

# 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.

### DIAMOND TRUST BANK GROUP: 3Q18 EARNINGS UPDATE

Dear All,

DIAMOND TRUST BANK (DTB) announced its 3Q18 results recording a **10.8% y-o-y growth in attributable income to KES 5.2 BN**. Profit After Tax (PAT) noted a 10.0% y-o-y growth to KES 5.6 BN, prior to a KES 396.6 MN non controlling interest income deduction (+7.9% y-o-y). EPS for the period stood at KES 18.76. Its trailing EPS stands at KES 25.07, down 3.2% y-o-y. Its annualized ROA and ROE declined 4 bps and 9 bps y-o-y to 2.0% and 12.3% respectively.

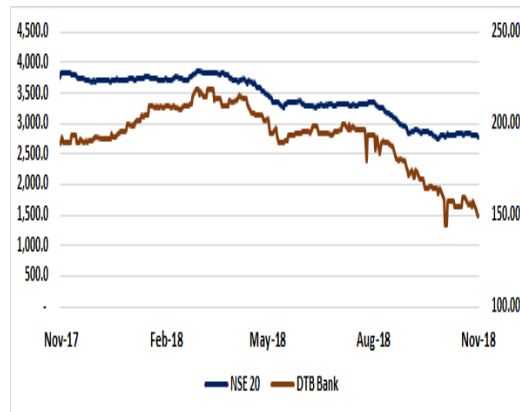
Below please find key highlights:

**Net interest income rose a modest 2.9% y-o-y to KES 14.9 BN.** This followed a 3.0% y-o-y rise in interest income to KES 26.5 BN and a similar 3.0% y-o-y rise in interest expense to KES 11.6 BN. Annualized yield on interest earning assets shed 58 bps y-o-y to 10.3% (-1 bps q-o-q) whereas annualized cost of funds eased by 24 bps y-o-y to 4.8% (-2 bps q-o-q). As a result, annualized Net Interest Margin (NIMs) dropped 34 bps y-o-y to 5.6% (+1 bps q-o-q). We believe that this hints at a bottoming out of DTB's loans and deposits yield restructuring, with NII to be driven by interest earning asset value growth going forward.

**Interest income from loans and advances** declined 1.5% y-o-y to KES 16.5 BN, placing the annualized yield on average loans at 11%, down 25 bps y-o-y from 11.4% in 3Q17. Interest income from government securities rose 11.1% y-o-y to KES 9.7 BN, placing the annualized yield on average government securities at 10.1%, down 60 bps y-o-y. Interest expense on customer deposits rose 1.2% y-o-y to KES 10.3 BN placing the annualized cost of average deposits at 4.8%, down 33 bps y-o-y.

**Non interest income rose 6.3% y-o-y to KES 4.1 BN** following a 7.4% y-o-y rise in fees and commissions to KES 2.6 BN and a 2.8% y-o-y increase in forex income to KES 1.2 BN. This comprised of a 7.7% y-o-y rise in fees on loans to KES

### DTB BANK: 52 WEEK PRICE PERFORMANCE



(Source: NSE, DBIB Research)

PRICE	ABSOLUTE	EXCESS
RETURN	RETURN	RETURN
3 months	(22.68)	(5.47)
6 months	(26.11)	(5.75)
12 months	(21.05)	6.41

### KEY METRICS

Current Price (KES)	150.00
52 week Range (KES)	175.00-219.00
YTD Return (%)	(21.9)
Issued Shares (Mn)	279.6
Market Cap (USD Mn)	407.7

Recommendation	OVERWEIGHT
Trailing EPS (KES)	25.07
NAV (KES)	185.53
P/E (x)	6.0
P/B (x)	0.8
Div Yld (%)	-

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1.0 BN and a 7.2% y-o-y rise in other fees and commissions to KES 1.6 BN. We note that the rise in fees & commissions from loans to be a factor of upward repricing rather than loan value growth, evidenced by a 7.0% y-o-y increase in fees/unit loan value. Funded income reliance declined 55 bps y-o-y to 78.3%.

**Operating expenses (less loan loss provisions) rose 6.1% y-o-y to KES 8.4 BN.** This was mainly due to an 11.3% y-o-y rise in other operating expenses to KES 3.7 BN and a 4.3% y-o-y rise in staff costs to KES 3.1 BN. Cost to income ratio rose 102 bps y-o-y to 44.4%.

**Total assets grew 7.8% y-o-y to KES 385.0 BN (+2.4% q-o-q).** This was courtesy of a 17.7% y-o-y rise in investment securities to KES 128.3 BN. Customer loans and advances remain unchanged, inching up 0.7% y-o-y to KES 197.7 BN. Notably, deposits from other banks rose 74.3% y-o-y to KES 15.7 BN while deposits due to other banks rose 62.8% y-o-y to KES 27.0 BN, suggesting a net borrowing position in the interbank market. We highlight that 2.0% of DTB's investment securities have been recognized at fair value, against a traditional 100% recognition of investment securities as Held To Maturity (HTM). This may be a possible indication of the KES 2.5 BN being liquidated and redirected towards interbank activities or onward lending.

**Customer deposits rose 6.5% y-o-y to KES 282.2 BN (+0.2% q-o-q)** whereas borrowed funds declined 17.4% y-o-y to KES 14.9 BN, evidence of further retirement of the more expensive funding base. Loan to deposits ratio declined 402 bps y-o-y to 70.0% whereas loans to deposits and borrowed funds ratio shed 451 bps y-o-y to 61.0%.

**Gross non-performing loans (NPLs) declined 1.7% y-o-y to KES 16.3 BN (+7.0% q-o-q)** whereas interest in suspense rose by 1.4% y-o-y to KES 2.4 BN. As a result, total NPLs declined 2.0% y-o-y to KES 13.8 BN. Loan loss provisions rose 40.8% y-o-y to KES 9.3 BN, translating to a coverage ratio of 67.4%, from 47.0% in 3Q17. In addition to the changes in IFRS 9 implementation, we attribute the significant q-o-q increase to full recognition of a sizeable loan stemming from the manufacturing sector. This resulted in the NPL ratio (Gross NPL/ Gross Loan) rising 48 bps q-o-q to 7.6% in 3Q18, despite improving by 15 bps from 3Q17's 7.8%. We believe this to be primarily attributable to an isolated loan, and not indicative of systemic issues rising or the bank's loan book quality in general.

**Capital adequacy ratios:** DTB Kenya's core capital to Total Risk Weighted Assets (TRWA) gained 130 bps y-o-y to 17.8% (up 40 bps q-o-q) whereas its Total capital to TRWA rose 70 bps y-o-y to 19.1% (up 40 bps q-o-q). Both ratios remain above the statutory minimum of 10.5% and 14.5% respectively. Relatively high capital

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ratios are indicative of the group's superior asset quality and provisioning levels over the years. The capital ratios adjusted for IFRS 9 requirements were recorded at 18.8% and 20.1% respectively, observing 100 bps improvement each on the currently reported ratios. We believe this to be due to reduced provisioning requirements from easing off-balance sheet activities. DTB's total contingent liabilities dipped 24.2% y-o-y primarily due to a 52.1% decline in forwards, swaps and options held in 3Q18. Liquidity ratio improved 70 bps y-o-y to 51.9%, above the statutory minimum of 20.0%.

**Going forward:** While DTB's option to increase earnings retention to 100% rather than maintain payout diluted ROE, we believe this may offer more sustainable returns in the medium term on the back of sturdier core capital ratios. This has enabled the bank to not only retire costly tier II funding, but improve its capacity for onward lending in the event of an interest rate cap amendment. We also highlight its low risk profile evidenced by reduced derivative engagement, superior asset book quality, low CTI, relatively high NPL provisioning to be a strong long term value proposition given that it currently trades below book value, despite its high asset quality. We however put a caveat, given that DTB's dividend yield has historically been low, while its income generation propensity indicates a foregoing of high margins for asset and liability stickiness. On a trailing basis, DTB is trading at a P/E of 6.0x relative to an industry median of 5.9x, a P/B of 0.8x relative to an industry median of 0.9x. Its ROA stands at 2.0%, relative to an industry median of 2.3% whereas its annualized ROE stands at 12.3%, relative to an industry median of 17.1%. We issue an **Overweight** recommendation.

## PROFIT AND LOSS SUMMARY (KES MN)

Year End: December	3Q18	3Q17	y-y% ch	3q18	2q18	3q17	y-y% ch	q-q% ch
Interest income	26,452	25,692	3.0	8,948	8,919	8,840	1.2	0.3
Interest expense	(11,549)	(11,211)	3.0	(19,124)	3,857	(18,568)	3.0	(595.9)
Net interest income	14,902	14,481	2.9	4,974	5,062	4,987	(0.3)	(1.7)
Other operating income	348	314	11.0	142	113	192	(26.4)	25.4
Fees and commission income	2,590	2,412	7.4	850	865	788	7.9	(1.8)
Net income from forex dealings	1,193	1,160	2.8	397	430	366	8.4	(7.8)
Total non-interest income	4,131	3,885	6.3	1,388	1,408	1,346	3.1	(1.4)
Total income	19,034	18,367	3.6	6,362	6,470	6,334	0.5	(1.7)
Less operating expenses	(8,442)	(7,958)	6.1	(2,842)	(2,808)	(2,678)	6.1	1.2
Operating profit	10,592	10,408	1.8	3,520	3,663	3,655	(3.7)	(3.9)
Bad debt charge	(2,394)	(2,894)	(17.3)	(717)	(981)	(1,178)	(39.1)	(26.9)
Exceptional items	11	11	1.8	5	2	3	72.8	175.3
Profit before tax	8,209	7,526	9.1	2,808	2,684	2,480	13.2	4.6
Less tax	(2,567)	(2,397)	7.1	(921)	(731)	(764)	20.6	26.1
Profit after tax	5,642	5,129	10.0	1,886	1,953	1,716	9.9	(3.4)
Attributable Income	5,245	4,735	10.8	1,747	1,817	1,538	13.6	(3.8)
EPS (KES)	18.76	17.42	7.7	6.25	6.50	5.42	15.3	(3.9)

(Source: Company, DBIB Research)

## BALANCE SHEET SUMMARY (KES MN)

Year End: December	3Q18	1H18	3Q17	y-y% ch	q-q% ch
Total shareholder's equity	51,874	50,012	46,744	11.0	3.7
Minority interest	5,108	4,978	5,161	(1.0)	2.6
Total Equity	56,981	54,990	51,905	9.8	3.6
Deposits due to other banks	26,973	18,729	16,572	62.8	44.0
Customer deposits	282,195	281,746	265,048	6.5	0.2
Borrowed funds	14,932	16,936	18,070	(17.4)	(11.8)
Other liabilities	3,895	3,676	5,609	(30.6)	5.9
Total equity and liabilities	384,976	376,078	357,204	7.8	2.4
Central bank balances	27,373	22,156	27,535	(0.6)	23.5
Deposits due from banks	15,746	11,225	9,032	74.3	40.3
Investment Securities	128,256	129,172	108,953	17.7	(0.7)
Held for dealing securities	0	0	0	0.0	0.0
Customer loans and advances	197,655	198,234	196,293	0.7	(0.3)
Other assets	7,910	7,268	7,315	8.1	8.8
Intangible assets	1,342	1,156	1,386	(3.1)	16.1
Fixed assets	6,695	6,867	6,691	0.1	(2.5)
Total assets	384,976	376,078	357,204	7.8	2.4

(Source: Company, DBIB Research)

## INVESTMENT RETURN

	3Q18	1H18	3Q17	y-y bps ch	q-q bps ch
ROA (%)*	2.0	1.9	1.9	4	9
ROIC (%)*	2.1	2.0	2.0	8	15
ROE (%)*	12.3	12.7	12.2	11	(45)

(Source: Company, DBIB Research)

\*Annualized

## CAPITAL ADEQUACY, LIQUIDITY & ASSET QUALITY

	3Q18	1H18	3Q17	y-y bps ch	q-q bps ch
Core capital/TRWA (%)	17.8	17.4	16.5	130	40
Min. Statutory Ratio (%)	10.5	10.5	10.5	-	-
Total capital/TRWA (%)	19.1	18.7	18.4	70	40
Min. Statutory Ratio (%)	14.5	14.5	14.5	-	-
Liquidity Ratio (%)	51.9	51.1	51.2	70	80
Min. Statutory Ratio (%)	20.0	20.0	20.0	-	-
Leverage Ratio (%)	13.5	13.3	13.1	39	18
Equity-to-Loans Ratio (%)	28.8	27.7	26.4	239	109
NPL Ratio (%)	7.6	7.2	7.8	(15)	48
NPL Coverage Ratio (%)	67.4	65.4	47.0	2,049	204
Long Term Debt to Total Liabilities and Equity (%)	3.9	4.5	5.1	(118)	(62)
Adj. Core capital/TRWA (%)	18.8	18.5	-	-	-
Adj. Total capital/TRWA (%)	20.1	19.8	-	-	-
Book value/share (KES)	178.9	177.7	163.4	1,546	120

(Source: Company, DBIB Research)

\*\*Total Loan Portfolio net of Interbank Lending

## OPERATING PERFORMANCE

	3Q18	1H18	3Q17	y-y bps ch	q-q bps ch
Yield on interest earning assets (%)*	10.3	10.3	10.9	(58)	(1)
Cost of funds (%)*	4.8	4.8	5.0	(24)	(2)
Net Interest Margin (%)*	5.6	5.6	5.9	(34)	1
Loan-to-Deposits ratio (%)	70.0	70.4	74.1	(402)	(32)
Loan-to-Dep.& Borrowed Funds ratio (%)	61.0	66.4	65.5	(451)	(538)
Funded Income Generating Potential (%)	88.7	90.0	88.0	76	(130)
Funded Income Reliance (%)	78.3	78.4	78.8	(55)	(6)
Cost to income ratio (%)	44.4	44.2	43.3	102	16
Pre-tax margin (%)	43.1	42.6	41.0	215	50
PAT margin (%)	29.6	29.6	27.9	172	0

\*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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