

Higher Interest Income and FX Revaluation Gain Drive Profitability

INVESTMENT SUMMARY

The 2020 unaudited first quarter reports released by Guaranty Trust Bank showed an impressive figure in the top-line as gross earnings improved by 2.30% to ₦112.87 billion (vs. ₦110.33 billion in the first quarter of 2019). In line with our expectation, the improvement in the top-line was boosted mainly by the interest income, which increased by 3.43% to ₦77.04 billion in Q1'20 (vs. ₦74.48 billion reported in Q'19). The higher interest income can be mainly attributed to the impressive income from the investment securities and loans & advances. During the period, the bank benefited significantly from the higher foreign exchange revaluation gain, which offset the lower fee & commission income recorded in the first quarter of 2020 and as a result, non-interest income remains flat at ₦35.83 billion in Q1'20 (vs. ₦35.84 billion in Q1'19). Impressively, the bank also benefited from the lower yield in the first quarter of 2020 as interest expense fell by 21.59% to ₦12.76 billion in Q1'20 (vs. ₦16.27 billion in Q1'19). Meanwhile, operating expenses increased by 10.85% to ₦39.77 billion (vs. ₦35.88 billion in Q1'19) while loan impairment charge rose significantly by 87.84% to ₦1.22 billion in Q1'20 (vs. ₦0.65 billion in Q1'19).

Due to the impressive higher interest income, lower interest expense and impressive FX revaluation gain, profit before tax rose by 2.14% to ₦58.20 billion in Q1'20 (vs. ₦56.98 billion in Q1'19). The bank made a higher tax provision of ₦8.14 billion in Q1'20 billion (vs. ₦7.68 billion in Q1'19). Consequently, profit after tax rose by 1.55% to ₦50.07 billion (vs. ₦49.30 billion in Q1'19). Impressively, 12-month trailing EPS improved by 4.42% to ₦6.71, from ₦6.43 recorded in the previous period. Based on the recent figure released by the bank, the impact of COVID-19 on the global economy and exposure of GTB to the oil sector, we downgrade our target price to ₦28.24 (Previous target price: ₦33.32) and as a result, we maintain a **BUY** recommendation on the bank's shares at the current price of ₦22.00

Fig. 1: Quarterly results highlights

	1Q2020	4Q2019	1Q2019	4Q2018	Q/q Δ
Net Int. Income (₦mn)	64,282	58,426	58,217	51,792	+3.28%
PBT (₦mn)	58,204	61,056	56,985	51,341	+11.29%
Net profit (₦mn)	50,067	49,876	49,303	42,416	+4.22%

Source: NSE, PAC Research

May 15, 2020

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Price:

- Current	₦22.00
- Target	₦28.24

Recommendation: **BUY**

* As at Thursday May 14, 2020

Fig. 2: Stock data

FYE	December
Price Mov't: YtD / 52wk	-25.93%/-37.23%
52-week range	₦16.70 - ₦34.40
30-day Average vol.	54,558,090
Shares Outstanding ('mn)	29,431.18
Market Cap. (₦bn)	647.49
EPS (₦) - 12months trailing	6.71
DPS (₦) - FY2019	2.80

Source: NSE, Bloomberg, PAC Research

Fig. 3: Key ratios

	Q1'20	Q1'19
Net Interest Margin	9.89%	9.90%
Net profit margin	44.36%	44.69%
Equity multiplier	6.14x	5.67x
Cash/ total Assets	11.89%	23.70%

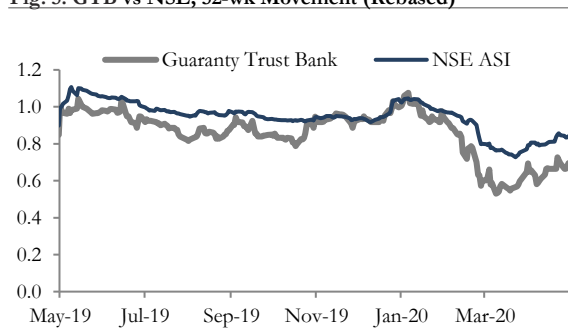
Source: NSE, PAC Research

Fig. 4: Valuation

	FY2018	FY2019	FY2020F	FY2021F
P/E	3.51x	3.29x	3.35x	3.22x
P/B	1.12x	0.94x	0.96x	0.92x
Div Yield (%)	12.50	12.73	12.73	12.95
Payout Ratio	43.83%	41.86%	42.58%	41.68%
Ev/Revenue	0.36x	0.52x	0.52x	0.57x
Rev per share	14.77	14.79	14.35	14.85
ROE	32.08%	28.64%	28.66%	28.65%
ROA	5.62%	5.24%	4.97%	4.99%

Source: NSE, PAC Research

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



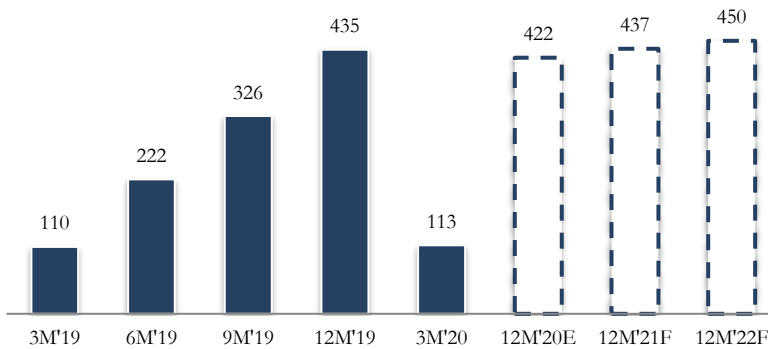
Source: Bloomberg, PAC Research

Gross earnings improves by 2.30% year-on-year, boosts by interest

income: In the first quarter of 2020, Guaranty Trust Bank released impressive figure for top-line as gross earnings increased by 2.30% to ₦112.87 billion (vs ₦110.33 billion in the first quarter of 2019), mainly as a result of impressive interest income line. The bank's interest income increased by 3.43% to ₦77.04 billion in the first quarter of 2020 (vs. ₦74.48 billion in the first quarter of 2019). The impressive figure for interest income during the period can be mainly ascribed to higher income from investment securities and improved interest income from loans and advances. However, during the period, the bank benefited significantly from higher foreign exchange revaluation gain, which offset the lower fee & commission income recorded in the first quarter of 2020 and as a result, non-interest income remains almost flat at ₦35.83 billion in Q1'20 (vs. ₦35.84 billion in Q1'19).

... during the period, the bank benefited significantly from higher foreign exchange revaluation gain, which offset the lower fee & commission income recorded in the first quarter of 2020.

Fig. 6: Gross Earnings – 3M'19 - FY'22F (Billion NGN)



Source: NSE, PAC Research

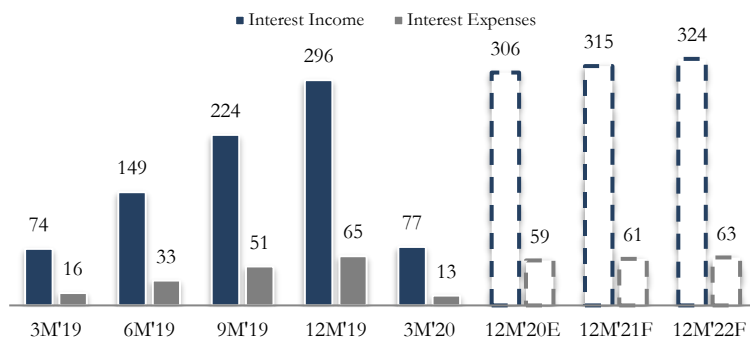
With Higher LDR, interest income rises by 3.43%: In line with our forecast in the last report, the interest income of Guaranty Trust Bank Plc increased by 3.43% to ₦77.04 billion in Q1'20 (vs. ₦74.48 billion in Q1'19). The improvement in interest income can be mainly ascribed to higher interest income from loans & advances and investment securities. In a bid to meet the Loan-to-deposit ratio (LDR) of 65%, as required by the Central Bank of Nigeria (CBN), Guaranty Trust Bank increased its total loans and advances by 26.56% to ₦1.62 trillion in the first quarter of 2020 (vs. ₦1.28 trillion in the first quarter of 2019) and this translated to a net loans-to-deposit ratio of 56.67% (vs. 50.99% in the first quarter of 2019). Consequently, interest income from loans and advances rose by 5.92% to ₦46.41 billion in Q1'20 (vs. ₦43.82 billion in Q1'19). In addition, interest income from investment securities increased by 10.71% to ₦25.41 billion in Q1'20 (vs. ₦22.95 billion in Q1'19).

The improvement in interest income can be mainly ascribed to higher interest income from loans & advances and investment securities.

Interest expenses fell significantly by 21.59% to ₦12.76 billion in the first quarter of 2020 (vs. ₦16.27 billion reported in the first quarter of 2019) and this is in line with our projection for the year 2020.

The lower interest expenses recorded during the period can be mainly attributed to the benefit the bank derived from the lower yield environment as the bank continued to repriced time deposits and sustained low cost deposit mix.

Fig. 7: Int. Income, Int. Expenses and NII: 3M'19 – 12M'22F (Billion NGN)



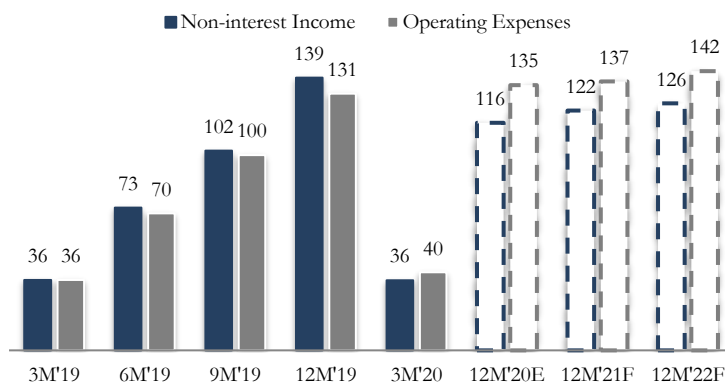
Source: NSE, PAC Research

Improved FX revaluation gain offsets the lower fee and commission income as total non-interest income remains flat: Effective January 1st 2020, the Central Bank of Nigeria reduced bank charges across board and this significantly affected the fee and commission income of GTbank in the first quarter of 2020. Fee and commission income fell significantly by 22.07% to ₦14.46 billion in the first quarter of 2020 (vs. ₦18.56 billion reported in the first quarter of 2019). However, the bank benefitted from the foreign exchange revaluation gain as it increased by 220.30% to ₦8.45 billion in the first quarter of 2020 (vs. ₦2.64 billion in the first quarter of 2019). Consequently, the benefit derived from the foreign exchange revaluation gain offset the lower fee and commission income, hence non-interest income remained relatively flat at ₦35.83 billion in three-month to March 2020 (vs. ₦35.84 billion in three-month to March 2019).

However, the operating expenses of the bank rose by 10.85% to ₦39.77 billion in the first quarter of 2020 (vs. ₦35.88 billion reported in the first quarter of 2019) and this resulted in cost-to-income ratio of 40.59% during the period (Q1'19: 38.64%). Impressively, the increase in operating expenses is far below the inflation rate of 12.26% for the month of March 2020. The growth in OPEX was largely as a result of higher personnel expenses, depreciation & amortisation and other operating expenses. Mainly as a result of higher wages and salaries, personnel expense rose by 1.16% to ₦9.24 billion in the first quarter of 2020 (vs. ₦9.14 billion reported in the first quarter of 2019). Depreciation & amortisation increased significantly by 49.20% to ₦6.85 billion (vs. ₦4.59 billion in Q1'19) while other operating expenses increased by 7.61% to ₦22.95 billion in Q1'19 (vs. ₦21.33 billion in Q1'19), mainly as a result of higher AMCON expenses and higher expenses on advert, promotion and corporate gifts.

Impressively, the increase in operating expenses is far below the inflation rate of 12.26% for the month of March 2020

Fig. 8: Non-Int. Income and Operating Expenses: 3M'19 – 12M'22F (Billion NGN)



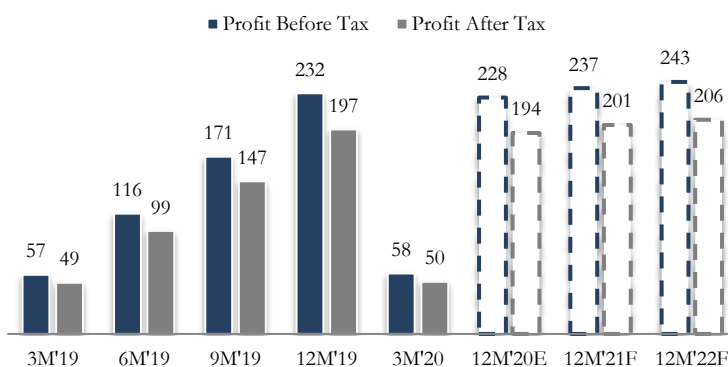
Source: NSE, PAC Research

Even with higher impairment charges, PBT grows by 7.48% year-on-year:

In the first quarter of 2020, the bank's impairment charges increased significantly by 87.84% to at ₦1.22 billion (vs. at ₦0.65 billion reported in the first quarter of 2019) due to higher expected credit loss. As a result of higher interest income, improved FX revaluation gain, and moderate OPEX growth, profit before tax increased by 2.14% to ₦58.20 billion in Q1'20 (vs. ₦56.99 billion reported in Q1'19). However, the bank made a higher provision of ₦8.14 billion for tax during the period (Q1'19: ₦7.68 billion) and as a result, profit after tax improved by 1.55% to ₦50.07 billion in Q1'20 (vs. ₦49.30 billion in Q1'19). Impressively, the performance of the bank reflected on 12-month trailing EPS as it improved by 4.42% to ₦6.71, from ₦6.43 recorded in the previous period.

As a result of higher interest income, improved FX revaluation gain, and moderate OPEX growth, profit before tax increased by 2.14% to ₦58.20 billion in Q1'20

Fig. 9: Profit before Tax and Profit after Tax – 3M'19 – 12M'22F (Billion NGN)



Source: NSE, PAC Research

Balance sheet remains strong as total assets hits ₦4.06 trillion;

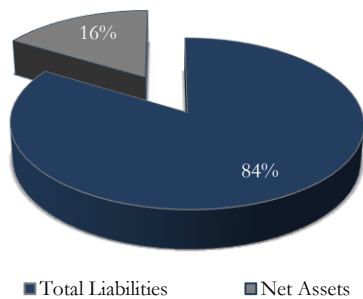
Expectation of impressive dividend yield in 2020: Guaranty Trust Bank Plc continued with strong and solid balance sheet in the first quarter of 2020 as total assets of the bank increased by 14.10% to ₦4.06 trillion (vs. ₦3.56 trillion in the first quarter of 2019).

The impressive growth in the total assets can be attributed to higher loans and advances during the period. In a bid to increase the loan-to-deposit ratio to 65%, as directed by the Central Bank of Nigeria, the bank improves its total loans and advances by 26.56% to ₦1.62 trillion in Q1'20 (vs. ₦1.28 trillion in Q1'19) and this translated to a net LDR of 56.67% (Q1'19: 50.99%). However, total liabilities of the bank increased by 15.96% to ₦3.40 trillion in Q1'20 (vs. ₦2.93 trillion in Q1'19), due to 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 5.40% to ₦661.07 billion in Q1'20 (vs. ₦627.18 billion in Q1'19). This translated to a net asset per share of ₦22.46 in the first quarter of 2020 (vs. ₦21.31 in the first quarter of 2019). The impressive balance sheet reflected on the liquidity ratio and capital adequacy ratio as they are well above the regulatory requirement. Liquidity ratio remained at 45.59% (Q1'19: 47.74%) while capital adequacy ratio (Full IFRS 9 impact) was 23.52% in Q1'20 (Q1'19: 22.25%).

In a bid to increase the loan-to-deposit ratio to 65%, as directed by the Central Bank of Nigeria, the bank improves its total loans and advances by 26.56% to ₦1.62 trillion in Q1'20 (vs. ₦1.28 trillion in Q1'19)...

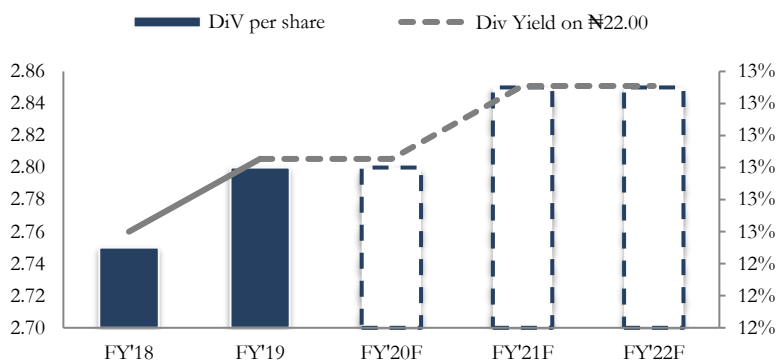
Although, we do not expect improved dividend per share in 2020 as we expect the impact of COVID-19 to affect the performance of the banking industry going forward. However, with the current market price of bank's share, we expect impressive dividend yield in the year 2020.

Fig. 10: Total Liabilities Vs Net Asset in Q1'20



Source: Guaranty Trust Bank Plc, PAC Research

Fig. 11: Dividend Per Share and Dividend Yield (FY'18 - FY'22F)



Source: Guaranty Trust Bank Plc, PAC Research

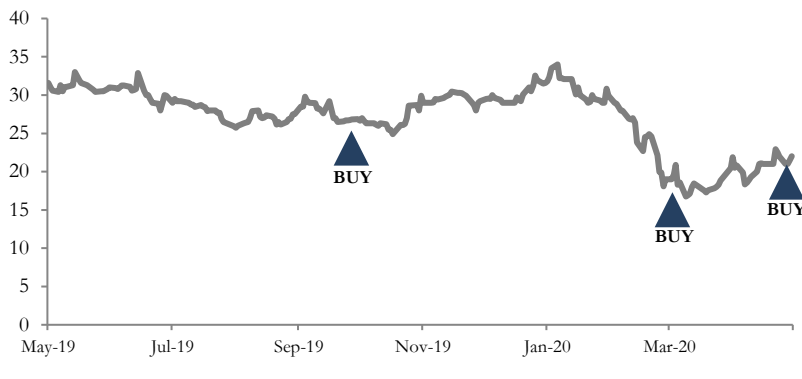
Valuation

Our valuation puts the target price of the stock at ₦28.24, representing an increase of 28.35% from the current price of ₦22.00. In arriving at the target price, we employed Residual Income 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 company, the current figures released by the company, the impacts of COVID-19 on the banking businesses, exposure of the bank to the oil sector and the performance of the bank in the banking industry.

Our valuation puts the target price of the stock at N28.24, representing an increase of 84.06% from the current price of N22.00

Fig. 14: Share Price History (Naira)



Source: NSE, PAC Research

Fig. 15: Statement of Profit or Loss, N'mn

	2018	2019	2020E	2021F
Gross Earnings	434,699	435,307	422,247	437,021
Change		0.14%	-3.00%	3.50%
Interest and Similar Income	306,963	296,205	306,129	314,651
Change		-3.50%	3.35%	2.79%
Interest and Similar Expenses	-84,530	-64,842	-59,115	-61,181
Change		-23.29%	-8.83%	3.50%
Net Interest Income	222,434	231,363	247,015	253,471
Change		4.01%	6.76%	2.62%
Impairment Charge for credit losses	-4,906	-4,912	-8,023	-8,301
Change		0.11%	63.34%	3.50%
Net Fees and Commission Income	50,470	59,444	47,292	49,381
Change		17.78%	-20.44%	4.42%
Trade gains	24,584	20,890	21,112	21,851
Change		-15.03%	1.07%	3.50%
Personnel expenses	-36,856	-37,284	-36,524	-38,021
Change		1.16%	-2.04%	4.10%
Profit Before Taxation	215,587	231,708	227,676	236,731
Change		7.48%	-1.74%	3.98%
Taxation	-30,947	-34,842	-34,151	-35,511
Change		12.59%	-1.98%	3.98%
Profit After Taxation	184,640	196,866	193,524	201,221
Change		6.62%	-1.70%	3.98%

Fig. 16: Statement of Fin. Position, N'mn

	2018	2019	2020E	2021F
Cash and cash equivalents	676,989	593,551	593,551	570,034
Loans and advances	1,262,005	1,502,085	1,635,533	1,692,777
Financial assets held for trading -Available for Sale/fair value thru other compr. Income	11,315	73,486	71,275	73,770
Held to Maturity	98,620	145,561	141,200	146,141
Assets pledged as collateral	56,777	58,037	59,115	61,184
Loans and advances to banks	2,995	1,513	1,436	1,486
Loans and adv. to customers	1,259,010	1,500,572	1,634,097	1,691,291
Property and equipment	111,826	141,775	147,787	152,959
Restr. deposits & other assets	508,679	577,433	591,146	611,836
Total Assets	3,287,343	3,758,919	3,897,174	4,034,100
Deposits from banks	82,803	107,518	105,562	109,257
Deposits from customers	2,273,903	2,532,540	2,702,383	2,796,966
Other liabilities	140,448	233,426	225,902	233,809
Deferred tax liabilities	7,786	10,569	10,556	10,926
Debt securities issued	0	0	0	0
Other borrowed funds	178,567	163,000	152,009	152,959
Total Liabilities	2,711,775	3,071,581	3,221,916	3,331,799
Net Assets	575,567	687,337	675,258	702,301
Total equity and liabilities	3,287,343	3,758,919	3,897,174	4,034,100

Fig. 17: Profitability Ratio

	2018	2019	2020E	2021F
Return on Equity	32.08%	28.64%	28.66%	28.65%
Return on Assets	5.62%	5.24%	4.97%	4.99%
Net interest income to Revenue	51.17%	53.15%	58.50%	58.00%
PBT margin	49.59%	53.23%	53.92%	54.17%
Net Profit Margin	42.48%	45.22%	45.83%	46.04%
ROCE	10.09%	9.72%	8.94%	9.00%

Fig. 18: Asset Utilisation

	2018	2019	2020F	2021F
Cash/Revenue	155.74%	136.35%	135.00%	135.00%
Revenue to total assets (x)	13.22%	11.58%	10.83%	10.83%
Interest Income / Total Assets	9.34%	7.88%	7.86%	7.80%
Loan Loss Exp./Net Int. Income	2.21%	2.12%	3.25%	3.28%
Loan Loss Exp./After Tax Profit	2.66%	2.49%	4.15%	4.13%
fixed asset turnover	0.50%	0.52%	0.55%	0.57%

Fig. 19: Liquidity Ratios

	2018	2019	2020E	2021F
Current ratio	1.21	1.22	1.21	1.21
Cash ratio	0.25	0.19	0.18	0.18
Interest Coverage ratio	2.55	3.57	3.85	3.87
Liquid Assets/Total Deposit	24.10	20.03	21.45	21.45
Loans & Advances/Total Deposit	6.51	5.75	6.00	6.00
Liquid Assets/Total Assets	0.61	0.57	0.58	0.58
Debt/net income	0.97	0.83	0.79	0.76
Debt to asset	0.05	0.04	0.04	0.04
Debt to equity	0.31	0.24	0.23	0.22
Total Liabilities / Total Asset	0.82	0.82	0.83	0.83
Cost to income ratio net interest margin AVERAGED	0.26	0.27	0.29	0.29
Total liabilities/equities	4.71	4.47	4.77	4.74

Fig. 20: Shareholders' Investment Ratios

	2018	2019	2020E	2021F
Earnings per share	6.27	6.69	6.58	6.84
DiV per share	2.75	2.80	2.80	2.85
NAVPS	19.56	23.35	22.94	23.86
Earnings yield	30.40%	30.40%	29.89%	31.08%

Fig. 21: Capital Adequacy Ratios

	2018	2019	2020E	2021F
Loans and Advances/Equity	2.19	2.19	2.42	2.41
Equity/Total Assets	0.18	0.18	0.17	0.17
Loan Loss Expense/ Equity	0.009	0.007	0.012	0.012

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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