 (vs ₦17.16 in FY'16). As a result, the bank paid dividend of ₦2.70 per share in FY'17, higher by 35% of ₦2.00 dividend per share paid in FY'16.

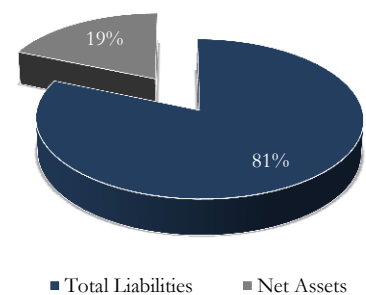
Liquidity and Capital Adequacy Ratio of the bank are well above industry requirements of 30% for liquidity and 15% for capital adequacy ratio. Liquidity and capital adequacy ratio of the bank in FY'17 are 47.56% (FY'16: 42.19%) and 25.68% (FY'16: 19.79%)

Fig. 11: Dividend Per Share and Dividend Yield (FY'16-FY'20F)



Source: NSE, PAC Research

Fig. 12: Total Liabilities Vs Net Asset in FY'17



Source: NSE, PAC Research

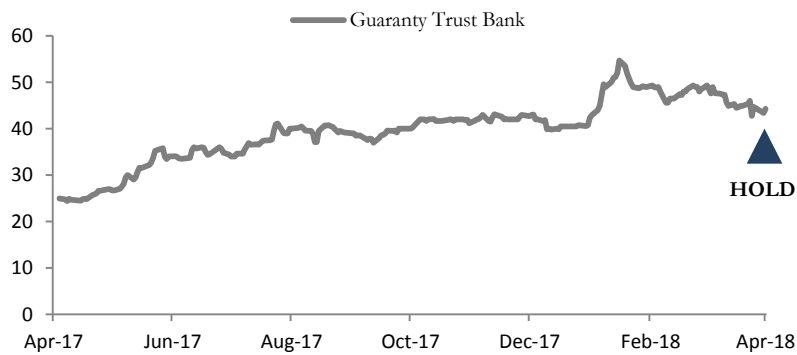
Valuation

Our valuation puts the target price of the stock at ₦47.70 representing an increase of 9.66% from the current price of ₦43.50. In arriving at the target price, we employed Discounted Cashflow Valuation methodology and Residual Income Model. Consequently, we maintained a **HOLD** recommendation on the stock of the company.

Our valuation and forecasts considered several factors (both quantitative and qualitative) among which are; the previous financial reports of the company, the current figures released by the company and the performance of the bank in the banking industry

Our valuation puts the target price of the stock at ₦47.70 representing an increase of 9.66% from the current price of ₦43.50.

Fig. 13: Share Price History



Source: NSE, PAC Research

Fig. 14: Statement of Profit or Loss, N'mn

	2016	2017	2018F	2019F
Gross Earnings	414,616	419,226	455,531	493,021
Change		1.11%	8.66%	8.23%
Interest Income	262,494	327,334	350,759	384,557
Change		24.70%	7.16%	9.64%
Interest Expenses	-67,094	-80,670	-88,920	-96,632
Change		20.23%	10.23%	8.67%
Net Interest Income	195,400	246,663	261,839	287,925
Change		26.23%	6.15%	9.96%
Impairment Charge for credit losses	-65,290	-12,169	-12,436	-12,326
Change		-81.36%	2.19%	-0.89%
Net Fees & Com. Income	35,947	40,732	48,833	55,662
Change		13.31%	19.89%	13.98%
Trade gains	5,218	11,339	14,076	19,179
Change		117.28%	24.14%	36.25%
Personnel expenses	-29,453	-32,832	-29,610	-32,046
Change		11.47%	-9.82%	8.23%
Profit Before Taxation	165,136	200,242	221,844	251,244
Change		21.26%	10.79%	13.25%
Taxation	-32,856	-29,772	-34,519	-38,214
Change		-9.38%	15.94%	10.71%
Profit After Taxation	132,281	170,470	187,325	213,030
Change		28.87%	9.89%	13.72%

Fig. 15: Statement of Financial Position, N'mn

	2016	2017	2018F	2019F
Cash and cash equivalents	455,863	641,974	710,629	798,695
Loans and advances	1,590,084	1,449,284	1,489,587	1,612,180
Fin. assets held for trading	12,054	23,946	30,521	33,525
Derivative financial assets	1,042	2,839	3,644	4,437
Investment Securities	528,213	544,523	575,605	610,754
Assets pledged as collateral	48,216	58,976	70,197	67,544
Property and equipment	93,488	98,670	104,954	113,592
Intangible asset	13,859	14,835	16,718	17,354
Deferred Tax Assets	1,578	1,667	2,824	3,205
Restr. Dep. & other assets	371,996	444,947	481,269	529,456
Total Assets	3,116,393	3,351,097	3,607,307	3,983,614
Deposits from banks	125,068	85,431	115,113	118,325
Deposits from customers	1,986,246	2,062,048	2,232,103	2,440,456
Fin. Liab. held for trading	2,065	2,647	2,551	2,761
Other liabilities	115,682	218,349	174,058	271,162
Current inc. tax liabilities	17,928	24,147	22,549	26,377
Deferred tax liabilities	17,641	18,076	19,497	21,101
Debt securities issued	126,238	92,132	100,126	108,366
Other borrowed funds	219,634	220,492	240,429	260,217
Total Liabilities	2,611,491	2,725,929	2,906,426	3,248,765
Net Assets	504,903	625,168	700,880	734,849

Fig. 16: Profitability Ratio

	2016	2017	2018F	2019F
Return on Equity	26.20%	27.27%	26.73%	28.99%
Return on Assets	4.24%	5.09%	5.19%	5.35%
Net interest income to rev.	47.13%	58.84%	57.48%	58.40%
PBT margin	39.83%	47.76%	48.70%	50.96%
Net Profit Margin	31.90%	40.66%	41.12%	43.21%
"ROCE	7.84%	9.53%	10.06%	9.99%

Fig. 17: Asset Utilisation

	2016	2017	2018F	2019F
Cash/Revenue	109.95%	153.13%	156.00%	162.00%
Revenue to total assets (x)	13.30%	12.51%	12.63%	12.38%
Int. Income /Total Assets	8.42%	9.77%	9.72%	9.65%
Loan Loss Exp./Net Int.	33.41%	4.93%	4.75%	4.28%
Loan Loss Exp./PAT	49.36%	7.14%	6.64%	5.79%
fixed asset turnover	22.55%	23.54%	0.62%	0.65%

Fig. 18: Liquidity Ratios

	2016	2017	2018F	2019F
Current ratio	1.19	1.23	1.24	1.23
Cash ratio	0.17	0.24	0.24	0.25
Interest Coverage ratio	2.46	2.48	2.49	2.60
Liquid Assets/Total Deposit	16.74	25.17	19.72	20.95
Loans & Advances/Total Deposit	3.58	6.06	4.95	5.42
Liquid Assets/Total Assets	0.67	0.64	0.63	0.62
Debt/net income	1.66	1.29	1.28	1.22
Debt to asset	0.07	0.07	0.07	0.07
Debt to equity	0.44	0.35	0.34	0.35
Total Liabilities / Total Asset	0.84	0.81	0.81	0.82
Cost to income ratio	0.48	0.24	0.22	0.20
net interest margin	0.08	0.08	0.08	0.08
Total liabilities/equities	5.17	4.36	4.15	4.42

Fig. 19: Shareholders' Investment Ratios

	2016	2017	2018F	2019F
Earnings per share	4.49	5.79	6.36	7.24
DiV per share	2.00	2.70	2.85	3.10
NAVPS	17.16	21.24	23.81	24.97
Earnings yield	10.33%	13.32%	14.63%	16.64%

Fig. 20: Capital Adequacy Ratios

	2016	2017	2018F	2019F
Loans & Advances/Equity	3.15	2.32	2.13	2.19
Equity/Total Assets	0.16	0.19	0.19	0.18
Loan Loss Expense/ Equity	0.13	0.02	0.02	0.02

Source: Company's Annual Reports, PAC Research

Equity research methodology employed in this report

Views documented in this equity research report stem from conclusions reached through the use of multiple valuation methodologies, industry-wide knowledge, company specific information and our near to medium term expectations of industry and company performance, as well as market outlook. Our forecasts are based on a combination of top down and bottom up analysis, alongside historical trends in industry and company financials. Where appropriate, we factored in available forecasts and business direction provided by company management.

Our recommendation tends towards value investing. Therefore, our investment rank gauge—a customized scale we use to judge how well a firm under coverage has performed—is determined using major value parameters as well as relevant ratios and multiples computed with figures from the company's most recent financials.

The variables used to arrive at the company's investment rank cover a wide range of measures which characterize liquidity, operational efficiency, profitability, profit margins, growth, economic viability, gearing, relative valuation ratios, capital structure and management performance. Our investment recommendation is underpinned by the upside or downside potential of a stock under coverage. This potential is estimated by comparing the stock's current market price to its price target and fair value, on a percentage increase or decrease basis as summarized below:

Deviation from current price	Recommendation
>30%	STRONG BUY
10% to < 30%	BUY
-10% to < 10%	HOLD
<-10%	SELL

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