

DYER & BLAIR INVESTMENT BANK

EARNINGS UPDATE

Founder Member of the Nairobi Securities Exchange

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DYER & BLAIR
INVESTMENT BANK

WE KNOW. YOU KNOW.

NIC GROUP PLC: 1H18 EARNINGS UPDATE

Dear All,

NIC Group PLC released their 1H18 results recording a 2.1% y-o-y decline in profit after tax to KES 2.0 BN. EPS for the period stands at KES 3.10. Trailing EPS stands at KES 6.41, down 1.6% y-o-y. Annualized ROA and ROE multiples dropped 17 and 53 bps y-o-y to 2.0% and 12.3% respectively.

Below please find key highlights:

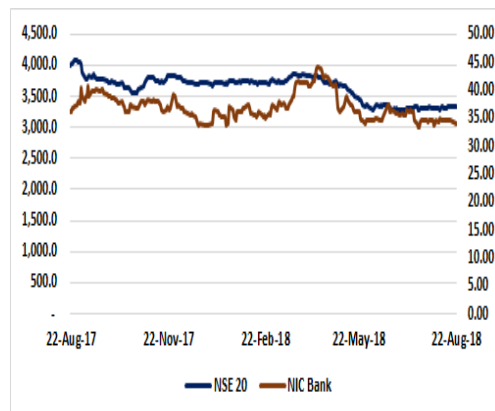
Net interest income declined 4.9% y-o-y to KES 5.1 BN on the back of an 8.6% y-o-y rise in interest income to KES 9.6 BN and a 30.0% y-o-y increase in interest expense to KES 4.4 BN. Annualized yield on interest earning assets rose 38 bps y-o-y to 10.7% whereas annualized cost of funds rose 96 bps y-o-y to 5.4%. As a result, annualized net interest margin declined 58 bps y-o-y to 5.3%.

Interest income from loans and advances declined 6.5% y-o-y to KES 6.2 BN (+4.4% q-o-q) placing the annualized yield on average loans at 10.7% (down 90 bps y-o-y). Interest income from government securities rose 52.8% y-o-y to KES 3.3 BN placing the annualized yield on government securities at 13.1%, up 150 bps y-o-y.

Interest expense from customer deposits rose 37.7% y-o-y to KES 3.7 BN placing the annualized cost of average deposits at 5.3%, up 90 bps y-o-y.

Non-funded income grew 7.0% y-o-y to KES 2.2 BN. This followed a 16.9% y-o-y growth in forex income to KES 683.0 MN. Fees and commissions income declined 3.0% y-o-y to KES 1.1 BN whereas other income rose 24.1% y-o-y to KES 385.6 MN. Fees and commissions on loans declined 13.6% y-o-y to KES 585.5 MN whereas other fees and commissions rose 13.5% y-o-y to KES 495.8 MN. Overall, funded income reliance dropped 240 bps y-o-y to 70.5%.

NIC BANK: 52 WEEK PRICE PERFORMANCE



(Source: NSE, DBIB Research)

PRICE	ABSOLUTE	EXCESS
RETURN	RETURN	RETURN
3 months (%)	(2.2)	(0.3)
6 months (%)	(3.5)	6.3
12 months(%)	(5.6)	11.1

KEY METRICS

Current Price (KES)	34.00
52 week Range (KES)	33.25-44.00
YTD Return (%)	0.74
Issued Shares (Mn)	639.95
Market Cap (USD Mn)	215.73

Recommendation	HOLD
Trailing EPS (KES)	6.41
NAV (KES)	50.35
P/E (x)	5.3
P/B (x)	0.7
Div Yld (%)	-

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Operating expenses (less loan loss provisions) rose 9.1% y-o-y to KES 3.3 BN on the back of a 7.7% y-o-y growth of staff costs to KES 1.7 BN and a 15.9% y-o-y growth in other operating expenses to KES 1.1 BN. As a result, the cost to income (CTI) ratio grew 452 bps y-o-y to 45.6%.

Total assets increased 6.0% y-o-y (+0.6% q-o-q) to KES 200.9 BN. The loan book contracted 1.6% y-o-y to KES 114.9 BN. Investment securities rose 25.7% y-o-y (1.8% q-o-q) to KES 55.7 BN.

Customer deposits rose 10.5% y-o-y to KES 147.1 BN whereas borrowed funds declined 16.8% y-o-y to KES 15.8 BN. Following the decline in loans vis-à-vis the funding base, loans to deposits and loans to deposits and borrowed funds ratios declined 957 bps and 620 bps y-o-y to 78.1% and 70.6% respectively.

Gross non-performing loans rose 12.7% y-o-y to KES 16.2 BN (+1.4% q-o-q) whereas interest in suspense declined 4.9% y-o-y to KES 1.6 BN (+4.0% q-o-q). As a result, total NPL rose 15.0% y-o-y to KES 14.6 BN. Loan loss provision rose 33.0% y-o-y to KES 6.8 BN. Consequently, net NPLs rose 2.8% y-o-y to KES 7.7 BN. The NPL ratio rose 123 bps y-o-y to 12.3% whereas the NPL coverage ratio rose 633 bps y-o-y to 46.9%.

Capital adequacy: NIC Bank Kenya's Core capital to total risk weighted assets (TRWA) declined 112 bps y-o-y to 15.2% while its total capital to TRWA ratio shed 232 bps y-o-y to 18.0%. Both ratios remain above the statutory minimums of 10.5% and 14.5% respectively. Liquidity ratio rose 310 bps y-o-y to 48.8% above the statutory minimum of 20.0%. Adjusted core and total capital ratios stood at 16.42% and 19.20% respectively.

Going forward: We believe that the deposit mix is less than ideal given the increase we continue to observe in the cost of funds this year. As at FY17, 56.0% of customer deposits were term deposits. We are also concerned with the consistent growth in NPLs and the delay in recovery of already non-performing loans. We will be engaging the management in the coming days to understand what their expectations are on these and other items.

On a trailing basis: NIC is trading at a **P/E** ratio of **5.3x** and a **P/B** ratio of **0.7x** below peer median **P/E** and **P/B** ratios of **8.4x** and **1.1x** respectively. However, its ROE and ROA multiples stand at 12.3% and 2.0% below peer median multiples of 14.5% and 2.3% respectively. We maintain our **HOLD** recommendation as we await a decision on whether the caps will be repealed because without that, the latent value reflected in the price multiples may not be realized given the relatively lower returns.

PROFIT AND LOSS SUMMARY (KES MN)

Year End: December	1H18	1H17	y-y% ch	2Q18	1Q18	2Q17	y-y% ch	q-q% ch
Interest income	9,569	8,811	8.6	4,905	4,664	4,499	9.0	5.2
Interest expense	(4,436)	(3,413)	30.0	(2,255)	(2,181)	(1,807)	24.8	3.4
Net interest income	5,133	5,399	(4.9)	2,650	2,483	2,692	(1.6)	6.7
Other operating income	386	311	24.1	207	179	177	17.3	15.9
Fees and commission income	1,081	1,114	(3.0)	517	564	560	(7.6)	(8.3)
Net income from forex dealings	683	584	16.9	383	300	283	35.1	27.5
Total non-interest income	2,150	2,009	7.0	1,107	1,043	1,020	8.5	6.1
Total income	7,283	7,408	(1.7)	3,757	3,527	3,712	1.2	6.5
Less operating expenses	(3,322)	(3,044)	9.1	(1,737)	(1,585)	(1,592)	9.1	9.6
Operating profit	3,962	4,364	(9.2)	2,020	1,942	2,120	(4.7)	4.0
Bad debt charge	(1,114)	(1,446)	(23.0)	(559)	(555)	(570)	(2.0)	0.8
Exceptional items	-	-	-	-	-	-	-	-
Profit before tax	2,848	2,918	(2.4)	1,461	1,387	1,550	(5.7)	5.3
Less tax	(861)	(889)	(3.1)	(447)	(414)	(472)	(5.3)	8.1
Profit after tax	1,987	2,030	(2.1)	1,014	973	1,078	(5.9)	4.2
Non controlling interest	-	-	-	-	-	-	-	-
Attributable Income	1,987	2,030	(2.1)	1,014	973	1,078	(5.9)	4.2
EPS (KES)	3.10	3.17	(2.1)	2	1.52	1.68	(5.9)	4.2

(Source: Company, DBIB Research)

BALANCE SHEET SUMMARY (KES MN)

Year End: December	1H18	1Q18	1H17	y-y% ch	q-q% ch
Total shareholder's equity	31,772	31,553	32,053	(0.9)	0.7
Minority interest	447	514	514	(13.0)	(13.0)
Total Equity	32,220	32,067	32,567	(1.1)	0.5
Deposits due to other banks	2,297	3,729	2,589	(11.3)	(38.4)
Customer deposits	147,088	143,932	133,159	10.5	2.2
Borrowed funds	15,777	16,746	18,968	(16.8)	(5.8)
Other liabilities	3,499	3,133	2,170	61.2	11.7
Total equity and liabilities	200,951	199,786	189,490	6.0	0.6
Central bank balances	9,606	8,857	8,554	12.3	8.5
Deposits due from banks	8,830	8,835	10,248	(13.8)	(0.1)
Investment Securities	55,737	54,746	44,329	25.7	1.8
Customer loans and advances	114,915	115,915	116,770	(1.6)	(0.9)
Other assets	2,148	1,726	1,660	29.4	24.5
Intangible assets	1,667	1,659	1,086	53.5	0.5
Fixed assets	1,095	1,385	1,025	6.8	(21.0)
Total assets	200,951	199,786	189,490	6.0	0.6

(Source: Company, DBIB Research)

INVESTMENT RETURN

	1H18	1Q18	1H17	y-y bps ch	q-q bps ch
ROA (%)*	2.0	1.9	2.1	(17)	3
ROIC (%)*	2.0	2.0	2.2	(17)	1
ROE (%)*	12.3	12.1	12.9	(53)	19

(Source: Company, DBIB Research)

*Annualized

CAPITAL ADEQUACY, LIQUIDITY & ASSET QUALITY

	1Q18	1Q17	4Q17	y-y bps ch	q-q bps ch
Core capital/TRWA (%)	18.2	17.9	19.2	31	(95)
Min. Statutory Ratio (%)	10.5	10.5	10.5	-	-
Total capital/TRWA (%)	20.8	21.9	22.3	(106)	(143)
Min. Statutory Ratio (%)	14.5	14.5	14.5	-	-
Liquidity Ratio (%)	48.2	39.0	48.2	918	(2)
Min. Statutory Ratio (%)	20.0	20.0	20.0	-	-
Leverage Ratio (%)	52.3	64.5	49.0	(1,218)	325
Equity-to-Loans Ratio (%)	27.6	26.7	29.0	96	(136)
NPL Ratio (%)	12.1	10.6	10.7	148	141
NPL Coverage Ratio (%)	13.9	25.4	23.3	(1,145)	(939)
Long Term Debt to Total Liabilities and Equity (%)	8.4	11.5	8.3	(313)	12
NTA/share (KES)	47.4	46.8	51.8	1	(433)
Book value/share (KES)	50.0	48.5	50.0	2	-

(Source: Company, DBIB Research)

OPERATING PERFORMANCE

	1Q18	1Q17	4Q17	y-y bps ch	q-q bps ch
Yield on interest earning assets (%)*	10.4	10.9	10.5	(57)	(18)
Cost of funds (%)*	5.3	4.6	5.2	72	10
Net Interest Margin (%)*	5.0	6.5	5.3	(148)	(28)
Loan-to-Deposits ratio (%)	80.5	98.7	86.2	(1,818)	(568)
Loan-to-Dep.&Borrowed Funds ratio (%)	72.1	84.4	76.8	(1,225)	(466)
Funded Income Generating Potential (%)	90.2	90.8	90.7	(61)	(48)
Funded Income Reliance (%)	70.4	73.2	73.2	(282)	(276)
Cost to income ratio (%)	45.0	39.3	45.3	566	(38)
Pre-tax margin (%)	39.3	37.0	32.3	229	697
PAT margin (%)	27.6	25.8	22.1	182	552

*Annualized

(Source: Company, DBIB Research)

APPENDIX

COMPANY INVESTMENT RATINGS

Buy: Share price may generate more than 15.0% upside over the next 12 months

Overweight: Share price may generate between 5.0% and 15.0% upside over the next 12 months

Hold: Share price may fall within the range of <+5.0/ -10.0% over the next 12 months

Take Profit: Target price has been attained. Look to accumulate at lower levels. Company fundamentals however remain strong

Underweight: Share price may generate between 10.0% and 15.0% downside over the next 12 months

Sell: Share price may generate more than 15.0% downside over the next 12 months, significant business and/or financial risks present, industry concerns

Not Rated: Counter is not within regular research coverage

SECTOR INVESTMENT RATINGS

Overweight: Industry performance better than that of the whole market

Equal weight: Industry performance about the same as that of the whole market

Underweight: Industry performance worse than that of the whole market

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