

Valuation Summary

- We recommend an accumulate for the NIC Bank stock with a target price of Kshs 42.9, representing an upside of 17.1% from the current price of Kshs 37.5 as at 6th May 2016, inclusive of a dividend yield of 2.7%
- NIC Bank is currently trading at a P/B of 0.9x and a P/E of 6.0x, versus an industry average of 1.6x and 7.8x, respectively

Key highlights during the quarter

- NIC Bank launched a co-branded card with Red Cross Kenya as part of its citizen responsibility agenda of liaising with good brands to drive up its impact on the community
- The bank implemented the Verified by Visa 3D secure cards to have proper security measures for online transactions to capture the growing e-commerce market shown by the growing online purchase community
- NIC Bank opened the Kisii Branch which is now fully operational. The Bank has plans to open 7 more branches in the larger Nairobi area as well as in Kiambu and Ruaka in the course of the year
- NIC Bank created new partnerships with Deacons, Nissan and General Motors as part of their Asset Financing business of which they have a market share of 27% as of March 2016 from 17% at the beginning of the year

Income Statement:

- Core Earnings per share remained flat at Kshs 1.55, share driven by 28.7% growth in operating revenue despite a faster growth in operating expenses of 53.7%
- Total operating revenue grew by 28.7% y/y to Kshs 4.1 bn from Kshs 3.2 bn in Q1'2015, 10.1% higher than our projection of Kshs 3.8 bn, driven by a 34.7% increase in net interest income to Kshs 3.0 bn, from Kshs 2.2 bn in Q1'2015, against our projections of a 13.6% growth. Interest income recorded a growth of 32.8% to Kshs 5.0 bn in Q1'2016 from Kshs 3.8 bn in Q1'2015 while interest expenses grew by 30.2% to Kshs 2.1 bn in Q1'2016 from Kshs 1.6 bn in Q1'2015
- Non-funded income recorded a growth of 15.3% to Kshs 1.3 bn in Q1'2016 from Kshs 1.0 bn in Q1'2015, supported by other income that grew by 45.9% attributable to sale of bonds that were acquired during the last quarter of 2015. This resulted in a revenue mix of 72%:38%, funded to non-funded income, respectively
- Total operating expenses rose by 53.7% y/y to Kshs 2.7 bn compared to Kshs 1.8 bn in Q1'2015, driven by a 212.3% jump in loan loss provision to Kshs 1.3 bn in Q1'2016 from Kshs 0.4 bn in Q1'2015, compared to our projections of a 25.0% increase in loan loss provisions. NIC Bank still factored in the same 5 corporate clients that they had accounted for in FY'2015 loan loss provision numbers as the situation has not improved. This is a prudent move to take to ensure the bank is not under covered
- The cost to income ratio rose to 65.8% in Q1'2016 compared to 55.1% in Q1'2015, compared to the listed industry average of 61.4% despite staff costs declining marginally by 6.5% to Kshs 0.6 bn from 0.7 bn
- Profit before tax declined slightly by 2.0% to Kshs 1.4 bn in Q1'2016 from Kshs 1.4 bn in Q1'2015, compared to our projections of Kshs 1.6 bn. Q1'2016 PAT remained flat declining by 0.3% to Kshs. 1.0 bn, from Kshs. 1.0 bn in Q1'2015, lower than our estimates of 13.2% growth

Balance Sheet:

- The balance sheet recorded a relatively fair growth with total liabilities increasing by 11.8% to Kshs 133.8 bn in Q1'2016 from Kshs 119.7 bn in Q1'2015 driven by customer deposits growth of 14.8% y/y to Kshs 110.3 bn, lower than our growth projection of a 19.2% growth. Deposit growth was driven by increased capital flight from small banks with the recent placing of Chase Bank under receivership and increased deposit mobilization through the bank's strategy of cross selling products across their existing customer base
- Total assets grew by 11.9% to Kshs 160.9 bn higher than our estimate of Kshs 143.7 bn with the loan book growing by 6.1% to Kshs 112.0 bn
- This resulted in a decline in the loan to deposit ratio of 101.5%, from 109.8% in Q1'2015 versus our projection of 103.0%. The loan to deposit is still high at over 100%, way above industry average of 89.0%, speaking to the need to see much better deposit mobilization by NIC Bank
- Non-performing loans grew marginally by 0.3% to Kshs 9.2 bn compared to an increase in gross loans of 2.9%, which led to a decrease in non-performing loans ratio to 8.0% from 8.2% in Q1'2015

- Yield on interest earning assets increased to 13.3% in Q1'2016 from 12.6% in Q1'2015 lower than the cost of funds which increased to 6.2% in Q1'2016 from 5.3% in Q1'2015, highlighting the impact of high cost deposits from the high rate environment in 2015 that rolled over to the first quarter despite declining interest rate environment. This led to a slight decline in net interest margin declining marginally to 7.1% from 7.3% in Q1'2015
- Shareholders' funds increased by 13.0% y/y to Kshs 26.6 bn in Q1'2016 from Kshs 23.6 bn in Q1'2015
- Return on equity declined to 17.8% from 19.7% in Q1'2015, while return on assets came in lower at 2.9% from 3.1% in Q1'2015
- The bank is currently well capitalised with its total capital to risk weighted ratio at 21.4%, 11.6% above the statutory requirement

Below is a summary of the key line items in the balance sheet and income statement.

Figures in Kshs billions unless otherwise stated

Balance Sheet	FY'2015	Q1'2015	Q1'2016	y/y change	Q1'2016e	% y/y change	Variance in Growth Actual vs. Expected
Government Securities	27.8	6.1	25.6	319.0%	26.4	332.0%	(12.9%)
Net Loans and Advances	116.0	105.6	112.0	6.1%	118.1	11.8%	(5.7%)
Total Assets	165.8	143.7	160.9	11.9%	166.6	15.9%	(3.9%)
Customer Deposits	112.4	96.1	110.3	14.8%	114.6	19.2%	(4.5%)
Borrowings	15.4	14.2	15.2	7.4%	15.4	8.3%	(0.9%)
Total Liabilities	139.4	119.7	133.8	11.8%	139.1	16.2%	(4.4%)
Shareholders' Funds	25.9	23.6	26.6	13.0%	27.0	14.5%	(1.6%)

Income Statement	FY'2015	Q1'2015	Q1'2016	y/y change	Q1'2016e	% y/y change	Variance in Growth Actual vs. Expected
Net Interest Income	9.7	2.2	3.0	34.7%	2.5	13.6%	21.2%
Net non-Interest Income	4.0	1.0	1.1	15.3%	1.3	29.8%	(14.5%)
Total Operating income	13.8	3.2	4.1	28.7%	3.8	18.6%	10.1%
Loan Loss provision	(1.7)	(0.4)	(1.3)	212.3%	(0.5)	11.1%	201.1%
Total Operating expenses	(7.4)	(1.8)	(2.7)	53.7%	(2.2)	23.4%	30.3%
Profit before tax	6.4	1.4	1.4	(2.0%)	1.6	12.6%	(14.6%)
Profit after tax	4.5	1.0	1.0	(0.3%)	1.1	13.2%	(13.6%)

Ratios	FY'2015	Q1'2015	Q1'2016
Loan to Deposit Ratio	103.2%	109.8%	101.5%
Return on average equity	18.4%	19.7%	17.8%
Return on average assets	2.9%	3.1%	2.9%
Yield on interest-earning assets	12.1%	12.6%	13.3%
Cost of funding	5.7%	5.3%	6.2%
Net Interest Margin	6.5%	7.3%	7.1%
Cost to Income	53.6%	55.1%	65.8%

Capital Adequacy Ratios	Q1'15	Q1'16
Core Capital/Total Liabilities	21.9%	20.5%
Minimum Statutory ratio	10.5%	10.5%
Excess	11.4%	10.0%
Core Capital/Total Risk Weighted Assets	14.6%	15.2%
Minimum Statutory ratio	10.5%	10.5%
Excess	4.1%	4.7%
Total Capital/Total Risk Weighted Assets	20.4%	21.4%

Minimum Statutory ratio	14.5%	14.5%
Excess	5.9%	6.9%
Liquidity Ratio	29.6%	31.6%
Minimum Statutory ratio	20.0%	20.0%
Excess	9.6%	11.6%
