Guaranty Trust Bank Plc.

First Glance: Improved NIR, contraction in impairment loss boost Q2 earnings.

Update: GUARANTY released its Q2 2018 result yesterday, showing growth in EPS by 20.63% y/y and 13.97% q/q, to NGN1.73. Annualized, the H1-2018 EPS beats Bloomberg's polled estimate of NGN5.91 for FY-2018 by 10%. Impressive growth in the NIR (+31.95% y/y, +30.53% q/q) salvaged the top line performance, as it outweighed the continued decline in the interest income. At the bottom line, reduction in the provision for impairment (-89.67% y/y, -76.06% q/q), as well as a close to flattish opex (+1.72% y/y, +11.55% q/q) growth, gave a boost to the bank's earnings.

Compressed asset yield, and increased CoF, translate to poor performing NIM: Interest income in Q2 (-0.82% q/q, +0.41%) remained suppressed by the lower interest rate environment in the quarter, as well as the continued contraction in the loan book (-13.25% y/y, -10.77% ytd), while interest expense (+24.50% y/y, +8.46% q/q) was higher, following increased interest on customer deposits (+38.43% y/y, +3.13% q/q), amidst growth in total deposits (+2.48% q/q, +10.02% y/y) during the period. As a result, NII (-8.15% y/y, -2.43% q/q) was lower. On our estimates, the annualized asset yield in H1 was lower by 100 bps at 12.5% (vs. FY 2017's 13.50%), while annualized CoF was flat YtD, at 3.3%, resulting in NIM compression (YtD: -107 bps) to 9.09%.

Impressive NIR in Q2: NIR sustained its growth sustained during the quarter, driven by improved performance on the net trading income (+499.31% y/y, +45.68% q/q), other income (+0.12% y/y, +116.44%), as well as fees and commission income (+20.90% y/y, -20.31% q/q) lines. A surge in foreign exchange gain to NGN6.0 billion, from a loss of NGN21.18 million in Q2 last year, led to the growth in net trading income, while the upturn in other income was attributable to a jump in dividend income from NGN107 million in Q2-2017, to NGN2.68 billion in the current quarter. While fees & commission income impressed on a year-on year basis (+20.90%), it dropped by 20.31% q/q. The y/y growth was as a result of the increases in E-business income (+21%) and Commission on foreign exchange deals (+397.97%).

Improvement in asset quality: GUARANTY's annualized CoR in H1 improved by 65 bps YtD to 0.11%, amidst decline in impairment provision (-71.83% y/y) in the half year, as well as the continued contraction in the loan book (-13.25% y/y, -10.77% YtD).

Further decline CAR: GUARANTY's CAR dropped to 21.89% in H1-18, from 24.57% in Q1-18 and 25.50% in FY-17, following increased deduction for IFRS 9 initial adjustment (unlike in ZENITH's case, which was a reduction) to NGN148.63 billion, as against NGN134.88 billion reported in Q1-18. We also link a deduction of NGN185.79 million from the retained earnings, for remeasurements of post-employment benefit obligations, as possibly exerting further strain on the bank's CAR.

Comment: Overall, we have a positive view of GUARANTY's Q2-18 performance. Together with the higher declared dividend of 30 kobo (2016: 25 kobo) – yielding 0.77% on yesterday's closing price – we expect the bank's stock will attract investor interest in today's trading session.

Company Data	
NSE Code	GUARANTY
Bloomberg Code	GUARANTY:NL
Reuters Code	GUARANT.LG
Sector	FINANCIAL SERVICES
Market Cap. (NGN' bn)	1,147
Free Float (%)	99.76

Ratios	H1-2018	H1-2017	2017FY
Assets Yield	12.47%	12.60%	13.72%
Cost of Funds	3.3%	-3.29%	-3.28%
Net Interest Margin	9.1%	9.52%	10.34%
Cost of Risk	0.3%	0.74%	0.85%
Cost to Income	38..39%	38.46%	38.66%
CAR	21.9%	24.57%	25.68%

Price movement (GUARANTY vs. Benchmark Indices)

Source: NSE, Bloomberg, Cordros Research

Summary of Results.

Highlight (N'Mn)	H1'2018	H1'2017	y/y	Q2'2018	Q1'2018	Q2'2017	q/q
Gross earnings	226,632	214,098	5.85%	117,662	108,970	109,967	7.98%
Interest income	161,881	165,885	-2.41%	81,108	80,773	81,776	0.41%
Interest expense	-43,951	-36,347	20.92%	-22,867	-21,084	-18,367	8.46%
Net interest income	117,930	129,538	-8.96%	58,241	59,689	63,409	-2.43%
Fee and commission income	27,356	23,715	15.35%	12,132	15,224	10,035	-20.31%
fee and commission expense	-1,447	-966	49.81%	-710	-737	-380	-3.66%
Net fee and commission income	25,910	22,749	13.89%	11,422	14,487	9,655	-21.16%
Net gains/(losses) on financial instruments	12,650	5,664	123.33%	7,497	5,153	1,251	45.48%
Other income	24,745	18,834	31.39%	16,925	7,820	16,906	116.44%
Non-interest income	63,305	46,601	35.84%	35,844	27,461	27,165	30.53%
Total Operating Income	181,234	176,139	2.89%	94,085	87,149	90,574	7.96%
Loan impairment charges	-2,032	-7,213	-71.83%	-392	-1,639	-3,801	-76.06%
Total Operating Expenses	-69,570	-67,825	2.57%	-36,684	-32,886	-36,063	11.55%
Profit before Income tax	109,633	101,101	8.44%	57,008	52,624	50,710	8.33%
Income tax expense	-14,051	-17,421	-19.34%	-6,097	-7,954	-8,506	-23.35%
Profit after Tax	95,582	83,680	14.22%	50,912	44,670	42,204	13.97%

Source: Company Accounts, Cordros Research estimates

Disclosures.

Analyst:

Janet Ogunkoya (*janet.ogunkoya@cordros.com)*

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