Guaranty Trust Bank Plc

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Nigeria | Equities | Financial Services | May 6, 2021 — PAC RESEARCH

Slow Start to the Year due to Setback in Interest Income Line

INVESTMENT SUMMARY

Most investors were initially upbeat as they anticipated improved performance from Guaranty Trust Bank in Q1, 2021 on expanded economic activities in the country during the quarter. However, the bank recorded a slow start in the first quarter of 2021 despite impressive performance during the pandemic year 2020. The commercial lender's gross earnings fell by 5.94% to ₦106.17 billion in the first quarter (vs. ₦112.87 billion in first quarter of 2020). The reduction in the gross earnings could be attributed to the setback recorded in total interest income, which declined significantly by 21.71% to ₦60.31 billion in Q1'21 (₦77.04 billion in Q1'20). On the other hand, the total non-interest income of the bank improved significantly by 27.99% to ₦45.86 billion in Q1'21 (vs. ₦35.83 billion in Q1'20), due improved fee & commission income and discounts & recoverables. Impressively, the total interest expense fell by 38.27% to ₦7.87 billion in Q1'21 (vs. ₦12.76 billion in Q1'20), and this may be attributed to the lower cost-of-fund during the period. In addition, the total operating expenses declined marginally to ₦39.38 billion in Q1'21, when compared with ₦39.77 billion reported in Q1'20. In line with our forecast, the loan impairment charge rose by 52.05% to ₦1.86 billion in Q1'21 (Q1'20: ₦1.22 billion), due to the heightened probability of default, triggered by the impact of COVID-19 on macroeconomic variables.

Weak performance in the interest income line saw the profit before tax declining by 7.77% to ₦53.68 billion in Q1'21 (vs. ₦58.20 billion in Q1'20). The bank made a provision of ₦8.14 billion for tax in Q1'21 billion (Q1'20: ₦8.14 billion). Consequently, profit after tax fell by 9.03% to ₦45.55 billion (vs. ₦50.07 billion in Q1'20) and this translated to 12-month trailing EPS of ₦6.69 (Q1'20: ₦6.71). Based on Q1'21 figures and prospect of improved performance in the coming quarters, we maintain a **BUY** rating on the stock at the current price of ₦29.00 as present forward estimate places the company share price at ₦38.19 (Previous target price: ₦38.31).

Fig. 1: Quarterly results highlights

	1Q2021	4Q2020	1Q2020	Q/q Δ	Y/y Δ
Net Int. Income (₦'mn)	52,434	63,932	64,282	-17.98%	-17.98%
PBT (₦'mn)	53,683	70,743	58,204	-24.12%	-7.77%
Net profit (₦'mn)	45,546	59,157	50,067	-23.01%	-9.03%

Source: NSE, PAC Research

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Price:	
- Current	**₦29.00**
- Target	**₦38.19**
Recommendation:	**BUY**

** As at Wednesday May 5, 2021*

Fig. 2: Stock data

FYE	December
Price Mov't: YtD / 52wk	-10.36%/+38.10%
52-week range	₦20.60 - ₦38.45
30-day Average vol.	27,289,190
Shares Outstanding ('mn)	29,431.18
Market Cap. (₦bn)	853.50
EPS (₦) - 12months trailing	6.69
DPS (₦) - FY2020	3.00

Source: NSE, Bloomberg, PAC Research

Fig. 3: Key ratios

	Q1'21	Q1'20
Net Interest Margin	6.96%	9.89%
Net profit margin	42.90%	44.36%
Equity multiplier	5.96x	6.07x
Cash/ total Assets	14.21%	15.08%

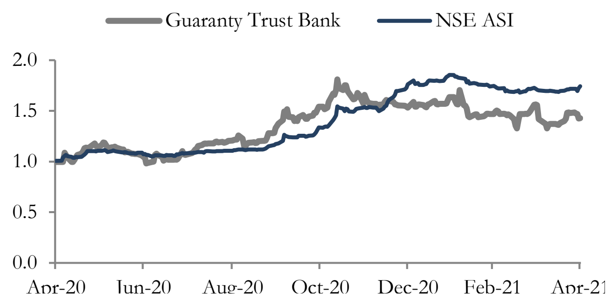
Source: NSE, PAC Research

Fig. 4: Valuation

	FY2019	FY2020	FY2021F	FY2022F
P/E	4.34x	4.24x	4.18x	3.99x
P/B	1.24x	1.05x	1.02x	0.95x
Div Yield (%)	9.66	10.34	10.34	11.03
Payout Ratio	41.86%	43.83%	43.23%	43.98%
Ev/Revenue	1.00x	0.54x	0.51x	0.47x
Rev per share	14.79	15.47	15.70	16.09
ROE	28.64%	24.73%	24.38%	23.92%
ROA	5.24%	4.07%	4.03%	4.12%

Source: NSE, PAC Research

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



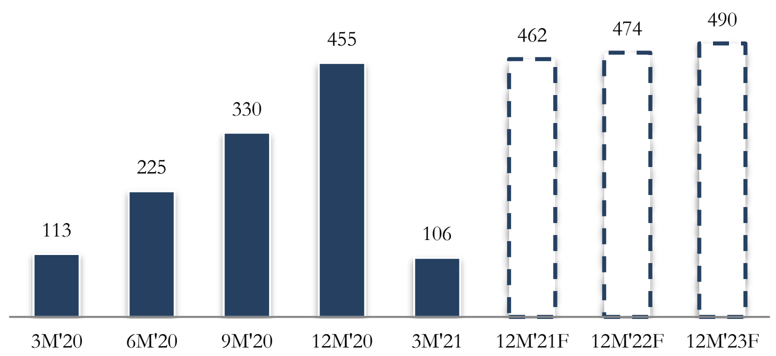
Source: Bloomberg, PAC Research

Gross earnings falls by 5.94% year-on-year, due to the setback in interest income: In the first quarter of 2021, Guaranty Trust Bank reported a lower figure for the top line as gross earnings fell by 5.94% to ₦106.17 billion (vs ₦112.87 billion recorded in the first quarter of 2020), mainly because of notable setback in the interest income line of the bank. The interest income of the bank fell significantly by 21.71% to ₦60.31 billion in first quarter of 2021 (vs. ₦77.04 billion in first quarter of 2020). However, the bank recorded significant improvement in the non-interest income line as it improved significantly by 27.99% to ₦45.86 billion in Q1'21 (vs. ₦35.83 billion recorded in Q1'20), due to significant improvement in fee & commission income lines and higher discounts & recoverables from foreign exchange.

…bank recorded significant improvement in non-interest income line as it improved significantly by 27.99% to ₦54.86 billion in Q1'21…

In terms of contribution to the gross earnings in the first quarter of 2021, the share of total non-interest income improved to 43.19% (vs. 31.74% in first quarter of 2020) while the share of total interest income declined to 56.81% (vs. 68.26% in first quarter of 2020). Going forward, we expect the contribution of interest income line to gross earnings to increase as we expect the recent rise in yields to have significant impact on interest income from investment securities.

Fig. 6: Grosss Earnings – 3M'20 – 12M'23F (Billion NGN)



Source: NSE, PAC Research

Interest income improves by 21.71% year-on-year, due to lower yield on earning assets: Despite the higher loans and advances recorded in the first quarter of 2021, the interest income of the bank decline significantly by 21.71% to ₦60.31 billion (vs. ₦77.04 billion in first quarter of 2020). The decline in interest income line could be attributed to the reduction in interest income from loans and advances and interest income from investment securities. Mainly as a result of lower yields in first quarter of 2021, the interest income from loans & advances and interest income from investment securities fell by 4.50% and 67.33% to ₦44.32 billion (Q1'20: ₦46.41 billion) and ₦8.30 billion (Q1'20: ₦25.41 billion) respectively. With improvement in the yields in recent times, we may likely see an improvement in interest income of the bank in coming quarters.

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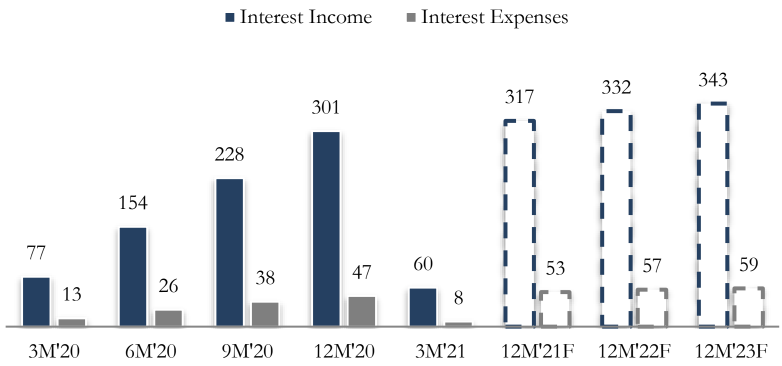
Impressively, the interest expenses of the bank fell significantly by 38.27% to ₦7.87 billion in first quarter of 2021 (vs. ₦12.76 billion in first quarter of 2020), which may be partially attributed to the revision of savings rate from 30% to 10% of Monetary Policy Rate (MPR). Again, we may likely see upward repricing of rates in the banking sector, due to the recent rise in yields across the board, which may translate to higher interest expenses in coming quarters.

Fig. 7: Interest Income and Interest Expenses: 3M'20 – 12M'23F (Billion NGN)



Source: NSE, PAC Research

Non-interest income rises by 27.99% year-on-year, driven by higher fee and commission income and other income: The lockdown of economic activities and restriction of movement in 2020 has improved the traffic of on-line banking service and this had significant impact on the fee and commission income of the bank in first quarter of 2021, as it increased by 21.51% to ₦17.57 billion (vs. ₦14.46 billion in first quarter of 2020). Specifically, the increase in fee and commission income was attributed to higher E-business income, account maintenance charges, transfer related charges, among others. In addition, discounts & recoveries (FX) and foreign exchange trading gain improved by 66.19% and 168.79% to ₦7.47 billion (Q1'20: ₦4.49 billion) and ₦12.60 billion (Q1'20: ₦4.69 billion) respectively in Q1'21, due to improved activities in FX market. Consequently, the non-interest income of the bank improved significantly by 27.99% to ₦45.86 billion in first quarter of 2021 (vs. ₦35.83 billion reported in first quarter of 2020).

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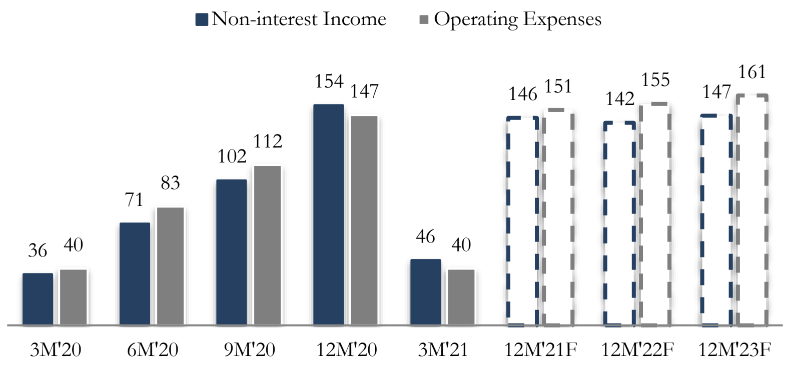
The banks maintained its cost minimisation strategy during the period as operating expenses remained flat at ₦39.78 billion (vs. ₦39.77 billion reported in first quarter of 2020) and this resulted to a cost-to-income ratio of 42.56% in Q1'21 (Q1'20: 40.59%). The zero percent growth in OPEX is way below the inflation rate of 18.17% for the month of March and this showed the bank's desire to consistently improve its cost minimisation strategy.

Fig. 8: Non-Int. Income and Operating Expenses: 3M'20 – 12M'23F (Billion NGN)



Source: NSE, PAC Research

In addition to lower interest income, loan impairment charges rises by 52.05% as PBT falls by ₦4.52 billion year-on-year: In line with our projection, the loan impairment charges of the bank increased significantly by 52.05% to ₦1.86 billion in first quarter of 2021 (vs. ₦1.22 billion in first quarter of 2020). The increase in loan impairment charge could be attributed to the heightened probability of loan default due to the impact of COVID-19 on macroeconomic variables which resulted in worsening forward-looking information which primarily drives IFRS 9 impairment numbers.

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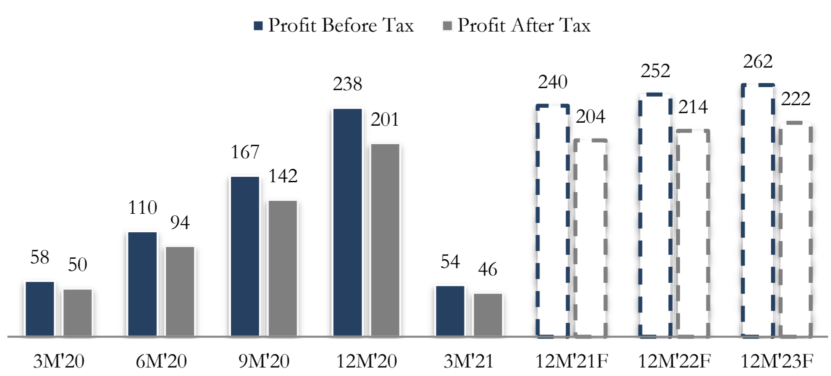
The setback in loan impairment charges and interest income line outweighed the improved figure recorded in non-interest income as profit before tax fell by 7.77% to ₦53.68 billion in Q1'21 (vs. ₦58.20 billion reported in Q1'20). The bank made a provision of ₦8.14 billion for tax during the period (Q1'20: ₦8.14 billion). Consequently, profit after tax declined by 9.03% to ₦45.55 billion in Q1'21 (vs. ₦50.07 billion in Q1'20) and this translated to trailing earnings per share (EPS) of ₦6.69 (vs. ₦6.71 recorded in previous period).

Fig. 9: Profit before Tax and Profit after Tax – 3M'20 – 12M'23F (Billion NGN)



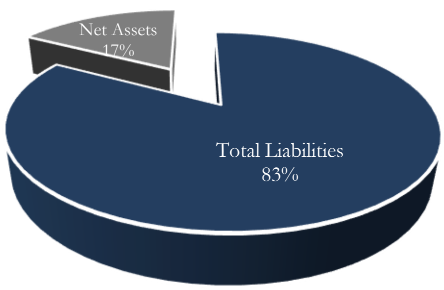
Source: NSE, PAC Research

Balance sheet remains strong and solid as total assets hits ₦5 trillion; Expectation of impressive dividend in 2021: Guaranty Trust Bank Plc continued with strong and solid balance sheet in the first quarter of 2021 as total assets of the bank increased marginally by 0.97% to ₦4.99 trillion (vs. ₦4.94 trillion in the first quarter of 2020). The marginal growth in the total assets could be attributed to improved loans & advances and higher restricted deposits & other assets during the period. The bank improves its total loans and advances by 1.03% to ₦1.64 trillion in Q1'21 (vs. ₦1.62 trillion in Q1'20) and this translated to a net loans-to-deposits ratio of 44.08% (Q1'20: 46.05%). However, the total liabilities of the bank increased marginally by 0.61% to ₦4.16 trillion in Q1'21 (vs. ₦4.13 trillion in Q1'20), due to higher deposits during the period.

Liquidity ratio increased to 42.04% (Q1'20: 38.91%) while capital adequacy ratio (Full IFRS 9 impact) improved to 26.12% in Q1'2…

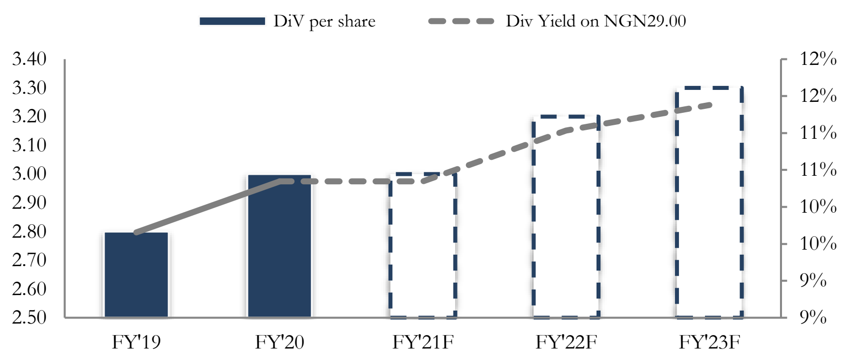
The improvement in the total assets of the bank outweighed the increase in total liabilities and as a result, the net assets of the bank increased by 2.80% to ₦837.24 billion in Q1'21 (vs. ₦814.40 billion in Q1'20). This translated to a net asset per share of ₦28.45 in the first quarter of 2021 (vs. ₦27.67 in the first quarter of 2020). The impressive balance sheet reflected on the liquidity ratio and capital adequacy ratio as they are well above the regulatory requirement. Liquidity ratio increased to 42.04% (Q1'20: 38.91%) while capital adequacy ratio (Full IFRS 9 impact) improved to 26.12% in Q1'21 (Q1'20: 25.90%). With the strong balance sheet and assumption of improved performance in the coming quarters, we expect the bank to, at least, match the previous total dividend in full year 2021.

Fig. 10: Total Liabilities Vs Net Asset in Q1'21



Source: Guaranty Trust Bank Plc, PAC Research

Fig. 11: 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 ₦38.19, representing an increase of 31.69% from the current price of ₦29.00. 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.

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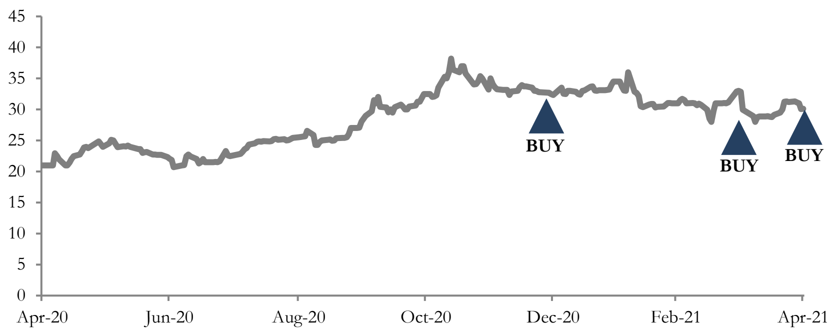
Our valuation and forecasts considered several factors (both quantitative and qualitative) among which are; the previous financial reports of the bank, the current figures released by the bank, the performance of the bank in the banking industry and the outlook of Management of the banks.

Fig. 12: Share Price History (Naira)



Source: NSE, PAC Research

Fig. 13: Statement of Profit or Loss, N'mn

	2019	2020	2021F	2022F
Gross Earnings	435,307	455,230	462,058	473,610
Change		4.72%	6.15%	2.50%
Interest and Similar Income	296,205	300,738	316,510	331,527
Change		-2.03%	6.86%	4.74%
Interest and Similar Expenses	-64,842	-47,069	-53,137	-56,833
Change		-44.32%	-18.05%	6.96%
Net Interest Income	231,363	253,668	263,373	274,694
Change		14.04%	13.84%	4.30%
Impairment Charge for credit losses	-4,912	-19,573	-20,793	-19,892
Change		298.92%	323.33%	-4.33%
Net Fees and Commission Income	59,444	46,935	54,061	55,412
Change		-7.00%	-9.06%	2.50%
Trade gains	20,890	24,486	26,799	27,469
Change		-0.40%	28.29%	2.50%
Personnel expenses	-37,284	-37,606	-39,275	-40,257
Change		2.03%	5.34%	2.50%
Profit Before Taxation	231,708	238,095	240,270	251,960
Change		10.44%	3.70%	4.87%
Taxation	-34,842	-36,655	-36,041	-37,794
Change		18.44%	3.44%	4.87%
Profit After Taxation	196,866	201,440	204,230	214,166
Change		9.10%	3.74%	4.87%

Fig. 14: Statement of Fin. Position, N'mn

	2019	2020	2021F	2022F
Cash and cash equivalents	593,551	627,224	593,551	748,534
Loans and advances	1,502,085	1,662,831	1,758,131	1,802,085
Financial assets held for trading	73,486	67,535	69,309	71,041
-Available for Sale/fair value tru other compr. Income	618,477	696,645	716,190	734,095
Held to Maturity	145,561	283,583	207,926	213,124
Assets pledged as collateral	58,037	62,200	64,688	66,305
Loans and advances to banks	1,513	99	2,310	2,368
Loans and adv. to customers	1,500,572	1,662,732	1,755,821	1,799,717
Property and equipment	141,775	148,783	161,720	165,763
Restr. deposits & other assets	577,433	1,226,481	1,293,763	1,326,107
Total Assets	3,758,919	4,944,653	5,072,475	5,199,855
Deposits from banks	107,518	101,510	101,653	104,194
Deposits from customers	2,532,540	3,509,319	3,696,466	3,750,989
Other liabilities	233,426	356,223	277,235	284,166
Deferred tax labilities	10,569	24,961	25,413	26,049
Debt securities issued	0	0	0	0
Other borrowed funds	163,000	113,895	106,273	108,930
Total Liabilities	3,071,581	4,130,258	4,234,948	4,304,543
Net Assets	687,337	814,396	837,527	895,312
Total equity and liabilities	3,758,919	4,944,653	5,072,475	5,199,855

Fig. 15: Profitability Ratio

	2019	2020	2021F	2022F
Return on Equity	28.64%	24.73%	24.38%	23.92%
Return on Assets	5.24%	4.07%	4.03%	4.12%
Net interest income to Revenue	53.15%	55.72%	57.00%	58.00%
PBT margin	53.23%	52.30%	52.00%	53.20%
Net Profit Margin	45.22%	44.25%	44.20%	45.22%
ROCE	9.72%	7.18%	7.07%	7.39%

Fig. 16: Asset Utilisation

	2019	2020	2021F	2022F
Cash/Revenue	136.35%	163.78%	162.00%	162.00'
Revenue to total assets (x)	11.58%	9.21%	9.11%	9.11%
Interest Income / Total Assets	7.88%	6.08%	6.24%	6.38%
Loan Loss Exp./Net Int. Income	2.12%	7.72%	7.89%	7.24%
Loan Loss Exp./After Tax Profit	2.49%	9.72%	10.18%	9.29%
fixed asset turnover	0.52%	1.04%	0.55%	0.57%

Fig. 17: Liquidity Ratios

	2019	2020	2021F	2022F
Current ratio	1.22	1.20	1.20	1.21
Cash ratio	0.19	0.18	0.18	0.18
Interest Coverage ratio	3.57	5.06	4.52	4.43
Liquid Assets/Total Deposit	20.03	24.34	25.30	25.30
Loans &Advances/Total Deposit	5.75	6.86	7.05	7.05
Liquid Assets/Total Assets	0.57	0.50	0.51	0.51
Debt/net income	0.83	0.57	0.52	0.51
Debt to asset	0.04	0.02	0.02	0.02
Debt to equity	0.24	0.14	0.13	0.12
Total Liabilities / Total Asset	0.82	0.84	0.83	0.83
Cost to income ratio	0.27	0.33	0.32	0.32
net interest margin AVERAGED	0.10	0.07	0.08	0.09
Total liabilities/equities	4.47	5.07	5.06	4.81

Fig. 18: Shareholders' Investment Ratios

	2019	2020	2021F	2022F
Earnings per share	6.69	6.84	6.94	7.28
DiV per share	2.80	3.00	3.00	3.20
NAVPS	23.35	27.67	28.46	30.42
Earnings yield	22.22%	22.74%	23.05%	24.18%

Fig. 19: Capital Adequacy Ratios

	2019	2020	2021F	2022F
Loans and Advances/Equity	6.69	6.84	6.94	7.28
Equity/Total Assets	2.80	3.00	3.00	3.20
Loan Loss Expense/ Equity	23.35	27.67	28.46	30.42

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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