

NIC Bank– 1H17 Earnings Update

NIC Bank announced an 11.9% y/y (+13.2%, q/q) drop in 1H17 net earnings to KES 2.0B. Net interest income fell 11.1% y/y (-0.6%, q/q) coupled with a 6.9% y/y (+3.1%, q/q) drop in non-interest income. The lender did not declare an interim dividend.

Interest income from loans decline despite growth in loan book

Total interest income dipped 10.6% y/y (+4.3% q/q) to KES 8.8B. Interest income from loans and advances decreased 16.9% y/y to KES 6.6B although the lender's loan book grew 4.1% y/y (+0.4% q/q) to KES 116.8B. Interest income from government securities rose 20.6% y/y to KES 2.1B on the back of a 52.5% y/y surge in total funds held in government securities to KES 44.3B. NIC like its peers is opting to shift its funds into risk-free government securities than lending to risky borrowers in the wake of the rate cap.

Loans to deposits dips easing cost of funds

Total interest expenses declined 9.7% y/y (+12.6% q/q) to KES 3.4B. Interest expenses incurred from customer deposits plummeted 13.5% y/y to KES 2.7B even though customer deposits saw an 18.9% y/y (+13.0% q/q) rise to KES 133.2B. This implies that the bank may have seen a growth in non-interest bearing deposits. Lenders continue to reduce the level of interest-bearing deposits on their books in a bid to reduce interest expenses after the implementation of the rate cap. The loan to deposit ratio slumped 12.4% y/y to 87.7%. Previously, the bank had embarked on aggressively growing its loan book leading to a higher uptake in interest bearing deposits. The bank now has the capacity to grow its loan book without attracting higher interest bearing deposits. In line with the rate cap, it has limited the growth of its loan book and we see the trend hold going forward.

Non funded income in the red

Non funded income slid 6.9% y/y to KES 2.0B (+3.1% q/q) primarily attributed to a 43.9% y/y slump in other income to KES 310.7M. However, gross fees and commission income posted a healthy growth of 8.6% y/y to KES 1.1B. Moreover, foreign exchange income (+1.2% y/y to KES 584.1M) remained largely flat as the first half of the year has seen a relative stability in the Kenyan Shilling leading to a reduction in currency trading. Non funded income contributed to 27.5% to total income, a 290bps drop y/y.

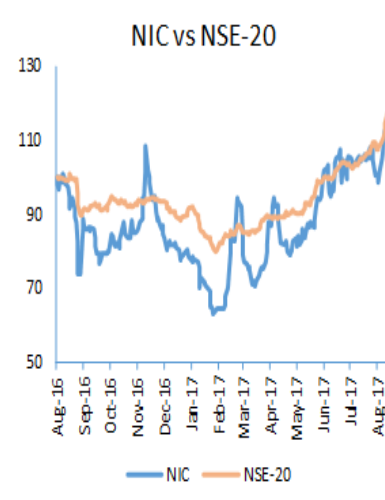
Lowest cost to income ratio among peers

Total operating expenses went up 4.8% y/y (+9.6% q/q) to KES 3.0B. The lender's cost to income ratio increased 600bps but still hovers comfortably at a record of 42.9%, which is among the lowest in comparison to its peers. Going forward we expect increased cost effi-

Bloomberg Ticker :	NICB. KN
Reuters Ticker:	NIC.NR

Share Statistics	
Current Price (KES)	36.75
Issued shares (M)	639.9
Market cap (USD M)	227.8
Year end	Dec
Foreign ownership (%)	1.3
Free float (%)	60.4
Avg daily trading vol (USD)	78.4

Price Trend



Source: Bloomberg

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ciency to bolster the bottom line as margins are squeezed due to the cap on lending rates.

On the other hand, loan loss provision expense plunged 31.5% y/y KES 1.4B even though gross NPLs climbed 14.1% y/y (+3.9% q/q) to KES 14.3B. The bank's coverage ratio has risen 430bps to 35.8% y/y, marking better provisioning over the year. On the contrary, its NPL ratio has risen 100 bps to 11.8%, which is on the higher side amidst the banking sector.

Looking ahead

The stock currently trades at 5.7x trailing FY16 earnings and 0.7x trailing FY16 book value, with a dividend yield of 5.1%. Going forward, we expect NIC to leverage on its cost to income ratio to support its bottom line. NIC seeks to attract cheaper deposits, which may lower its cost of funds further and improve its NIM currently at 5.8% (-180bps y/y). The concern lies in NIC's decline in non-interest income, especially at a time when banks are reducing their reliance on interest income and driving growth in non-interest income to maintain profitability. NPLs and the cap on lending rates continue to pose key challenges for the lender in medium to long term. The attractive P/E and P/B multiples highlight a good time to buy the counter. However, the low dividend yield may not entice dividend seeking investors.

	FY15	1Q16	2Q16	3Q16	4Q16	FY16	1Q17	2Q17	% chg y/y	% chg q/q
Income Statement	KES '000	KES '000	KES '000	KES '000	KES '000	KES '000	KES '000	KES '000	1H17 vs 1H16	2Q17 vs 1Q17
Interest Income	17,014,132	5,007,257	4,848,725	4,870,074	4,294,619	19,020,675	4,312,231	4,499,237	-10.6%	4.3%
Interest Expense	7,271,599	2,052,454	1,728,414	1,548,694	1,522,516	6,852,078	1,605,110	1,807,453	-9.7%	12.6%
Net Interest Income	9,742,533	2,954,803	3,120,311	3,321,380	2,772,103	12,168,597	2,707,121	2,691,784	-11.1%	-0.6%
Foreign Exchange Income	1,431,231	305,109	272,245	287,859	239,934	1,105,147	300,718	283,350	1.2%	-5.8%
Gross Fees and Commission	1,844,429	505,612	520,675	514,721	469,343	2,010,351	554,045	560,147	8.6%	1.1%
Other Income	756,500	326,758	226,687	114,003	236,613	904,061	134,223	176,514	-43.9%	31.5%
Non Interest Income	4,032,160	1,137,479	1,019,607	916,583	945,890	4,019,559	988,986	1,020,011	-6.9%	3.1%
Total Operating Income	13,774,693	4,092,282	4,139,918	4,237,963	3,717,993	16,188,156	3,696,107	3,711,795	-10.0%	0.4%
Total Operating Expenses	5,724,943	1,377,899	1,525,951	1,631,456	1,736,371	6,271,677	1,452,245	1,591,566	4.8%	9.6%
Loan Loss Provision Expense	1,652,475	1,315,115	794,553	1,085,928	553,934	3,749,530	875,234	570,469	-31.5%	-34.8%
Operating Profit	6,397,275	1,399,268	1,819,414	1,520,579	1,427,688	6,166,949	1,368,628	1,549,760	-9.3%	13.2%
Profit Before Tax	6,397,275	1,399,268	1,819,414	1,520,579	1,427,688	6,166,949	1,368,628	1,549,760	-9.3%	13.2%
Current Tax	2,388,860	408,479	505,101	461,775	1,850,980	3,226,335	416,592	472,033	-2.7%	13.3%
Profit After Tax	4,485,125	990,789	1,314,313	1,058,804	966,490	4,330,396	952,036	1,077,727	-11.9%	13.2%
EPS (KES)	7.00	1.55	2.05	1.66	1.51	6.77	1.49	1.68	-11.9%	12.8%
Balance Sheet										
Total Shareholders' Equity	26,346,142	27,115,560	28,289,935	29,551,617	30,345,364	30,345,364	31,022,766	32,567,413	15.1%	5.0%
Deposits due to Banks & Financial Institutions	9,064,552	5,756,289	5,877,891	4,656,169	2,775,926	2,775,926	2,141,065	2,588,622	-56.0%	20.9%
Borrowed Funds	15,356,190	15,232,609	20,412,988	14,755,486	19,965,484	19,965,484	20,002,325	18,967,950	-7.1%	-5.2%
Customer Deposits	112,364,637	110,331,939	112,000,727	108,358,276	111,824,685	111,824,685	117,841,957	133,158,753	18.9%	13.0%
Total Liabilities	139,442,126	133,785,620	140,768,400	135,717,861	139,113,621	139,113,621	142,801,551	156,922,411	11.5%	9.9%
Total Equity and Liabilities	165,788,268	160,901,180	169,058,335	165,269,478	169,458,985	169,458,985	173,824,317	189,489,824	12.1%	9.0%
Cash and CBK Balances	8,940,056	10,400,155	8,117,105	8,435,060	7,263,501	7,263,501	8,878,687	10,135,442	24.9%	14.2%
Balances due from Banks & Financial Institutions	6,675,640	5,981,317	13,237,433	4,812,264	9,682,208	9,682,208	9,945,596	10,247,516	-22.6%	3.0%
Government and Other Securities	27,832,978	25,571,332	29,063,685	34,589,735	30,470,895	30,470,895	31,078,256	44,328,933	52.5%	42.6%
Net Loans and advances	116,009,302	111,987,605	112,150,830	110,470,843	114,466,274	114,466,274	116,323,035	116,769,833	4.1%	0.4%
Fixed Assets	1,063,760	1,007,252	1,067,345	1,080,168	1,043,497	1,043,497	1,023,268	1,024,797	-4.0%	0.1%
Total Assets	165,788,268	160,901,181	169,058,335	165,269,478	169,458,985	169,458,985	173,824,317	189,489,824	12.1%	9.0%
Key Ratios										
Gross NPL (KES M)	14,351,893	13,391,635	12,565,456	14,251,802	13,587,912	13,587,912	13,800,506	14,341,928	14.1%	3.9%
Interest In Suspense (KES M)	1,123,359	1,461,626	553,456	676,464	704,080	704,080	1,334,166	1,688,021	205.0%	26.5%
Total NPL (KES M)	13,228,534	11,930,009	12,012,000	13,575,338	12,883,832	12,883,832	12,466,340	12,653,907	5.3%	1.5%
Loan Loss Provision (KES M)	2,776,627	3,732,017	3,952,895	4,978,105	5,022,089	5,022,089	4,643,679	5,132,699	29.8%	10.5%
Net NPL	10,451,907	8,197,992	8,059,105	8,597,233	7,861,743	7,861,743	7,822,661	7,521,208	-6.7%	-3.9%
NPL Ratio	12.1%	11.6%	10.8%	12.3%	11.4%	11.4%	11.4%	11.8%		
Coverage Ratio	19.3%	27.9%	31.5%	34.9%	37.0%	37.0%	33.6%	35.8%		
Cost of Risk	1.4%	4.7%	2.8%	3.9%	1.9%	3.3%	3.0%	2.0%		
Loan to Deposits	103.2%	101.5%	100.1%	101.9%	102.4%	102.4%	98.7%	87.7%		
Yield on Interest Earning Assets	11.3%	14.0%	12.6%	13.0%	11.1%	12.3%	11.0%	10.5%		
Cost of Funds	5.3%	6.3%	5.0%	4.8%	4.5%	5.1%	4.6%	4.7%		
NIM	6.0%	7.7%	7.6%	8.1%	6.6%	7.2%	6.4%	5.8%		
Non Funded/Total Income	29.3%	27.8%	24.6%	21.6%	25.4%	24.8%	26.8%	27.5%		
Cost to Income Ratio	41.6%	33.7%	36.9%	38.5%	46.7%	38.7%	39.3%	42.9%		
ROE	17.0%	14.6%	18.6%	14.3%	12.7%	14.3%	12.3%	13.2%		
ROA	2.7%	2.5%	3.1%	2.6%	2.3%	2.6%	2.2%	2.3%		
Core Capital/TRWA	14.9%	15.2%	16.7%	17.2%	18.7%	18.7%	17.9%	17.7%		
Total Capital/TRWA	20.6%	21.4%	22.8%	23.0%	23.0%	23.0%	21.9%	21.6%		
Liquidity Ratio	29.2%	31.6%	38.6%	34.0%	38.7%	38.7%	39.0%	45.7%		
P/E (x)						5.7				
P/B (x)						0.7				
Dividend Yield						5.1%				

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