

Interest Income Recedes as Gross Earnings Falls by 7.7%

INVESTMENT SUMMARY

In the first half of 2021, Guaranty Trust Holding Company (GTCO) recorded a slowdown in its top-line as gross earnings fell by 7.65% to ₦207.91 billion from ₦225.14 billion reported in the first half of 2020. The reduction in the gross earnings could be attributed to the decline in total interest income, which receded significantly by 17.97% to ₦126.09 billion in H1'21 (vs. ₦153.71 billion in H1'20) as a result of reduced average yield on earnings assets during the period. However, the total non-interest income of the bank rose by 14.55% to ₦81.82 billion in H1'21 (vs. ₦71.43 billion in H1'20), driven by significant fall in the fee & commission income. Impressively, the total interest expense of the bank fell by 27.05% to ₦19.04 billion in H1'21 (vs. ₦26.09 billion in H1'20), as a result of lower yields, which resulted in lower cost-of-fund during the period. Meanwhile, the total operating expenses fell by 7.24% to ₦89.34 billion in H1'21, (vs. ₦83.31 billion reported in H1'20), due to higher AMCON expenses. With increase in economic activities in H1'21 relative to the same period last year and positive economic outlook in months ahead, the loan impairment charge fell significantly by 30.35% to ₦4.72 billion in H1'21 (H1'20: ₦6.77 billion).

The weak interest income and higher operating expenses outweighed the improvement in loan impairment charge and non-interest income. Consequently, the profit before tax declined by 15.18% to ₦93.06 billion in H1'21 (vs. ₦109.71 billion in H1'20). The bank made a lower provision of ₦13.64 billion for tax in H1'21 billion (H1'20: ₦15.44 billion). Despite the lower tax provision, profit after tax decreased by 15.76% to ₦79.42 billion (vs. ₦94.27 billion in H1'20) and this translated to 12-month trailing EPS of ₦6.34 (H1'20: ₦6.52). Impressively the bank rewarded the shareholders with interim dividend payment of ₦0.30 per share (H1'20: ₦0.30). Based on the figures released by the company, we downgrade our target price to ₦35.53 (Previous target price: ₦38.19) but maintain a **BUY** rating on the stock at the current price of ₦27.40.

Table 1: Quarterly results highlights

	1Q2021	4Q2020	1Q2020	Q/q Δ	Y/y Δ
Gross Earnings (₦mn)	101,748	106,166	112,273	-4.16%	-9.37%
PBT (₦mn)	39,373	53,683	51,510	-26.66%	-26.66%
Net profit (₦mn)	33,868	45,546	44,204	-25.64%	-23.38%

Source: NSE, PAC Research

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Price:

- Current	₦27.40
- Target	₦35.53
Recommendation:	BUY

* As at Thursday September 23, 2021

Table 2: Stock data

FYE	December
Price Mov't: YtD / 52wk	-15.30%/+7.87%
52-week range	₦25.35 - ₦38.45
30-day Average vol.	27,289,190
Shares Outstanding ('mn)	8,641.67
Market Cap. (₦bn)	806.41
EPS (₦) - 12months trailing	6.34
DPS (₦) - FY2020	3.00

Source: NSE, Bloomberg, PAC Research

Table 3: Key ratios

	H1'21	H1'20
Net Interest Margin	6.98%	9.74%
Net profit margin	38.20%	41.87%
Equity multiplier	6.29x	6.26x
Cash/ total Assets	15.83%	16.82%

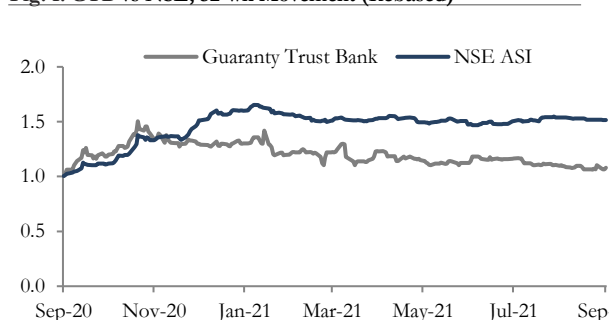
Source: NSE, PAC Research

Table 4: Valuation

	FY2019	FY2020	FY2021F	FY2022F
P/E	4.10x	4.00x	4.69x	4.17x
P/B	1.17x	0.99x	0.93x	0.97x
Div Yield (%)	10.22	10.95	10.95	11.68
Payout Ratio	41.86%	43.83%	51.38%	48.69%
Ev/Revenue	0.89x	0.44x	0.36x	0.37x
Rev per share	14.79	15.47	15.00	15.38
ROE	28.64%	24.73%	24.38%	23.92%
ROA	5.24%	4.07%	4.03%	4.12%

Source: NSE, PAC Research

Fig. 1: GTB vs NSE, 52-wk Movement (Rebased)



Source: Bloomberg, PAC Research

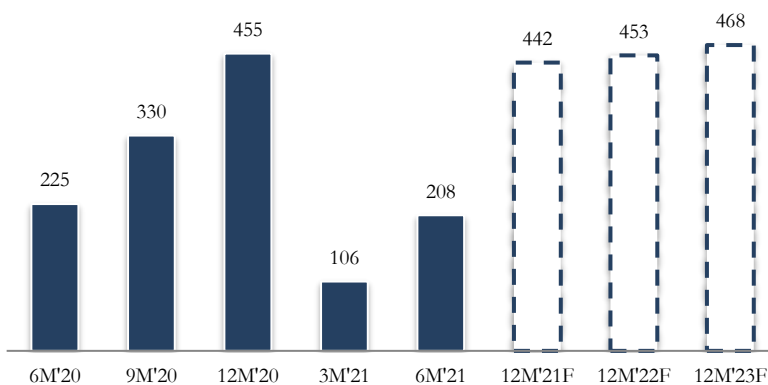
Gross earnings dips by 7.65% year-on-year, as a result of lower interest

income: Guaranty Trust Holding Company reported a setback in the top-line in the H1'21 as gross earnings dipped by 7.65% to ₦207.91 billion (vs ₦225.14 billion reported in H1'20), mainly as a result of lower interest income recorded during the period. The interest income of the bank fell significantly by 17.97% to ₦126.09 billion in H1'21 (vs. ₦153.71 billion in H1'20). However, the non-interest income line of the bank continued to improve as it increased by 14.55% to ₦81.82 billion in H1'21 (vs. ₦71.43 billion recorded in H1'20), due to significant improvement in fee & commission income lines and higher discounts & recoverables from foreign exchange.

The contribution of total non-interest income to gross earnings improved significantly to 39.35% (vs. 31.73% in H1'20) while the share of total interest income fell to 60.65% in H1'21 (vs. 68.27% in first half of 2020). In the second half of 2021, we may likely see improvement in the gross earnings as we expect the bank to improve the interest income line and non-interest income line. The interest income line would be driven by relatively high yields (when compared to the lower yields in the second half of 2020) while the non-interest income line of the bank would be driven by the persistent increase in the electronic business transactions.

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Fig. 2: Gross Earnings – 6M'20 – 12M'23F (Billion NGN)



Source: NSE, PAC Research

Interest income falls by 17.97% year-on-year, driven by 372 bps decline in

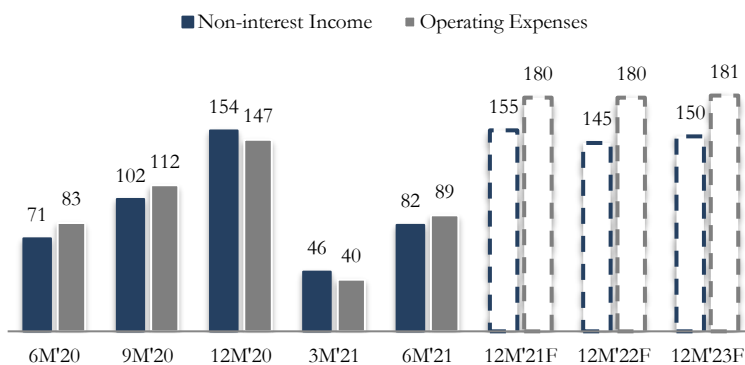
yield on interest earning assets: The total interest income of the bank continued on a downward trend in H1'21 as it declined by 17.97% to ₦126.09 billion (vs. ₦153.71 billion in H1'20), despite the improvement in earning assets during the period. The setback recorded in interest income line could be attributed to the reduction in interest income from loans and advances and interest income from investment securities, driven by 372 bps fall in average yield during the period.

The interest income from loans & advances and interest income from investment securities fell by 2.16% and 22.34% to ₦91.71 billion (H1'20: ₦93.74 billion) and ₦116.87 billion (H1'20: ₦150.49 billion) respectively. With the current high yields, when compared with lower yields in the second half of the previous year, we expect a growth in the interest income line of the bank in the second half of 2021.

Propped the lower yields environment, the interest expenses of the bank fell significantly by 27.05% to ₦19.04 billion in first half of 2021 (vs. ₦26.09 billion in first half of 2020), driven by changes to interest paid on savings account deposits which is indexed to Monetary Policy Rate (MPR). Recall that the Central Bank of Nigeria changed interest rate paid on savings deposit from 30% to 10% of MPR when the Apex bank adjusted the MPR downward to 11.5% in September 2020 (from 12.5%). This resulted in a lower cost-of-fund of 0.7% in H1'21 (H1'20: 1.5%). However, the lower interest income outweighed the progress recorded in non-interest income as net-interest income fell by 16.11% to ₦107.06 billion in H1'21 (vs. ₦127.62 billion). We maintain that the second half of 2021 will witness upward repricing of rates in the banking sector as we expect the yields during this period to be higher than the yields recorded in the second half of 2020. This may lead to higher interest expense in the coming quarters.

With the current high yields, when compared with lower yields in the second half of previous year, assume a turnaround in the interest income line of the bank in the second half of 2021.

Fig. 3: Interest Income and Interest Expenses: 6M'20 – 12M'23F (Billion NGN)



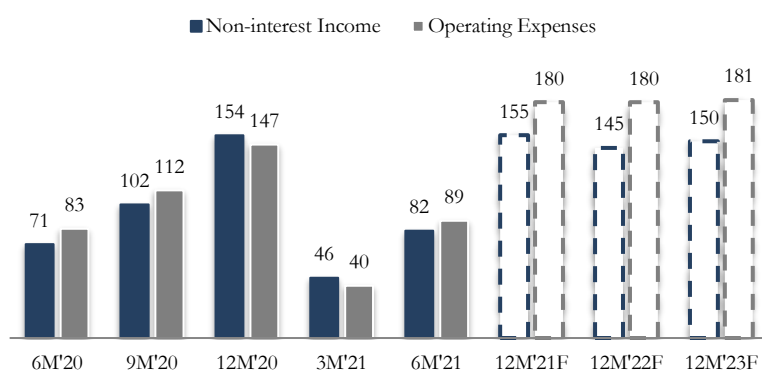
Source: NSE, PAC Research

With significant improvement in fee and commission income, non-interest income rises by 14.55% year-on-year: In six-month to June 2021, the non-interest income of GTCO grew by 14.55% to ₦81.82 billion (vs. ₦71.43 billion in six-month to June 2020). This was driven mainly by the significant improvement in fee and commission income during the period. The fee and commission of the bank increased by 44.70% to ₦38.28 billion in H1'21 (vs. ₦26.46 billion reported in H1'20) due to the progress recorded in electronic business income and account maintenance charges. The electronic business revenue of the bank improved by 59.90% to ₦10.50 billion in H1'21 (H1'20: ₦6.57 billion) due to increased in the level of awareness of the online banking services with attendant decline in traffic in the banking halls.

In addition, account maintenance charges increased by 40.82% to ₦7.80 billion in H1'21 (H1'20: ₦5.51 billion) due to growth recorded in turnover volumes.

However, the operating expenses of the bank increased by 7.24% to ₦89.34 billion in H1'21 (vs. ₦83.31 billion in H1'20), mainly driven by the significant increase in AMCON expenses, higher right-of-use asset depreciation, among others. The increase in the operating expenses of the bank resulted in a higher cost-to-income ratio of 48.98% in H1'21 (H1'20: 43.16%). In our own opinion, the cost-minimisation strategy of the bank is yielding positive result as the 7.24% increase in the OPEX is significantly lower than Nigeria's inflation rate of 17.75% recorded in June 2021..

Fig. 4: Non-Int. Income and Operating Expenses: 6M'20 – 12M'23F (Billion NGN)



Source: NSE, PAC Research

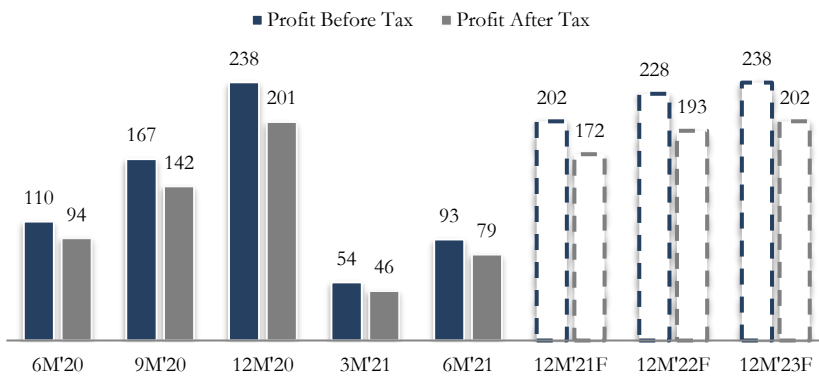
Despite the lower loan impairment charges, PBT falls by 15.18% year-on-year: Following the positive outlook of the macro-economic variables which impacted the Expected Credit Loss (ECL) model, the loan impairment charges of the bank declined significantly by 30.35% to ₦4.72 billion in the first half of 2021 (vs. ₦6.77 billion in the first half of 2020). However, the progress recorded in the non-interest income line and loan impairment charge was outweighed by the setback reported in the interest income line and operating expenses as profit before tax declined by 15.18% to ₦93.06 billion in H1'21 (vs. ₦109.71 billion reported in H1'20). However, the bank made a lower provision of ₦13.64 billion for tax during the period (H1'20: ₦15.44 billion). Notwithstanding the lower tax provision, profit after tax fell by 15.76% to ₦79.42 billion in H1'21 (vs. ₦94.27 billion in H1'20). This resulted in lower trailing earnings per share (EPS) of ₦6.34 (vs. ₦6.52 recorded in previous period).

With the expectation of improved interest income and higher demand for electronic banking products, we expect sticky growth in the bottom line of GTCO in the third quarter and fourth quarter of 2021.

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Fig. 5: Profit before Tax and Profit after Tax – 6M'20 – 12M'23F (Billion NGN)



Source: NSE, PAC Research

A well-structured and diversified balance sheet: The bank rewarded the shareholders with interim dividend payment of 30 kobo per share: Guaranty Trust Holding Company maintained a robust balance sheet as total assets of the bank increased by 11.22% to ₦5.02 trillion in the first half of 2021 (vs. ₦4.51 trillion in the first half of 2020), driven mainly by higher investment securities and improved cash and cash equivalents. The bank continued to watch its risky assets closely as total loans and advances remained almost flat at ₦1.64 trillion in H1'21, when compared with ₦1.62 trillion in reported in H1'20. Upstream Oil and Gas industry accounted for 28% of the total loans, followed by the manufacturing industry (15%) and Midstream Oil and Gas Industry (14%) (Fig. 6). However, the downstream Oil and Gas Industry, which accounted for 0.5% of the total loans, has non-performing loans of 8.7% in H1'21 (H1'20: 10.9%) (Fig. 7)

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Fig. 6: Gross Loans by Industry: H1'20/H1'21

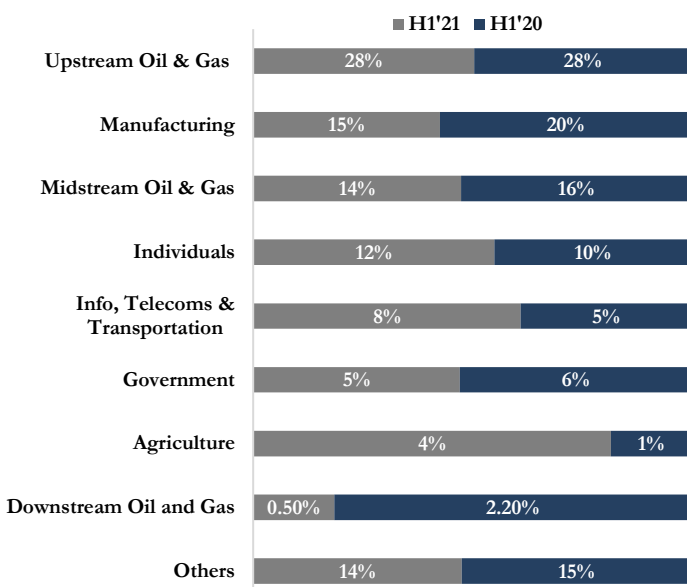
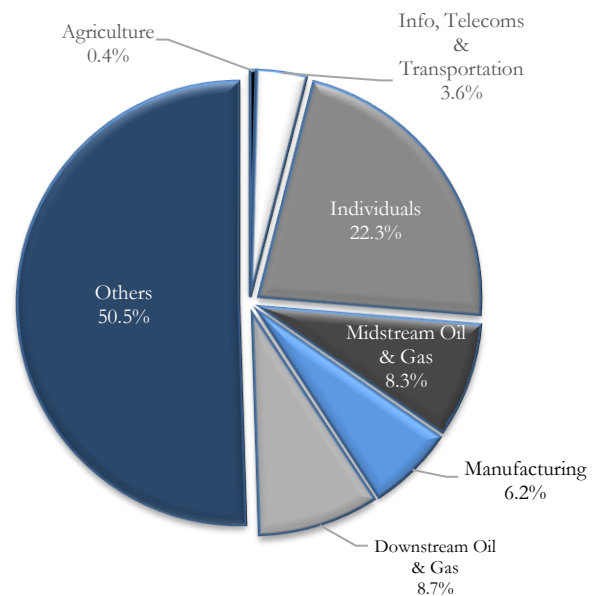


Fig. 7: Non-Performing Loans by Industry: H1'21



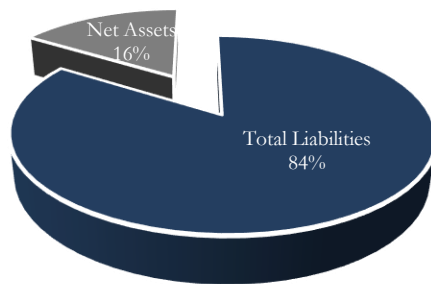
Source: GTCO PAC Research

The total liabilities of the bank increased marginally by 11.33% to ₦4.22 trillion in H1'21 (vs. ₦3.79 trillion in H1'20), mainly as a result of higher deposits during the period. The improvement in the total assets of the bank outweighed the increase in total liabilities and as a result, the net assets of the bank increased by 10.63% to ₦0.80 trillion in H1'21 (vs. ₦0.72 trillion in H1'20). This translated to a net asset per share of ₦27.10 in the first half of 2021 (vs. ₦24.50 in the first quarter of 2020)

Guaranty Trust Bank Plc maintained a well-structured and diversified balance sheet in the first half of 2021. The impressive balance sheet reflected on the liquidity ratio and capital adequacy ratio as they are well above the regulatory requirement. During the period, liquidity ratio increased to 44.71% (H1'20: 38.91%), driven mainly by the higher investment in Special Bills which closed at ₦561.1 billion, and this represents 61% of the Group's investment securities portfolio in H1'21. Also, the capital adequacy ratio of the bank improved to 24.00% in H1'21 (H1'20: 21.89%).

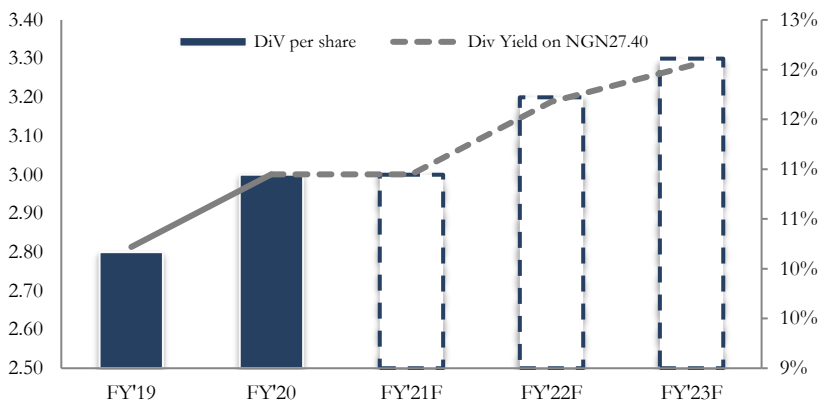
In line with our projections, the bank rewarded the shareholders with an interim dividend of ₦0.30 per share as balance sheet remained strong and healthy in the first half of 2021.

Fig. 8: Total Liabilities Vs Net Asset in H1'21



Source: Guaranty Trust Bank Plc, PAC Research

Fig. 9: Dividend Per Share and Dividend Yield (FY'19 - FY'23F)



Source: Guaranty Trust Bank Plc, PAC Research

Valuation

Our valuation puts the target price of the stock at ₦35.53, representing an increase of 29.66% from the current price of ₦27.40. In arriving at the target price, we employed Residual Income Valuation Model and Dividend Discount Model. Consequently, we maintain a **BUY** 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 bank, the current figures released by the bank, the performance of the bank in the banking industry and the outlook of Management of the banks.

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Fig. 10: Share Price History (Naira)



Source: NSE, PAC Research

Table 5: Statement of Profit or Loss, N'mn

	2019	2020	2021E	2022F
Gross Earnings	435,307	455,230	441,573	452,612
Change		4.72%	1.44%	2.50%
Interest and Similar Income	296,205	300,738	287,022	307,776
Change		-2.03%	-3.10%	7.23%
Interest and Similar Expenses	-64,842	-47,069	-46,365	-49,787
Change		-44.32%	-28.49%	7.38%
Net Interest Income	231,363	253,668	240,657	257,989
Change		14.04%	4.02%	7.20%
Impairment Charge for credit losses	-4,912	-19,573	-15,455	-15,841
Change		298.92%	214.66%	2.50%
Net Fees and Commission Income	59,444	46,935	68,885	75,134
Change		-7.00%	15.88%	9.07%
Trade gains	20,890	24,486	23,757	24,351
Change		-0.40%	13.72%	2.50%
Personnel expenses	-37,284	-37,606	-37,534	-38,472
Change		2.03%	0.67%	2.50%
Profit Before Taxation	231,708	238,095	202,152	227,573
Change		10.44%	-12.76%	12.58%
Taxation	-34,842	-36,655	-30,323	-34,136
Change		18.44%	-12.97%	12.58%
Profit After Taxation	196,866	201,440	171,829	193,437
Change		9.10%	-12.72%	12.58%

Table 6: Statement of Fin. Position, N'mn

	2019	2020	2021E	2022F
Cash and cash equivalents	593,551	627,224	593,551	772,753
Loans and advances	1,502,085	1,662,831	1,680,185	1,722,189
Financial assets held for trading -Available for Sale/fair value thru other compr. Income	73,486	67,535	72,860	67,892
Held to Maturity	618,477	696,645	300,270	307,776
Assets pledged as collateral	145,561	283,583	865,483	887,120
Loans and advances to banks	58,037	62,200	70,652	72,418
Loans and adv. to customers	1,513	99	2,208	2,263
Loans and adv. to customers	1,500,572	1,662,732	1,677,977	1,719,926
Property and equipment	141,775	148,783	154,551	158,414
Restr. deposits & other assets	577,433	1,226,481	1,236,404	1,267,314
Total Assets	3,758,919	4,944,653	5,209,677	5,306,425
Deposits from banks	107,518	101,510	101,562	104,101
Deposits from customers	2,532,540	3,509,319	3,819,605	3,937,726
Other liabilities	233,426	356,223	264,944	271,567
Deferred tax liabilities	10,569	24,961	24,287	24,894
Debt securities issued	0	0	0	0
Other borrowed funds	163,000	113,895	101,562	104,101
Total Liabilities	3,071,581	4,130,258	4,338,630	4,471,265
Net Assets	687,337	814,396	871,047	835,160
Total equity and liabilities	3,758,919	4,944,653	5,209,677	5,306,425

Table 7: Profitability Ratio

	2019	2020	2021E	2022F
Return on Equity	28.64%	24.73%	19.73%	23.16%
Return on Assets	5.24%	4.07%	3.30%	3.65%
Net interest income to Revenue	53.15%	55.72%	54.50%	57.00%
PBT margin	53.23%	52.30%	45.78%	50.28%
Net Profit Margin	45.22%	44.25%	38.91%	42.74%
ROCE	9.72%	7.18%	5.83%	6.26%

Table 8: Asset Utilisation

	2019	2020	2021E	2022F
Cash/Revenue	136.35%	163.78%	175.00%	170.00%
Revenue to total assets (x)	11.58%	9.21%	8.48%	8.53%
Interest Income / Total Assets	7.88%	6.08%	5.51%	5.80%
Loan Loss Exp./Net Int. Income	2.12%	7.72%	6.42%	6.14%
Loan Loss Exp./After Tax Profit	2.49%	9.72%	8.99%	8.19%
fixed asset turnover	0.52%	1.04%	1.05%	1.05%

Table 9: Liquidity Ratios

	2019	2020	2021E	2022F
Current ratio	1.22	1.20	1.20	1.19
Cash ratio	0.19	0.18	0.18	0.17
Interest Coverage ratio	3.57	5.06	4.36	4.57
Liquid Assets/Total Deposit	20.03	24.34	24.85	24.63
Loans & Advances/Total Deposit	5.75	6.86	2.96	2.96
Liquid Assets/Total Assets	0.57	0.50	0.48	0.48
Debt/net income	0.83	0.57	0.59	0.54
Debt to asset	0.04	0.02	0.02	0.02
Debt to equity	0.24	0.14	0.12	0.12
Total Liabilities / Total Asset	0.82	0.84	0.83	0.84
Cost to income ratio net interest margin AVERAGED	0.27	0.33	0.37	0.34
Total liabilities/equities	0.09	0.09	0.08	0.09
	4.47	5.07	4.98	5.35

Table 10: Shareholders' Investment Ratios

	2019	2020	2021E	2022F
Earnings per share	6.69	6.84	5.84	6.57
DiV per share	2.80	3.00	3.00	3.20
NAVPS	23.35	27.67	29.60	28.38
Earnings yield	24.41%	24.98%	21.31%	23.99%

Table 11: Capital Adequacy Ratios

	2019	2020	2021E	2022F
Loans and Advances/Equity	2.19	2.04	1.93	2.06
Equity/Total Assets	0.18	0.16	0.17	0.16
Loan Loss Expense/ Equity	0.007	0.024	0.018	0.019

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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