NIC BANK – FY2012 EARNINGS UPDATE

8th March 2013

Analyst:

Samuel Mugacha

E-mail: samuel.mugacha@fib.co.ke

Head Office:

Crawford Business Park, Ground floor

State House Road Tel: 0207606026-37

www.fib.co.ke

P.O Box 45236, 00100
Nairobi.

Investment Summary

We maintain our BUY recommendation

We maintain our **BUY** recommendation for NIC Bank with a revised price target of KES 57.97, based on P/B multiple which represents a 22.1% upside from the current share price of KES 47.50 as at 8th March 2013. This is following the release of their FY2012 results which showed a profit after tax of KES 3.0 billion, a KES 152.6 million variance from our forecast of KES 3.2 billion.

Key results highlight includes:

Total interest income went up by 67.9%

- ✓ **Interest Income buoyed by high yield**: Total interest income went up by 67.9% to KES 11.5 billion compared to KES 6.8 billion recorded during the previous financial year. Interest on loans and advances went up by 63.9% to KES 9.9 billion compared to KES 6.0 billion recorded in FY2011.

Interest expenses went up by 134.5%

- ✓ **Interest expenses not spared in the high interest rate environment**: Total interest expenses went up by 134.5% to KES 6.0 billion compared to KES 2.6 billion recorded in FY2011. The average cost of deposits rose from 3.7% in FY2011 to 6.9% in the financial year under review.

- ✓ **Net Interest Margin deteriorates:** The net interest margin deteriorated slightly to 5.6% compared to 6.1% recorded in the previous financial year.

Total non interest income went up by 21.6%

- ✓ **Non funded income grows while its contribution to total income declines:** The total non interest income grew by 21.6% to KES 2.9 billion compared to KES 2.4 billion recorded in FY2011. As a percentage of total income, the contribution of non funded income stood at 34.6% compared to a contribution of 35.8%.

Operating expenses went up by 26.4%

- ✓ **Slight increase in cost to income:** Total operating expenses went up by 26.4% to KES 3.9 billion compared to KES 3.1 billion recorded in FY2011. The cost to income ratio went up slightly to 46.1% compared to 45.9% recorded during the previous financial year.

Year to 31 Dec	2011A	2012A	2013F
Net Income (KES '000,000)	3,904	5,483	6,870
EPS (KES)	5.54	6.03	8.23
BVPS	24.02	28.51	34.80
P/B	2.5X	2.0X	1.7X
ROE	25.7%	19.6%	24.7%
C/I	41.5%	46.1%	39.9%

Source: company reports & FIB estimates

NIC BANK

NIC Bank	KES '000		
FY2012 Income statement	**FY2011**	**FY2012**	**% Growth**
Net Interest Income	3,904,050	5,483,868	40.5%
Fees and commissions	958,183	1,053,112	9.9%
Total income	*6,602,734*	*8,380,398*	26.9%
Loan loss provisions	(258,151)	(297,485)	15.2%
Operating expenses	(2,739,635)	(3,862,431)	41.0%
Profit before tax	*3,604,948*	*4,517,967*	*25.3%*
Tax	(897,811)	(1,481,173)	65.0%
Profit after tax	***2,707,137***	***3,036,794***	***12.2%***
Earnings Per Share(EPS)- Basic& Diluted	**5.54**	**6.03**	**8.8%**
Dividend per share- proposed	**0.25**	**1.00**	**300.0%**

Forecasted Balance Sheet	FY2011	FY2012	% Growth
Total Assets	***78,984,005***	***108,348,593***	***37.2%***
Loan book	56,624,621	71,540,092	26.3%
Government securities	7,500,288	17,478,232	133.0%
Total customer Deposits	66,293,053	83,379,576	25.8%
Total Liabilities	*68,461,052*	*92,866,971*	*35.6%*
Shareholder funds & non controlling int.	*10,522,953*	*15,481,622*	*47.1%*
Total shareholder and liability funds	***78,984,005***	***108,348,593***	***37.2%***

Profit before tax up by 25.3%

NIC Bank released its FY2012 results which showed a 25.3% growth in profit before tax to KES 4.5 billion compared to KES 3.6 billion recorded during the previous financial year. This is a KES 225.5 million variance compared to our forecasted profit before tax of KES 4.3 billion, in our banking sector report, "The innovation imperative".

Hogher yield on loans

This was driven by a higher yield on loans and advances (from 10.3% to 13.8%) coupled with increased interest income on government securities due to increased investments in government securities using funds raised in the rights issue.

Government securities went up to KES 17.5 billion compared to KES 14.5 billion recorded during the first nine months of the year under review.

Total interest income up by 67.9%

Interest Income buoyed by high yield: Total interest income went up by 67.9% to KES 11.5 billion compared to KES 6.8 billion recorded during the previous financial year. Interest on loans and advances went up by 63.9% to KES 9.9 billion compared to KES 6.0 billion recorded in FY2011. This is higher than our forecast of KES 8.2 billion, as the bank achieved a much higher yield than expected.

The interest yield on loans and advances stood at 13.8% compared to 10.6% recorded during the previous financial year. We forecasted a much slower yield on loans at 12.9% for FY2012, due to the lower interest rate environment which we expected to pass down to the customer.

Interest income yield on finance leases grew by 17.8%

This yield was pushed up by the finance leases book which grew by KES 4.0 billion during the financial year and had an interest income yield of 17.8% according to management.

Interest from government securities went up by 75.9% to KES 1.2 billion compared to KES 660.2 million recorded in FY2011.

Interest on deposits and placements went up by 199.5% to KES 412.3 million compared to KES 137.7 million recorded during the previous financial year.

Total interest expenses went up by 134.5%

Interest expenses not spared in the high interest rate environment: Total interest expenses went up by 134.5% to KES 6.0 billion compared to KES 2.6 billion recorded in FY2011. The high interest rate environment and tight liquidity during the first half of the financial year saw the interest paid on customer deposits go up by 137.3% to KES 5.7 billion.

The average cost of deposits rose from 3.7% in FY2011 to 6.9% in the financial year under review. This was higher than our forecast of 5.0% which shows the bank continues to have a challenge in raising cheap and sticky deposits.

Net interest margin deteriorated to 6.1%

Net Interest Margin deteriorates: The net interest margin deteriorated slightly to 5.6% compared to 6.1% recorded in the previous financial year. However, the net interest income increased by 28.1% to KES 5.5 billion compared to KES 4.3 billion recorded in FY2011.

The deterioration of net interest margin can be attributed to the high cost of funding during FY2012.

Non funded income grows while its contribution to total income declines: The total non interest income grew by 21.6% to KES 2.9 billion compared to KES 2.4 billion recorded in FY2012. As a percentage of total income, the contribution of non funded income stood at 34.6% compared to a contribution of 35.8% in FY2011 which is due to a higher than expected growth in interest income driven by high yields.

Operating expenses went up by 26.4%

Slight increase in cost to income: Total operating expenses went up by 26.4% to KES 3.9 billion compared to KES 3.1 billion recorded in FY2011. This was buoyed by a 27.3% increase in other operating expenses to KES 1.1 billion compared to KES 863.5 million recorded during the previous financial year. Depreciation and amortization charges also went up by 30% and 173.3% to KES 204.5 million and KES113.5 million respectively.

The cost to income ratio went up slightly to 46.1% compared to 39.9% recorded during the previous financial year.

Balance Sheet

Total assets went up by 36.4%

Total assets for the firm went up by 36.4% to KES 108.3 billion compared to KES 79.5 billion recorded during the previous financial year. This was largely driven by the 26.3% growth in the loan book to KES 71.2 billion compared to KES 56.6 billion recorded in FY2011. This is slightly below our forecast of KES 72.3 billion.

Total liabilities went up by 35.6% to KES 92.9 billion compared to KES 68.5 billion recorded during the previous financial year.

Customer deposits grew by a moderate 0.5%, KES 410.4 million, to KES 83.4 billion. We forecasted customer deposits to settle at KES 84.8 billion driven by retail deposits.

Outlook

Risk in NIC bank remains its high dependence on corporate and institutional deposits

Going forward, the risk to NIC Bank in our view remains its high dependence on corporate and institutional banking deposits, as stated in our banking sector report, "The innovation imperative". During the year under review, the bank initiated various retail deposit mobilization mechanisms in order to boost the proportion of the cheap and sticky deposits which come at a cheaper cost of funding.

BUY recommendation

We maintain our **BUY** recommendation in NIC with a target price of KES 57.97 which represents a 22.1% upside from the current share price of KES 47.50 as at 8th March 2013.