Diamond Trust Bank Kenya – FY’2021

1st April, 2022

Below is a summary of Diamond Trust Bank - Kenya’s FY’2021 performance:

Balance Sheet Items	FY’2020 (Kshs bns)	FY’2021 (Kshs bns)	y/y change
Government Securities	111.1	124.3	11.9%
Net Loans and Advances	208.6	220.4	5.7%
Total Assets	**425.1**	**456.8**	**7.5%**
Customer Deposits	298.2	331.5	11.2%
Total Liabilities	356.7	382.3	7.2%
Shareholders’ Funds	**62.0**	**67.3**	**8.6%**

Balance Sheet Ratios	FY’2020	FY’2021	y/y change
Loan to Deposit Ratio	70.0%	66.5%	(3.5%)
Return on average equity	5.8%	6.8%	1.0%
Return on average assets	0.9%	1.0%	0.1%

Income Statement	FY’2020 (Kshs bns)	FY’2021 (Kshs bns)	y/y change
Net Interest Income	18.1	20.0	10.6%
Net non-Interest Income	6.1	6.3	3.0%
Total Operating income	**24.2**	**26.3**	**8.7%**
Loan Loss provision	7.3	7.6	3.2%
Total Operating expenses	19.7	19.9	1.1%
Profit before tax	**4.7**	**6.6**	**41.9%**
Profit after tax	**3.5**	**4.4**	**25.1%**
Core EPS	**12.6**	**15.8**	**25.1%**

Income Statement Ratios	FY’2020	FY’2021	% point change
Yield from interest-earning assets	8.7%	8.7%	0.0%
Cost of funding	3.93%	3.89%	(0.04%)
Net Interest Spread	4.7%	4.8%	0.1%
Net Interest Income as % of operating income	74.7%	76.0%	1.3%
Non-Funded Income as a % of operating income	25.3%	24.0%	(1.3%)
Cost to Income Ratio (CIR)	81.3%	75.6%	(5.7%)
CIR without provisions	51.0%	46.9%	(4.1%)
Cost to Assets	4.8%	4.5%	(0.3%)
Net Interest Margin	5.0%	5.1%	0.1%

Capital Adequacy Ratios	FY’2020	FY’2021
Core Capital/Total Liabilities	22.8%	22.0%
Minimum Statutory ratio	8.0%	8.0%
Excess	14.8%	14.0%
Core Capital/Total Risk Weighted Assets	20.7%	19.9%
Minimum Statutory ratio	10.5%	10.5%
Excess	10.2%	10.2%
Total Capital/Total Risk Weighted Assets	22.5%	21.2%
Minimum Statutory ratio	14.5%	14.5%
Excess	8.0%	7.6%
Liquidity Ratio	56.0%	61.6%
Minimum Statutory ratio	20.0%	20.0%
Excess	**36.0%**	**41.6%**
Adjusted Core Capital/Total Liabilities	23.4%	22.1%

Adjusted Core Capital/Total RWA	21.0%	20.0%
Adjusted Total Capital/Total RWA	22.7%	21.3%

Key Highlights - FY'2021

- In FY'2021, Diamond Trust Bank (DTB) became one of the seven banks that had partnered with the National Government to implement the Credit Guarantee Scheme, which is meant to offer SMEs affordable credit to sustain their operations from the adverse effects of the pandemic. Currently, over 170 loans amounting to over Kshs 427.0 mn have been disbursed by the banks under the programme, and,
- Also in FY'2021, DTB-K committed Kshs 1.6 bn for onward lending to Micro, Small and Medium Enterprises (MSMEs) to aid in recovery amid the pandemic. 30.0% of the money was targeted to women, youths and persons living with disability which will help businesses get back to their feet by boosting their working capital, aiding in acquisition of business assets and offsetting enterprises from the impacts of COVID-19. Further, the Group committed an additional Kshs 100.0 mn towards cushioning Kenya against the adverse effects of the pandemic where Kshs 50.0 mn was directed to the National COVID-19 Emergency Response Fund while the other Kshs 50.0 mn was directed towards initiatives to support vulnerable Kenyans.

Income Statement

- The bank's core earnings per share increased by 25.1% to Kshs 15.8, from Kshs 12.6 in FY'2020, in line with our expectations. The bank's performance was driven by the 8.7% increase in total operating income to Kshs 26.3 bn, from Kshs 24.2 bn in FY'2020, which outpaced the 1.1% increase in total operating expenses to Kshs 19.9 bn from Kshs 19.7 bn in FY'2020,
- Total operating income increased by 8.7% to Kshs 26.3 bn, from Kshs 24.2 bn in FY'2020 mainly driven by a 10.6% increase in the Net Interest Income (NII) to Kshs 20.0 bn, from Kshs 18.1 bn in FY'2020, coupled with a 3.0% growth in Non-Funded Income (NII) to Kshs 6.3 bn, from Kshs 6.1 bn in FY'2020,
- Interest income increased by 9.1% to Kshs 33.9 bn, from Kshs 31.1 bn in FY'2020. This was driven by a 21.9% increase in interest income from government securities to Kshs 15.1 bn, from Kshs 12.4 bn in FY'2020, coupled with a 0.2% increase in Interest income from loans and advances to Kshs 18.6 bn from Kshs 18.5 bn in FY'2020. Interest income from deposit placements also increased by 39.4% to Kshs 235.8 mn, from Kshs 169.2 mn in FY'2020. The Yield on Interest-Earning Assets remained unchanged at 8.7% as recorded in FY'2020, attributable to the 9.2% growth in average interest-earning assets to Kshs 391.2 bn, from Kshs 358.4 bn in FY'2020, which was at par with the 9.1% increase in trailing interest income,
- Interest expense increased by 6.9% to Kshs 13.9 bn, from Kshs 13.0 bn in FY'2020, following a 10.5% increase in interest expense on customer deposits to Kshs 12.4 bn, from Kshs 11.2 bn in FY'2020. The increase was however mitigated by a 7.4% decline in other interest expenses to Kshs 1.1 bn, from Kshs 1.2 bn in FY'2020 and a 33.6% decline on interest expense on placement liabilities to Kshs 374.3 mn, from Kshs 563.4 mn in FY'2020. Cost of funds, declined marginally to 3.89% from 3.93%, in FY'2020, owing to the 6.9% increase in interest expenses coupled with 7.9% growth in average interest-bearing liabilities. Net Interest Margin (NIM) marginally increased to 5.1%, from 5.0% in FY'2020 due to the faster 9.2% growth in average interest-earning assets which slightly outpaced the 10.6% increase in Net Interest Income,
- Non-Funded Income (NFI) rose by 3.0% to Kshs 6.3 bn, from Kshs 6.1 bn in FY'2020. The increase was mainly driven by the 5.3% increase in foreign exchange trading income to Kshs 2.5 bn from Kshs 2.3 bn recorded in FY'2020 coupled with a 26.2% increase in other fees to Kshs 2.3 bn, from Kshs 1.8 bn in FY'2020. The growth in NFI was however weighed down by an 8.9% decline in fees and commissions to Kshs 1.3 bn, from Kshs 1.4 bn in FY'2020. Notably, total fees and commissions increased by 10.8% to Kshs 3.6 bn, from

Kshs 3.3 bn, attributable to the lifting of the waiver on charges between mobile money wallets and bank accounts at the beginng of the year. As a result, the revenue mix shifted to 76:24 from 75:25 funded to non-funded income, owing to the 10.6% growth in NII which outpaced the 3.0% increase in NFI,

- Total operating expenses rose by 1.1% to Kshs 19.9 bn, from Kshs 19.7 bn in FY'2020, largely driven by the 3.2% increase in Loan Loss Provisions (LLP) to Kshs 7.6 bn from Kshs 7.3 bn in FY'2020 coupled with a 2.5% increase in staff costs to Kshs 4.8 bn from Kshs 4.7 bn in FY'2020. On the other hand, other operating expenses declined by 1.8% to Kshs 7.5 bn from Kshs 7.6 bn recorded in FY'2020,
- Cost to Income Ratio (CIR) improved to 75.6%, from 81.3% in FY'2020 owing to the 8.7% increase in operating income to Kshs 26.3 bn, from Kshs 24.2 bn in FY'2020 which outpaced the 1.1% increase in operating expenses to Kshs 19.9 bn, from Kshs 19.7 bn in FY'2020. Without LLP, the cost to income ratio also improved to 46.9%, from 51.0% in FY'2020, highlighting improved efficiency levels,
- Profit before tax rose by 41.9% to Kshs 6.6 bn, from Kshs 4.7 bn in FY'2020. Profit after tax increased by 25.1% to Kshs 4.4 bn in FY'2021, from Kshs 3.5 bn recorded in FY'2020, with the effective tax rate increasing to 33.4%, from 24.4% in FY'2020, and,
- The Board of Directors recommended a final dividend per share of Kshs 3.0 for FY'2021, subject to shareholders' approval, translating to a total dividend payout of Kshs 0.8 bn. At the current price of Kshs 58.8, this translates to a dividend yield of 5.3%.

Balance Sheet

- The balance sheet recorded an expansion as Total Assets increased by 7.5% to Kshs 456.8 bn, from Kshs 425.1 bn recorded in FY'2020. This growth was largely driven by an 11.9% increase in government securities to Kshs 124.3 bn, from Kshs 111.1 bn in FY'2020, coupled with a 5.7% increase in net loans to Kshs 220.4 bn, from Kshs 208.6 bn in FY'2020. The increased allocation in government securities was mainly on the back of the lender's cautious lending owing to the relatively high Non-Performing Loans,
- Total liabilities grew by 7.2% to Kshs 382.3 bn, from Kshs 356.7 bn in FY'2020, driven by an 11.2% increase in customer deposits to Kshs 331.5 bn from Kshs 298.2 bn in FY'2020. However, the growth was weighed down by a 19.1% decline in placements to Kshs 16.1 bn, from Kshs 20.0 bn, in FY'2020. Deposits per branch increased by 15.5% to Kshs 2.6 bn from Kshs 2.2 bn, as the number of declined to 129 in FY'2021 from 134 branches in FY'2020 after the Group closed 6 branches in Kenya, in order to reduce operational costs, but opened 1 branch in Uganda. In FY'2022, the Group plans on opening 20 more branches and an additional 20 by 2024, in a bid to expand their network coverage. Currently, the Kenyan subsidiary has 63 branches out of the Group's 129, representing 48.8% of the total,
- Loans to deposit ratio declined to 66.5%, from 70.0% in FY'2020, owing to the faster 11.2% growth in deposits, compared to the 5.7% growth in the net loans during the period,
- Gross Non-Performing Loans (NPLs) rose by 32.0% to Kshs 30.1 bn in FY'2021, from Kshs 22.8 bn recorded in FY'2020. Consequently, the NPL ratio deteriorated to 12.9% from 10.4% recorded in FY'2020, due to the faster 32.0% growth in gross NPLs which outpaced the 6.5% growth in gross loans,
- General Loan Loss Provisions increased by 17.8% to Kshs 11.4 bn from Kshs 9.6 bn in FY'2020. Consequently, the NPL coverage (having added interest in suspense) declined to 41.8% in FY'2021, from 44.6% in FY'2020, owing to the faster 32.0% increase in Gross NPLs, which outpaced the 17.8% growth in, general provisions,
- Shareholders' funds increased by 8.6% to Kshs 67.3 bn in FY'2021, from Kshs 62.0 bn largely due to the 7.6% increase in the retained earnings to Kshs 54.9 bn, from Kshs 51.0 bn in FY'2020,
- Diamond Trust Bank is currently sufficiently capitalized with a core capital to risk-weighted assets ratio of 19.9%, 9.4% points above the statutory requirement of 10.5%. Additionally, the total capital to risk-

weighted assets ratio was 21.2%, exceeding the 14.5% statutory requirement by 6.7% points. Adjusting for IFRS 9, the core capital to risk-weighted assets stood at 20.0%, while total capital to risk-weighted assets came in at 21.3%, and,

- The bank currently has a Return on Average Assets (ROaA) of 1.0%, and a Return on Average Equity (ROaE) of 6.8%.

Key Take-Outs:

1. **Asset Quality** - The bank's asset quality deteriorated, with the NPL ratio increasing to 12.9% in FY'2021, from 10.4% in FY'2020, due to the faster 32.0% growth in gross NPLs, which outpaced the 6.5% growth in gross loans. Notably, this is the highest it has been for more than a decade attributable to the faster growth in gross NPLs as opposed to the growth in gross loans. The increased NPLs can be attributed to the fact that the bank lends mostly to the trade, real estate, manufacturing and tourism sectors which are yet to recover from the pandemic effects. The four sectors contributed a total of 87.1% of their NPLs as of December 2021. Net loans increased by 5.7% to Kshs 220.4 bn, from Kshs 208.6 bn in FY'2020. The muted growth in the loan book is as a result of the bank's continuous selective lending to prevent further erosion of the asset quality,
2. **Operating Efficiency** - The bank's operating efficiency improved as evidenced by the decline in cost to income ratio to 75.6%, from 81.3% in FY'2020, which indicates reduced operational costs and improved operational efficiency. This can be attributed to the closure of six branches that were in close proximity to each other in a bid to reduce operational costs. However, the Group is set to open 20 more branches in Kenya in FY'2022 which is likely to increase the costs of operation. As such, we expect the bank to redesign their operational model as they restructure and restrategize in order to minimize on costs, and,
3. **Increased innovation and digitization** which saw 93.0% of all transactions of the bank being done on alternative channels, with mobile transactions taking up 88.0% of all transactions in FY'2021. In terms of the value of transactions, digital banking and ATMs contributed 96.5% and 3.5%, respectively.

Going forward, we expect the bank's growth to be driven by:

I. **Digital platforms** - The bank intends to expedite its digital transformation agenda and leverage on the strategy in improving their customer experience. Further, the Group is set to invest Kshs 3.5 bn in technology between 2022 and 2023 to expand its digital lending footprints, having already invested Kshs 2.4 bn between 2018 and 2021.

<u>Valuation Summary</u>

- We are of the view that Diamond Trust Bank Kenya is an **"ACCUMULATE"** with a target price of Kshs 64.8, representing an upside of 15.4%, from the current price of Kshs 58.8 as of 1st April 2022,
- Diamond Trust Bank Kenya is currently trading at a P/TBV of 0.2x and a P/E of 3.7x vs an industry average of 0.9x and 4.8x, respectively.