Tanzania Securities Limited
Stock Brokers | Investment Advisers | Fund Managers
MEMBER OF THE DAR ES SALAAM STOCK EXCHANGE

EQUITY RESEARCH
LOCAL LISTED BANKS

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Recommendation: MEDIUM TERM BUY/HOLD

We recommend a:

- **MEDIUM TERM BUY** on CRDB and NMB,
- **MEDIUM TERM HOLD** on DCB.

The three listed banks under study (CRDB, NMB, and DCB) have respective P/Bs valuations of 1.28x, 1.50x, and 1.20x. They are also trading on **trailing** P/Es of 7.22x, 6.47x and 6.28x respectively. We consider these valuations to be fairly attractive for the sector.

We continue to believe that the market might be too much focusing on the historical dividend payouts (especially for CRDB Bank) rather than the bank's profitability and future prospects.

We continue to believe that, in order to sustain and improve from current market price levels, the banks would need to continue to deliver strong profitability and maintain a good dividend payout

Relative Statics

PERx	NMB	CRDB	DCB
2011A	5.92	8.66	6.28
2012E	6.33	7.87	5.35
2013E	6.33	7.63	5.07
2014E	6.27	7.59	4.79
Div. Yield			
2011A	5.9%	6.0%	7.8%
2012E	5.6%	6.6%	9.0%
2013E	5.7%	6.8%	9.3%
2014E	5.9%	6.9%	9.7%
P/NAVx			
2011A	1.50	1.28	1.20
2012E	1.47	1.11	1.01
2013E	1.34	1.03	0.92
2014E	1.22	0.98	0.83

Source: NMB, CRDB, DCB Financials & Tanzania Securities Estimates

Our recommendations are also supported by strong balance sheets growth over the next 3 years (CAGR 20%) and profitability (CAGR 10%). We project reductions in cost-to-income to below 60% in FY14 (from the 63% in FY10). We estimate FY12 EPS of Tshs. 19.05, Tshs. 112.13 and Tshs. 158.05 on CRDB, DCB and NMB respectively.

Changes in Shares Prices

Bank	Current Prices	1month	3months	6months	1 year
NMB	930	870	850	850	830
CRDB	125	123	150	150	180
DCB	640	640	640	640	470

Bank	Current Price	%1 month	% 3 months	% 6 Months	% 1 year
NMB	930	6.9%	9.4%	9.4%	12.0%
CRDB	125	2.0%	-16.7%	-16.7%	-30.6%
DCB	640	0.0%	0.0%	0.0%	36.2%

Source: Tanzania Securities Analysis – as of June 30th 2012

We expect CRDB, DCB and NMB to continue to generate >10% earnings growth over the medium term based on the CAGR 10% recorded over the past 5 years, the prevailing financial and economic situation in the country, and, future business outlook.

This level of profitability will be derived from both funded and non-funded transactions. The ongoing system modernization and expansion programmes, innovation, cost and debt management, capitalization, and other measures taken by banks, will continue to favourably affect income and business volumes.

Our stance on the sector remains **a bullish medium term** view on Tanzanian economy. Improvements in the money and credit markets will continue to drive up the economic outlook for the rest of 2012. We also anticipate an easing out of the liquidity squeeze that, when combined with an improving local currency and other factors, will positively impact the banking sector in the country.

Our projections support continuity in growth trend and levels for 2012/2013 sustained by reductions in risks and funding costs. We continue to believe that the sector's ROTE 2014E will increase. We project an increase of up to 25% from 23% in 2010.

Based on the new Basel III proposals Tier I capital for the banks, we project that all three banks are in line to meet or exceed this requirement by FY 2013. Over the medium term, we project the Tier I capital for the banks to increase three fold from the current (lowest) Tshs 5 billion to Tshs. 15.

We believe (basing on our model, data, and analysis) that two of the listed banks – CRDB and NMB are overcapitalized, with core capital 2012E Tier I ratios of 24% and 20% respectively. DCB will still require recapitalization of up to Tshs. 3 billion to be in a position to meet or exceed its projections.

Sector Key Statistics

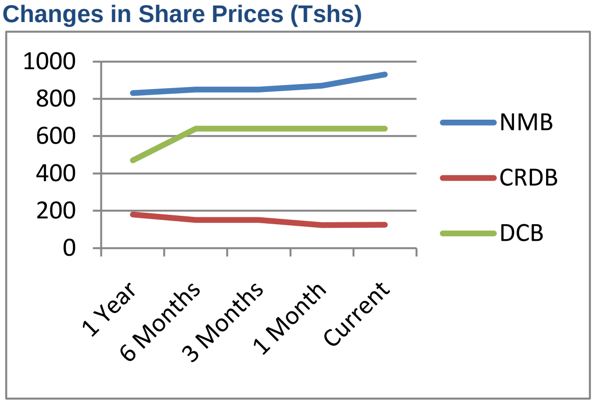
Key Statistics	NMB	CRDB	DCB
Price	850	150	640
Number of shares mn)	500	2,177	32
Market Cap (Tshs.bn)	425	326	20
EPS (Tshs.)			
2011A	144	17	101
2012E	158	19	112
2013E	174	21	123
2014E	191	23	136
DPS (Tshs.)			
2011A	50	9	50
2012E	56	10	54
2013E	63	11	58
2014E	70	12	63
NAV (Tshs.bn)			
2011A	284	255	17
2012E	341	293	19
2013E	409	337	22
2014E	491	387	25

Source: NMB, CRDB, DCB Financials & Tanzania Securities Estimates

Loan impairment measures of over Tshs. 50 billion (mostly by CRDB) recently taken by the banks continue to pose challenges to the sector. Even as we don't expect a substantial rise in NPL's in the immediate future, we still consider this to somehow affect banks' performances in the short term.

We however consider actions taken by banks to clean up their books to have a positive impact in the long run as banks will position themselves better to meet similar challenges that might arise in the future. Our 3 year CAGR in the profitability till 2014E for the banks stands at 10%, this could easily outweigh negative impact from the loan impairment measures and thus, providing attractive **buying opportunities**.

Changes in Share Prices (Tshs)



Source: DSE and TSL Analysis

We also see rising business and income volumes, improving economic outlook, a focused and innovative management (especially on growth for both assets and profit), an improving cost-income ratio, and growing non-funded income.

We therefore recommend a **BUY for NMB** at Tshs. 850.00 – Tshs. 950.00, **CRDB** at Tshs. 120.00 – Tshs. 175.00, and, a **HOLD for DCB** at prevailing prices of between Tshs. 600.00 and 650.00.

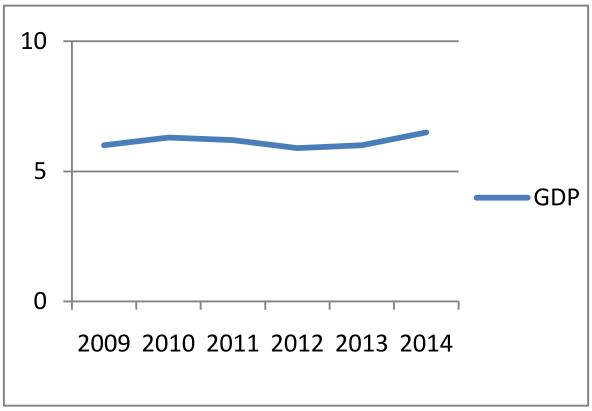
Macroeconomic Update

Economic Growth Outlook

Strong domestic demand should support growth through 2012 despite double-digit inflation and power outages. We are expecting domestic demand to remain the main driver of growth in 2012 in spite of higher than normal food prices.

In addition, gold production has increased substantially since the opening of the Buzwagi mine in June 2009, and, mining is likely to continue to underpin GDP growth despite the power rationing imposed by state-owned utility Tanesco in 2011.

GDP Movement (%)



We expect fiscal and monetary policy to remain on the stimulative side in 2012 although the authorities are likely to gradually move towards rebalancing economic policy in tandem with rising inflation.

We are expecting economic growth that slowed to around 6% in 2011 to pick up somewhat in 2012. GDP data for the first half of 2011 indicate that economic activities slowed more radically than expected. This was particularly the case with agricultural growth, which slowed to 3.2% in the first half of 2011 after a strong 5.7% expansion in the second half of 2011.

The manufacturing sector has also slowed down in the first half of 2012 to 5.5%, from 11.9% in the second half of 2011. The National Bureau of Statistics partly attributes this slowdown to an unreliable power supply in the second quarter. Projections for the rest of the year will be the same as we continue to expect power cuts resulting from poor water levels in hydropower reservoir.

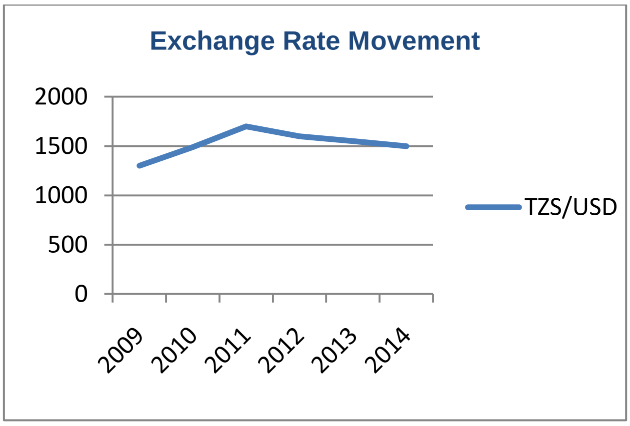
Even as most of users are switching to alternative sources of energy (thermal power and likes), the situation will continue to be affected by higher oil and gas prices in the country. This scenario was one of the factors considered in the reduction of the GDP growth forecast for 2012 from 6.3 to 5.9.

While the near-term growth picture remains robust, we caution that Tanzania faces challenges in maintaining its current growth rates (GDP growth averaged 6.5% over 2000–11). These are primarily found in removing the constraints on economic growth found in infrastructure, mainly power generation and distribution. Tanzania also needs to do more to raise its economic competitiveness through improving governance and the business environment.

If these issues are not sufficiently addressed, which is our base-case scenario; we then expect a slowing in economic growth in the coming years. We are currently forecasting GDP growth to average 6.1% in 2011 through 2015, roughly a percentage point lower than the expansion rate in 2001–10. However, limited integration with global financial markets and Tanzania's status as an oil importer and a gold exporter make it fairly well insulated to another downturn in global economic growth.

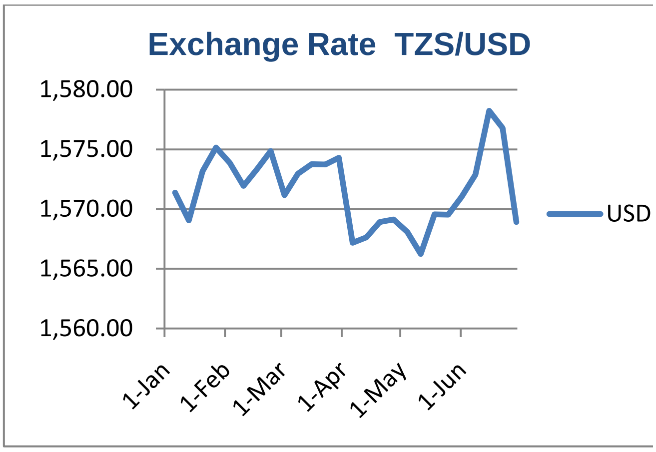
Exchange rates

The Tanzanian shilling, like its regional peers, came under pressure in the first half of 2011 due to political unrest in the Middle East and North Africa, raising risk aversion and the global oil prices.



The situation has recently started (especially in the second quarter of 2012) to improve as the shilling has been gaining against various foreign currencies (including the dollar).

While the shilling has historically held up well compared with some of its emerging market peers, it remains vulnerable to shifts in investor appetite due to Tanzanian's high current-account deficit, which is likely to increase in tandem with the higher oil price, and higher dependence on the unreliable/unpredictable farming based economy.



We expect the Tanzanian shilling to hold steady for the remainder of 2012. We believe that, the slight downtick movement in the prices and inflation in a whole in recent months will continue to hold for the rest of the year.

The current account deficit however, remains a weakness to the overall economic performance, leaving Tanzania reliant on foreign aid and investment inflows.

We are expecting Tanzania's current-account deficit to remain above 10% of GDP in both 2012 and 2013, which will mean that the Tanzanian shilling will remain vulnerable to interruptions in aid and investment inflows. Investment into the mining and energy sector should bolster the balance of payments in the medium term.

Monetary Policy

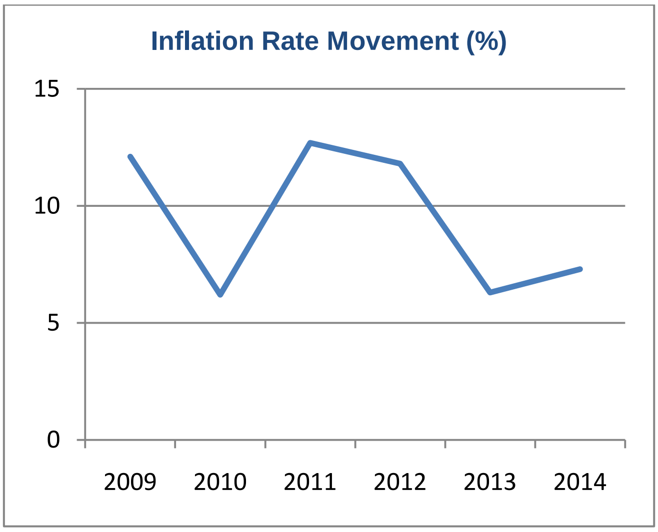
The Central Bank of Tanzania continued to pursue broad-based monetary measures trying to curb the higher than normal inflation rates, and easy out liquidity squeeze that affected the economy and financial/credit markets for most of the Q1 2012. Even though some might argue that these measures have done little to help out the situation, but, there seems to be improvements of the economy as a whole.

Even though, the International Monetary Fund has stated that it will support the external sector's stability, which should help ease some concerns about the shilling and economic outlook, the medium-term trend for Tanzanian shilling will be determined by the maintenance of a positive outlook for the external sector and the steady return of foreign direct investment and aid flows to emerging markets, as well as good performance in the tourism, mining, and agricultural sectors. In addition, Tanzania's stable political environment and reform program should bolster the long-term currency outlook.

Effectiveness of these measures is still limited and minimal, given the nature of the financial structures in the country, in addition to the underdeveloped structure of the banking sector. Monetary policy remains focused on managing liquidity conditions to decrease the volatility resulting from inflows and outflows of foreign exchange. However, the development of a commercial banking sector over the past two decades has considerably improved credit availability for the private sector and underpinned the strong economic growth rates experienced in recent years.

Inflation

We expect consumer price inflation to remain in double digits well into 2012. With projections from the Bureau of Statics showing stronger-than-expected impetus to food prices, expectations are higher that consumer price inflation would very likely fall in December.



While seasonal factors should see food-price inflation ease out over the coming months, we expect consumer price inflation to remain in the high teens on the back of the pricing-in of higher utility prices and sustained demand-side pressures.

The consumer price index (CPI) slightly fell to 18.2% in May 2012. This was slightly down from the yearly high of 19.2 in March 2012. The inflation rate for April 2012 was 18.9%. **The National Bureau of Statistics (NBS) switched its methodology from a simple-average to a geometric-means method as of October 2010,** which should see consumer price inflation come in at lower and less-volatile rates in the medium term. The collective change in consumer price index calculation is aimed at harmonizing and improving statistical methods across the East African Community as part of a wider move toward regional integration.

This also included changing the index's weights, base prices, and sub-index baskets to align them more with modern consumption preferences and patterns. The new method is likely to facilitate monetary policymaking for the Bank of Tanzania going forward.

Overall, we expect consumer price inflation to improve towards the end of the year. We are expecting oil and energy prices to hold steady or slightly fall as we are expecting food prices to go down as the spring harvest continue to come to market. Food-supply conditions acted as a disinflationary force during most of the second half of 2010 and 2011 on the back of good rains during the summer harvest period will continue to help out the situation.

The Banking Sector

Today, according to BOT, the banking sector has 45 banks and financial institutions (29 commercial banks), with a combination of subsidiaries of international banks, large domestic banks, and smaller typically domestic, banks. In additional there are non-bank financial institutions. Smaller clients are served by more than 650 savings and credit cooperatives and large number of microfinance institutions.

Despite its diversity, however, the Tanzania financial sector is largely concentrated in the commercial banking and is very small. With the capital adequacy of over 20% and limited lending activities, banks in Tanzania are generally well-capitalized and are expected to be resilient to shocks of credit quality. Their weakest area is a considerable exposure to interest-rate risk, resulting from large government securities holding. The interbank market, trading at a low of 6% to 13% of broad money, remains underdeveloped.

The total industry balance sheet grew at a CAGR of 20% in the past five years (2007-2011).

Tshs. Billion	2007	2008	2009	2010	2011	CAGR
Loan & Advances	2,833	4,163	4,534	5,485	7,100	26%
Government & Debt Securities	1,603	1,549	1,719	2,442	2,030	6%
Balances with other banks	1,259	1,114	1,459	1,857	1,932	11%
Other assets	1,209	1,451	2,105	2,581	3,220	28%
Total	**6,904**	**8,277**	**9,817**	**12,365**	**14,282**	**20%**

Over 80% of the banking assets are funded by client deposits.

NMB and CRDB represents 34% of the total banking sector assets: NMB accounts for 15% (Tshs. 2,170 billion, December 2011) and CRDB accounts for 19% (Tshs. 2,713 billion, December 2011).

There is already a substantial liquidity in the system, but these funds tend to be held unevenly, with some banks (i.e. NMB, CRDB) holding the bulk of it and others experiencing shortages. Despite some successful financial-sector reforms, the banking industry tends to play only a small role in the country's economy – despite the sector wealth balance sheet, providing very limited and mostly short-term credit. Payment services are underdeveloped, particularly in rural areas.

The relatively large number of commercial banks within the Tanzania banking sector has resulted in aggressive competition, price wars that have sometimes involved undercutting on price and contracting interest spread. At the same time, larger banks are being squeezed on both lending and deposit rates as mid tier banks gain market share and use of pricing as a competing tool for deposits with alternative investment products such as money market instruments, equity investments, collective investment schemes i.e. unit trusts, fixed income instruments, property and other forms of investments.

Over the past five years, the banking sector has recorded substantial growth in income and earnings – the sector has recorded a 16% CAGR on income received over the past five years and 3% (sharply down from the 10% by the end of last year) CAGR on the earnings generated over the review period.

The table below depicts income and earnings results from 2006-2011:

Tshs. Billion	FY2007	FY2008	FY2009	FY2010	FY2011	CAGR
Total Income	829	941	1,110	1,282	1,511	16%
Gross Income	648	757	832	975	1,190	16%
Net Earnings	209	209	217	197	231	3%

Observations

The sector's solvency is satisfactory. We believe that solvency should not be a major source of concerns to investors. On our estimates NMB and CRDB still do not have to implement any measures to reach a level of solvency as proposed for Basel III compliance. However, we believe that in the medium term, small and medium sized banks will start to discuss capital raising opportunities more aggressively. However, we note that large-scale M&A transactions involving significant goodwill payments are unlikely for some time.

We believe that the regulatory changes should have only a moderate impact rather than extreme share price volatility though we may be too optimistic too soon. Following a re-run of the regulatory impact we now believe that Basel III will be much less costly than previously anticipated.

We view the economic background as supportive, given that the current yield curve, low real short term rates, and improving lead indicators, as well as current lending criteria are supportive of stronger not weaker growth. These, in turn, would improve asset values and potentially increase earnings development for the sector.

Despite the underlying pessimism in the market and bank's inability to outperform investors' expectations in delivering profits and dividends -- we see these uncertainties as opportunities to reinforce a **BUY or HOLD** option. Our opinion is that NMB and CRDB shares are still attractive and call for a **BUY** recommendation. With DCB, we are calling for a **HOLD** right now while the bank work on its capitalization plans.

National Microfinance Bank ("NMB")

Recommendation: MEDIUM TERM BUY

Executive Summary

We recommend a **MEDIUM TERM BUY** on NMB at a price of Tshs. 900 with up/down side of 10%. Despite the high earnings growth potential and its recent price fall, with a 2011A PER of 5.9x, NMB trades at the sector's average PER of 6.7x 2011A.

Key Statistics

	FY2008	FY2009	FY2010	FY2011	CAGR
Number of shares (Mn)	500	500	500	500	
Pre-tax profit (Tshs. Mn)	70,935	68,038	78,445	102,786	13%
Profit after Tax (Tshs. Mn)	48,707	47,550	53,981	71,839	14%
Dividend (Tshs. Mn)	15,000	15,700	18,000	25,000	19%
Market Capitalization (Tshs. Mn)	485,000	395,000	330,000	425,000	-4%
Net Assets value (Tshs Mn)	140,933	192,239	230,519	284,000	26%
Price per share (Tshs.)	970	790	660	850	-4%
Book value per share (Tshs.)	282	384	461	568	26%
Earnings per share (Tshs.)	97	93	108	144	14%
Dividends per share (Tshs.)	29	31	36	50	20%
Price Earnings Ratio	10.00	8.53	6.11	5.90	-16%
Dividend Yield	3.0%	4.0%	5.5%	5.9%	25%
Dividend Payout Ratio	31%	33%	35%	35%	5%
Price book value	3.44	2.05	1.43	1.50	-24%

Source: NMB Financials and TSL Analysis

NMB continues to offer a combination of solvency, low funding costs, moderate exposure to risks and an appealing valuation, in our view – we believe that market participants do not reward the quality and caution of the bank's management. NMB trades at a discount to its peers in the NSE.

The bank has a very interesting presence (over 140 branches – present in each district in the country and over 400 ATMs) in the market with positive long term fundamentals and it is generating enough cash to comfortably pay 2011A 5.9% dividend yield and still finance its network expansion and modernization

NMB's strategy to offer a full range of banking services to the lower end has proven resoundingly successful and resulted in unprecedented growth. This is backed by the banks innovative strategy complemented by technology. The next phase of growth will be driven by product diversification and operating efficiencies as the bank's economies of scale continue to pay off. Further expansion will also impact profitability significantly over the medium term.

Following the recent share decline across the sector and the market, valuations look compelling. A consistent earnings growth story backed by a wider branch network, increase in loan book, a low funding cost and optimal utilization of capital despite a short term non-compelling dividend payout forms a basis for our bullish outlook of this bank. The 3 year CAGR for dividends is expected at 10% as the expansion starts yielding results.

	FY2012E	FY2013E	FY2014E
Number of shares (Mn)	500	500	500
Pre-tax profit (Tshs. Mn)	115,120	128,935	144,407
Profit after Tax (Tshs. Mn)	80,584	90,254	101,085
Dividend (Tshs. Mn)	28,000	31,360	35,123
Market Capitalization (Tshs. Mn)	500,000	550,000	600,000
Net Assets value (Tshs. Mn)	340,800	408,960	490,752
Price per share (Tshs.)	1,000	1,100	1,200
Book value per share (Tshs.)	682	818	982
Earnings per share (Tshs.)	158	173	191
Dividends per share (Tshs.)	56	62	70
Price Earnings Ratio	6.33	6.33	6.27
Dividend Yield	5.6%	5.7%	5.85%
Dividend Payout Ratio	35%	36%	37%
Price book value	1.47	1.34	1.22

Source: TSL Analysis Estimates

NMB offers a combination of solid solvency (even after Basel III proposals implementation), low funding cost, moderate exposure to risks and appealing valuation, in our view. We believe that market participants do not reward the quality and risk caution of the bank's management. We also believe that its resilience in the event of a financial sector crisis would be strong.

FY2011 results highlighted a strong performance in the bank's activities, the resilience of the commercial division thanks to the MSMEs, agribusiness and corporate business, and a significant positive surprise in the corporate centre which we view as sustainable. In our view, NMB is reaping the benefit of having a wider branch network, innovation, its recent systems modernization and a strong funding source. On our forecasts, the bank's TE should continue to grow >5% per annum over the next 3 years.

Downward risks to our bullish outlook include a protracted period of high inflation and rising cost pressures that could erode revenue growth and domestic private consumption. Further, if economic growth does not pick up pace, rising loan defaults on both the corporate and retail end could dampen profitability growth prospects. We also note that the ongoing bank's IT infrastructure upgrade will work effectively so as to compete effectively with peer banks. We hold the view that technical innovation and good customer services will ultimately become a key selling point for retaining and gaining customers.

Key Themes

Growing Network – Continued Focus on MSMEs

We expect NMB to generate >10% profits growth over the medium term. This level of profitability is derived from a dominant position in the Tanzania banking market.NMB contracts with the government of Tanzania to be a medium of salaries and wages payments also continues to serve the bank favourably. With branches all across Tanzania, the bank is poised to increase its innovation, distribution and branch network to its core MSMEs clientele base.

The bank has plans to increase the number of branches to bring the number up to 200 branches by 2012. The motivation behind branch expansion is to increase and consolidate the bank's retail reach, which also forms a good base of its low cost funding. We note that there is a steep competition in this area particularly from CRDB and to a lesser extent Barclays and NBC.

NMB at the Threshold of Innovation

NMB has made a lot of positive leaps since 2003, where the business orientation was reshaped. Its diversification into corporate banking and agribusiness financing compounded with innovative and diversified scenarios to compete with the corporate clientele focused and more innovative foreign subsidiaries banks – the bank has been able to significantly gain its market share into the new segments. With a recent refocus in developing new products i.e. NMB Mobile, and the current upgrade of its core banking software to allow increased functionality, automation, cross selling of products, automation, and provision of e-banking and other valued services – the bank is well positioned to consolidate its market share increase shareholders' value in the near future.

With its large branch network and a focus in rural areas, NMB is positioned to maximize on the Government's policy initiative in agriculture (KILIMO KWANZA). The bank continues to serve the agricultural sector particularly sugar cane, paddy growers, barley and tobacco farmers. NMB is also in collaboration with AGRA and FSDT in financing agro dealers. The bank's NFAD project financed by Rabobank Foundation which focuses in financing commercially viable agro-based cooperatives and improving management and technical/financial capacities is a commendable initiative towards playing a leading role in the agro-business financing.

Capital Retention

The bank's major source of funding its expansion plans has traditionally been retained reserves, the bank has increased earnings retention with dividend payout average 33% over the past three years ('08 to '10). The motive behind this is to raise capital to match its medium to long term lending. NMB operates on relatively loose liquidity and strong capital adequacy framework relative to its peers, the bank offers a combination of solid solvency even after Basel III proposals, low funding cost and a moderate exposure to risks.

The Future Outlook

Through its innovative distribution and extensive branch network, NMB focus on service delivery is underpinned in the following key themes:

- Innovation – for alternative banking channels and customer outreach
- Good customer services – for competitive edge
- Interest rate squeezing – competitive pressure
- Expansion – for less costly funding source

Key Risks

In our view the three key downward risks that investors have to contend with are:

- **Operational Risk**: With the fast pace of growth both in network, business volumes, innovation and technology enhancement; NMB faces execution and operational risk. We, however, note that the bank has engaged the consultant to review and assist in the implementation of its ICT platform. The bank has also increased its staff compliment commensurately with the pace of growth in the network.
- **Credit and default risk** is also a concern. Historically the bank loan loss has been below the sector mean as the bank has benefited from the low magnitude of NPL's over a number of loans and also the bank's model of financing MSMEs through the SACCOs and its microfinance subsidiaries.
- **Contractual risk**: there are speculations that the Government may pull out its accounts with the bank and start using the Central bank's (BOT) branch network – if the proposal materializes, it will have a significant impact on the bank's low cost funding source and thus its underlying returns to shareholders.

CRDB Bank PLC ("CRDB")

Recommendation: MEDIUM TERM BUY

We recommend a medium term **BUY** on the CRDB at a price of 150 with up/down side of 20%. Our bullish outlook is based on a promising future outlook, successful continuance expansion strategy, innovative approach to business development, and product diversification.

Despite recent significant NPL and loans impairments provisions (to the tune of Tshs. 60 billion) in the last three years, in our view, CRDB continues to be a good example of a bank that has resiliently managed to deal with the 2008/09 loan crisis and recent revealed more loan/booking losses the bank may write-off more debts than previously projected. The bank's future projections and expansion plans, in addition to its current healthy balance sheet, excellent liquidity, strongly capitalization and low leverage and moderate loan-to-deposit ratios, are making a very good case for the counter.

The bank's implementation of its two prolonged strategies that sought to generally improve services and the image of the bank – improving services & offering customers convenience, innovative, alternative delivery channels for fulfilling customers demands and increase its market share. The bank's market share of sector assets is grew to 19% by FY2011A relative to 16% in 2010A and 18% 2009A, making it being one of the largest and fastest growing banks in the sector. The growth is expected to be driven by rapid branch and network expansion plans, coupled with innovation and upgrading of its ICT systems – the bank plans to have a branch in each district in Tanzania over the next three years.

The bank has a substantial presence in markets (using its network, SACCOs and Microfinance subsidy) with positive medium and long term fundamentals; it has generated enough cash to pay a 2011A 6.0% dividend yield.

Financial highlights 2007-2011

	FY2007	FY2008	FY2009	FY2010	FY2011	CAGR
Loan & Advances	588,347	836,803	949,505	1,123,348	1,429,262	25%
Government securities	120,428	205,720	252,977	426,546	493,735	42%
Other Assets	433,894	407,278	652,197	755,508	790,644	16%
Total Assets	1,142,669	1,449,801	1,854,679	2,305,402	2,713,641	24%
Deposits	1,015,071	1,276,433	1,624,795	2,036,224	2,411,577	24%
Interest income	89,145	110,287	143,319	156,685	188,357	21%
Interest expenses	(17,007)	(20,846)	(35,925)	(35,511)	(34,972)	20%
Loan impairment	(3,229)	(5,019)	(18,173)	(20,357)	(31,216)	76%
Other income	37,993	43,489	54,079	68,339	57,363	11%
Operating expenses	(55,199)	(68,147)	(81,428)	(106,067)	(130,657)	24%
Net earnings	37,325	40,257	47,583	46,355	36,322	-1%

CRDB is looking at three growth avenues to cushion its assets base and earnings, especially in light of increased competition in the high volume wholesale banking and the SME market. The bank wants to push growth in the retail market and increase the small and medium sized loan book, achieve low cost of funding as well as higher consumer banking commission income. The strategy is critical to the bank because its earnings growth in 2010 slowed compared with 2009 when the bank outperformed the sector.

EPS stood at Tshs. 17 in 2011, a sharp drop from the Tshs. 22 in 2010. We forecast a Tshs. 19 EPS 2012E, meaning a higher growth rate this year – which is in line with the bank's profit of Tshs. 50 billion 2012E. Lower yields in government papers, which account for 23% of the total interest earning assets, have slowed due to a drop in interest rates. The drop is one of the reasons CRDB want to make a big push for expansion in its retail banking outreach.

Key Statistics

CRDB Bank PLC	FY2008	FY2009	FY2010	FY2011	CAGR
Number of shares (Mn)	2,175	2,175	2,175	2,177	
Pre-tax profit (Tshs. Mn)	60,005	61,922	64,134	51,013	-5%
Profit after Tax (Tshs. Mn)	40,257	47,583	47,246	37,710	-2%
Dividend (Tshs. Mn)	4,253	15,928	17,432	19,589	66%
Market Capitalization (Tshs. Mn)	485,000	255,743	250,125	326,480	-12%
Net Assets value (Tshs Mn)	140,932	207,774	240,922	254,764	22%
Price per share (Tshs.)	220	120	115	150	-12%
Book value per share (Tshs.)	65	96	111	117	22%
Earnings per share (Tshs.)	22	17	22	17	-8%
Dividends per share (Tshs.)	2.2	5.9	8.1	9.0	60%
Price Earnings Ratio	10.26	6.95	5.18	8.82	-5%
Dividend Yield	1.0%	5.0%	7.1%	6.0%	82%
Dividend Payout Ratio	11%	33%	37%	53%	69%
Price book value	3.44	1.23	1.04	1.28	-28%

Source: CRDB Financials and TSL Analysis

In 2011, the bank continued to work on execution of the Bank five year business strategy which included the rollout of the new Core Banking System (Bank Fusion-Universal Banking). This enabled the bank enhance its service delivery efficiency and also complete the rollout of centralising back office transactions.

The bank's strategy rests on portfolio diversification and retail banking with a focus on loans, liquidity, assets quality and risks and costs management. Downside risks to our projections include execution risk given the accelerated pace of growth, exposure to credit risk and growing non performing loans as well as a significant drop in commissions and lending rates that could impact profitability as competition intensifies.

CRDB Bank PLC	FY2012E	FY2013E	FY2014E
Number of shares (Mn)	2,177	2,177	2,177
Pre-tax profit (Tshs. Mn)	71,595	78,755	86,630
Profit after Tax (Tshs. Mn)	50,117	55,128	60,641
Dividend (Tshs. Mn)	21,550	23,700	26,100
Market Capitalization (Tshs. Mn)	326,550	348,320	380,975
Net Assets value (Tshs. Mn)	292,980	336,930	364,495
Price per share (Tshs.)	150	160	175
Book value per share (Tshs.)	135	155	178
Earnings per share (Tshs.)	19	21	23
Dividends per share (Tshs.)	10	11	12
Price Earnings Ratio	7.87	7.63	7.59
Dividend Yield	6.6%	6.8%	6.9%
Dividend Payout Ratio	52%	52%	52%
Price book value	1.11	1.03	0.98

Source: TSL Estimates

Key Growth Drivers

Innovation and Underpenetrated Market

Following the rapid expansion and growth in scale and volumes, the bank is poised for a strong future growth. Sustained growth and enhancement of the retail services capabilities by opening of new branches will, in our opinion, outweigh dismal 2011 financial performance. Future projections of its balance sheet, profitability, and costs are within acceptable levels. For now, the bank will "bank" on its future to guide and sustain it present.

The bank continues to implement changes to its technology, upgrade its communication -- it is implementing system based changes geared towards centralising back office transactions and upgrading its core banking system. The bank's microfinance subsidiary also increased its network of partners to over 472.

The bank's business model of reaching the lower end retail and SME base through SACCOS and microfinance subsidiaries has given it the scale to take advantage of under penetration of the bankable population. CRDB enjoys a competitive edge in the retail & SME segment by virtue of increasing presence in key deposit taking urban, peri-urban areas, and rural centres and offering easy access to banking products. However, competitors such as NMB, NBC, microfinance institutions, SACCO's and other mainstream commercial banks targeting the retail space are becoming stronger.

On the SME side, the bank has been able to successfully reach this market segment through its SACCOs and Micro finance Service Company. The bank plans to increase its SACCOs network from the current 200 to over 500 in 2015. However, in a view of increasing its outreach and access less costly sources of funding, the banks has embarked in aggressive branch network expansion strategy and is also encouraging and attracts customers to deposit in low cost accounts i.e. savings and current accounts.

Adapting to a changed environment

CRDB, in general hold healthy balance sheet, enjoy excellent liquidity and is strongly capitalised – with low leverage and moderate (current and projected) loan-to deposit ratios.

The spillover from the global financial crisis and the resulting recession - - for CRDB was not significant or destabilising as was in other emerging economies. By contrast, the bank remained stable, despite impairment of assets quality caused by weaknesses waning commodity prices and the slowdown in direct investment in the agricultural, tourism and manufacturing sectors.

The bank's lending margins reduced marginally on both foreign and local currency lending. Trade financing also became a little expensive and hard to source – with soaring interest rates and confirmation fees for LCs and bank guarantees. There were some cases where the bank required LCs to be cash collateralised. Despite this, in our view, CRDB is a good example of a bank that has resiliently managed to deal with the crisis and has good future potential – but which has not yet been given credit for this by the market.

Key Risks

In our view the three key risks that investors have to contend with are execution risk, credit risk and default risk.

With the fast pace of growth both in network, business volumes, innovation and technology enhancement, CRDB bank faces significant execution and operational risk. We, however, note that the bank has been increasing staff numbers commensurately with the pace of growth in the network. Further, the bank's core banking system (Bank Fusion- Universal Banking) has been designed specifically for banks with a high volume business model; the system/software is both flexible and scalable.

Credit and default risk is also a concern. Historically the bank loan loss has been below the sector mean as the bank has benefited from the low magnitude of NPL's over a number of loans and also the bank's model of financing MSMEs through the SACCOs and its microfinance subsidiaries. However, the bank's impairment charges increased significantly in recent years.

Dar es Salaam Community Bank ("DCB") ➔ DCB Commercial Bank

Recommendation: MEDIUM TERM HOLD

We recommend a **medium term HOLD** on DCB. The bank has recently been converted from a community bank to a commercial bank (thus changing its name to DCB Commercial Bank). The changes are part of the effort by the bank to become a fully fledged commercial bank while also expanding outside Dar es Salaam – its original (and previously only) base.

Changing to commercial banking status, has inevitably necessitated the bank to increase its capital (to meet BOT requirements) while also expanding its presence. This has led to different capitalization schemes now contemplated by the bank. For example, even though the bank had announced a TZS 50 per share cash dividend to its shareholders in April, it has recently reversed itself to announce a BONUS dividend per share.

The bank is also finalizing plans for right issue to be done in the near future. Despite its above average past performance and dividend payout policy, we are recommending a **HOLD** status while studying closely how the bank will handle all these changes coming already in the pipeline.

DCB is trading at FY11A price earnings ratio of 6.3x with attractive valuation with P/B of 1.2x - DCB currently trades on a trailing P/B and P/E of 1.2x and 6.3x, which we view as attractive in the sector. DCB also has an attractive dividend yields of 7.8% (a sharp drop though from last year's 17.1%)

Key Statistics

	FY2008	FY2009	FY2010	FY2011	CAGR
Number of shares (Mn)	32	32	32	32	
Pre-tax profit (Tshs. Mn)	2,320	2,484	4,364	4,437	24%
Profit after Tax (Tshs. Mn)	1,417	1,484	3,166	3,262	32%
Dividend (Tshs. Mn)	648	907	1,555	1,600	35%
Market Capitalization (Tshs. Mn)	11,340	9,232	9,070	20,480	22%
Net Assets value (Tshs Mn)	11,363	12,559	14,818	16,525	13%
Price per share (Tshs.)	350	282	280	640	22%
Book value per share (Tshs.)	351	388	457	531	15%
Earnings per share (Tshs.)	44	54	99	101	32%
Dividends per share (Tshs.)	21	28	48	50	34%
Price Earnings Ratio	7.95	5.26	2.94	6.37	-7%
Dividend Yield	6.0%	9.0%	17.1%	7.8%	9%
Dividend Payout Ratio	46%	49%	49%	50%	3%
Price book value	1.00	0.74	0.61	1.20	6%

Source: DCB Financials and TSL Analysis

In the medium term, we **remain cautious** of the measures and changes currently implemented by the bank. We are closely monitoring the capitalization process currently undertaken by the bank. We don't anticipation major shifts in the performance of the bank even as we still remain optimistic and positive about the long term situation.

The banks' future looks strong, prospects of expanding to other regions in the country should play along with current plans of pursuing less costly deposits (savings and current) over its current expensive time deposits. We still expect the bank to install and/or increase its branch network and/or ATM machines to match the overall expansion strategy.

	FY2012E	FY2013E	FY2014E
Number of shares (Mn) – without right issue***	32	32	32
Pre-tax profit (Tshs. Mn)	4,791	5,175	5,589
Profit after Tax (Tshs. Mn)	3,523	3,805	4,109
Dividend (Tshs. Mn)	1,728	1,866	2,016
Market Capitalization (Tshs. Mn) – without right issue***	19,200	20,000	20,800
Net Assets value (Tshs. Mn)	19,004	21,854	25,132
Price per share (Tshs.) - anticipating right issue	600	625	650
Book value per share (Tshs.)	594	683	785
Earnings per share (Tshs.)	112	123	135
Dividends per share (Tshs.)	54	58	63
Price Earnings Ratio	5.35	5.07	4.79
Dividend Yield	9.0%	9.3%	9.7%
Dividend Payout Ratio	48%	47%	46%
Price book value	1.01	0.92	0.83

Source: TSL Estimates

In relation to the new Basel III proposals for capital adequacy, the bank's current capital solvency (currently at Tshs. 9 billion) is still unsatisfactory. We therefore still expect DCB management will target the Tshs. 15 billion core capital solvency requirement in the medium term even if BOT doesn't enforce the rule. According to our estimates, DCB still have to implement measures to reach a level of implied solvency we would view as solid enough.

Key risks to our moderate outlook on DCB include structural limits due to its geographical location, struggles with long term sources of financing and planned long term projects, delays in network expansion and ATM installation, and, complicated expansion and capitalization program. Credit and default risk is also a concern.

Key Earnings Drivers

We expect DCB assets to grow at a 3 year CAGR of 30%. Deposits are expected to drive balance sheet growth with commensurate 3 year CAGR of 30%. Interest income growth (CAGR 29%) in the last four years will very likely be sustained by the banks. Customer deposits growth will continue to be driven by economic growth and business expansion.

	2007	2008	2009	2010	2011	CAGR
Loan & Advances	21,243	28,665	41,167	55,987	57,440	28%
Government securities	7,668	6,182	7,288	11,150	10,848	9%
Other Assets	5,612	13,003	23,382	28,076	31,070	53%
Total Assets	34,523	47,850	71,837	95,213	99,358	30%
Deposits	28,498	35,143	55,767	79,166	81,107	30%
Interest income	6,174	8,881	10,211	14,654	17,314	29%
Interest expenses	(2,041)	(2,321)	(3,744)	(5,468)	(5,881)	30%
Loan impairment	(141)	(924)	(674)	(945)	(532)	39%
Other income	560	702	1,333	1,776	1,263	23%
Operating expenses	(2,267)	(4,020)	(4,641)	(5,793)	(7,726)	36%
Net earnings	1,339	1,417	1,844	3,166	3,261	25%

DCB's cost of deposit at 7% is higher than the industry average rate and higher than the other two banks listed in the stock market. We expect this to change in the immediate future as the banks implement its measures for cheaper deposit sources in the long term.

The bank's focus on lending remains strong on the retail based and lending to Micro, Small and Medium Enterprises (MSMEs) and solidarity groups. It has also participated in unsecured lending to salaried employees. As with other banks, in order to control credit risk, interest and principal are deducted from salaries.

With low returns on government securities, the bank shown fresh appetite for the personal salaried loan market seen as the next frontier of growth in the medium term – especially with the recovery and optimism in business rebound has booted workers' willingness to take up loan.

Going forward, increased stable deposits, capitalization, expansion, and introduction of new products i.e. DCB diversification to the housing microfinance space and establishment of the corporate banking is likely to be a significant long term drive of the loan book.

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