Stanbic Holdings – FY’2022

10th March, 2023

Below is a summary of Stanbic Holding’s FY’2022 performance:

Balance Sheet	FY'2021	FY'2022	y/y change
Net Loans and Advances	229.3	266.8	16.4%
Government Securities	40.6	58.0	42.9%
Total Assets	**328.9**	**399.8**	**21.6%**
Customer Deposits	254.6	304.3	19.5%
Deposits Per Branch	9.8	10.1	3.6%
Total Liabilities	**272.4**	**337.6**	**23.9%**
Shareholders' Funds	**56.5**	**62.2**	**10.2%**

Key Ratios	FY'2021	FY'2022	% point change
Loan to Deposit ratio	90.1%	87.7%	(2.4%)
Return on average equity	13.3%	15.3%	2.0%
Return on average assets	2.2%	2.5%	0.3%

Income Statement	FY'2021	FY'2022	y/y change
Net interest Income	14.4	18.9	31.8%
Net non-interest income	10.6	13.1	23.7%
Total Operating income	**25.0**	**32.1**	**28.4%**
Loan loss provision	(2.5)	(4.9)	95.9%
Total Operating expenses	**(15.2)**	**(19.9)**	**30.7%**
Profit before tax	9.8	12.2	24.8%
Profit after tax	**7.2**	**9.1**	**25.7%**
Core EPS	**18.2**	**22.9**	**25.7%**
Dividend Per Share	**9.0**	**12.6**	**40.0%**

Income Statement Ratios	FY'2021	FY'2022	% point change
Yield from interest-earning assets	7.0%	8.0%	1.0%
Cost of funding	2.4%	2.5%	0.1%
Net Interest Margin	5.0%	5.9%	0.9%
Net Interest Income as % of operating income	57.5%	59.1%	1.6%
Non-Funded Income as a % of operating income	42.5%	40.9%	(1.6%)
Cost to Income Ratio	61.0%	62.1%	1.1%
CIR without LLP	50.9%	46.7%	(4.2%)
Cost to Assets	3.9%	3.7%	(0.2%)

Capital Adequacy Ratios	FY'2021	FY'2022	% points change
Core Capital/Total Liabilities	18.2%	16.5%	(1.7%)
Minimum Statutory ratio	8.0%	8.0%	
Excess	**10.2%**	**8.5%**	**(1.7%)**
Core Capital/Total Risk Weighted Assets	15.3%	13.8%	(1.5%)
Minimum Statutory ratio	10.5%	10.5%	
Excess	**4.8%**	**3.3%**	**(1.5%)**
Total Capital/Total Risk Weighted Assets	17.3%	16.8%	(0.5%)
Minimum Statutory ratio	14.5%	14.5%	
Excess	**2.8%**	**2.3%**	**(0.5%)**
Liquidity Ratio	47.9%	45.2%	(2.7%)
Minimum Statutory ratio	20.0%	20.0%	
Excess	**27.9%**	**25.2%**	**(2.7%)**
Adjusted Core Capital/Total Deposit Liabilities	**18.3%**	**16.5%**	**(1.8%)**

Adjusted Core Capital/Total Risk Weighted Assets	**15.4%**	**13.8%**	**(1.6%)**
Adjusted Total Capital/Total Risk Weighted Assets	**17.3%**	**16.8%**	**(0.5%)**

Income Statement

- Core earnings per share rose by 25.7% to Kshs 22.9, from Kshs 18.2 in FY'2021, lower than our projected growth to Kshs 25.8 in FY'2022, with the variance brought on by the lenders' increased loan loss provision to Kshs 4.9 bn from Kshs 2.5 bn in FY'2021 which is in contrast to our projection of a 16.1% increase to Kshs 2.9 bn. The lender disclosed that its decision to significantly increase its loan loss provision is mainly due to elevated credit risk as a result of challenging economic environment which might impair loan repayments by its customers. The lender's overall performance was driven by the 28.4% growth in total operating income to Kshs 32.1 bn, from Kshs 25.0 bn in FY'2021. However, it was weighed down by a 30.7% growth in total operating expenses to Kshs 19.9 bn, from Kshs 15.2 bn in FY'2021,
- The 28.4% growth in total operating income was mainly driven by a 31.8% increase in Net Interest Income (NII) to Kshs 18.9 bn, from Kshs 14.4 bn in FY'2021, coupled with a 23.7% increase in Non-Funded Income (NFI) to Kshs 13.1 bn, from Kshs 10.6 bn in FY'2021,
- Interest income grew by 27.3% to Kshs 25.6 bn, from Kshs 20.1 bn in FY'2021, mainly driven by a 29.2% increase in interest income from loans and advances to Kshs 19.5 bn, from Kshs 15.1 bn in FY'2021. Thus, Yield on Interest-Earning Assets (YIEA) increased to 8.0% from 7.0% recorded in FY'2021, mainly attributable to the faster 27.3% growth in interest income compared to a 11.4% increase in average interest earning assets to Kshs 321.7 bn, from Kshs 288.8 bn in FY'2021,
- Interest expenses rose by 15.2% to Kshs 7.2 bn, from Kshs 6.2 bn in FY'2021, driven by 58.0% increase in interest expense on deposits and placements to Kshs 0.7 bn, from Kshs 0.4 bn in FY'2021, coupled with a 9.1% increase in interest expense from customer deposits to Kshs 5.9 bn in FY'2022 from Kshs 5.4 bn recorded in FY'2021. Cost of funds (COF) increased by 0.1% points to 2.5%, from 2.4% recorded in FY'2021, following a 15.2% increase in Trailing interest expense, to Kshs 7.2 bn from Kshs 6.2 bn recorded in FY'2021, coupled with a 9.3% increase in average interest bearing liabilities to Kshs 287.4 bn from Kshs 262.9 bn in FY'2021.Trailing interest expense refers to the performance of the interest expense for the past 12 consecutive months. Net Interest Margin (NIM) increased by 0.9% points to 5.9% from 5.0% in FY'2021, attributable to a 31.8% increase in trailing net interest income to Kshs 18.9 bn from Kshs 14.4 bn recorded in FY'2021 to Kshs which outpaced the 11.5% growth in average interest earning assets to Kshs 321.7 bn from Kshs 288.8 bn in FY'2021,
- Non-Funded Income (NFI) increased by 23.7% to Kshs 13.1 bn, from Kshs 10.6 bn in FY'2021, mainly driven by a 36.8% increase in the Stanbic Bank Kenya's foreign exchange trading income to Kshs 8.6 bn, from Kshs 6.3 bn in FY'2021, highlighting the group's increased foreign exchange margins. Total fees and commissions remained relatively unchanged at Kshs 3.7 bn as was recorded in FY'2021. The revenue mix shifted to 59:41 from 58:42 for the funded to non-funded income owing to the 31.8% growth in Net Interest income which outpaced 23.7% growth in the Non-Funded Income,
- Total operating expenses increased by 30.7% to Kshs 19.9 bn, from Kshs 15.2 bn in FY'2021, driven by 95.9% increase in loan loss provisions to Kshs 4.9 bn from Kshs 2.5 bn recorded in FY'2021. The banks' decision to increase provisioning is largely due to rising credit risk as a result of worsening economic environment, evidenced by the average Purchasing Managers Index (PMI) in 2022, which came at 49.2, below the no change threshold of 50. The unfavorable operating environment is largely brought on by elevated inflationary pressures globally as well as supply chain instability, which might hamper loan repayments due to reduced business activities,
- Cost to Income Ratio (CIR) increased to 62.1%, from 61.0% in FY'2021, owing to the 30.7% increase in total operating expense, which outpaced the 28.4% increase in total operating income. Notably, CIR without LLP declined by 4.2% points to 46.7% from 50.9% recorded in FY'2021 an indication of improved efficiency, and,
- Profit before tax increased by 24.8% to Kshs 12.2 bn, from Kshs 9.8 bn in FY'2021, with effective tax rate decreasing to 25.6% in FY'2022 from 26.1% in FY'2021, leading to a 25.7% increase in profit after tax to Kshs 9.1 bn in FY'2022, from Kshs 7.2 bn in FY'2021.

The group's directors recommended a record high dividend per share (DPS) of Kshs 12.6 in FY'2022, a 40.0% increase from dividend per share of Kshs 9.0 paid in FY'2021, representing a dividend yield of 11.6% at the current price per share of Kshs 108.8.

Balance Sheet

- The balance sheet recorded an expansion as total assets grew by 21.6% to Kshs 399.8 bn, from Kshs 328.9 bn in FY'2021, driven by a 16.4% loan book expansion to Kshs 266.8 bn, from Kshs 229.3 bn in FY'2021, coupled with a 42.9% increase in investment in government securities to Kshs 58.0 bn, from Kshs 40.6 bn in FY'2021. The higher growth in investment in government securities than loan book expansion is partly attributable to the low risk associated with government securities as opposed to loans extended to the private sector which carries high risk, particularly in the current challenging economic environment,
- Total liabilities rose by 23.9% to Kshs 337.6 bn, from Kshs 272.4 bn in FY'2021, driven by a 19.5% growth in customer deposits to Kshs 304.3 bn, from Kshs 254.6 bn in FY'2021, coupled with a 77.9% increase in borrowings to 10.1 bn from Kshs 5.7 bn recorded in FY'2021. With 29 branches countrywide and 1 branch in South Sudan, compared to 26 branches in 2021, deposits per branch increased by 3.6% to Kshs 10.1 bn, from Kshs 9.8 bn in FY'2021,
- The 19.5% growth in deposits as compared to the 16.4% growth in loans led to a decrease in the loan to deposits ratio to 87.7%, from 90.1% in FY'2021,
- The group's Asset Quality deteriorated, with NPL ratio increasing to 10.0% in FY'2022, from 9.3% in FY'2021, attributable to 26.4% increase in Gross non-performing loans to Kshs 28.4 bn, from Kshs 22.5 bn in FY'2021, which outpaced the 17.5% increase in gross loans to Kshs 284.8 bn, from Kshs 242.4 bn recorded in FY'2021,
- General Provisions (LLP) increased by 38.9% y/y to Kshs 12.2 bn in FY'2022, from Kshs 8.8 bn in FY'2021. The NPL coverage increased to 63.1% in FY'2022, from 58.1% in FY'2021, attributable to a 38.9% increase in provisions coupled with 33.6% increase in interest in suspense to Kshs 5.7 bn from 4.3 bn in FY'2021, which offset the 26.4% increase in gross non-performing loans,
- Shareholders' funds increased by 10.2% to Kshs 62.2 bn in FY'2022, from Kshs 56.5 bn in FY'2021, supported by a 15.3% increase in retained earnings to Kshs 43.3 bn, from Kshs 37.6 bn in FY'2021,
- Stanbic bank remains capitalized with a core capital to risk-weighted assets ratio of 13.8%, 3.3% points above the statutory requirement of 10.5%, though lower than 15.3% recorded in FY'2021. In addition, the total capital to risk-weighted assets ratio came in at 16.8%, exceeding the statutory requirement of 14.5% by 2.3% points. Adjusting for IFRS 9, the core capital to risk-weighted assets stood at 13.8%, while total capital to risk-weighted assets came in at 16.8%, and,
- The bank currently has a Return on Average Assets (ROaA) of 2.5%, and a Return on Average Equity (ROaE) of 15.3%.

Key Take-Outs:

1. **Increased Provisioning** – On the back of high credit risk brought on by deteriorated business environment, the bank increased its provisions holdings to cover for the anticipated losses in the future, with its provisions increasing by 38.9% to Kshs 12.2 bn from Kshs 8.8 bn recorded in FY'2021. The high credit risk is further evidenced by the 26.4% increase in bank's gross non-performing loans to Kshs 28.4 bn in FY'2022, from Kshs 22.5 bn recorded in FY'2021. Consequently, the NPL coverage increased to 63.1%, from 58.1% recorded in FY'2021.

Going forward, the factors that would drive the bank's growth would be:

- **Digital transformation**. The lender has capitalized on digital innovation for service delivery over the past two years to improve its operational efficiency, which has been a key factor in its financial performance. The lender disclosed that 93.0% of customer's transactions in 2022 were conducted through its digital channels. In 2022 the bank introduced borderless banking, allowing its customers across East Africa to conduct transaction smoothly and in real time. The bank disclosed that the platform has so far facilitated more than USD 0.8 bn in transactions across the East African region, demonstrating how the strategy has been a key driver in boosting the bank's non-funded income as well as accelerating customer acquisition,

- **Inclusivity.** The lender has been intentional in its focus on fostering inclusivity to drive its growth. The lender has committed Kshs 20.0 bn to finance women through its women specific-platform known as "DADA". Since the launch of the platform 3 years ago, it has attracted more than 53,000 women to the bank and a cumulative loans amounting to Kshs 7.7 bn has been disbursed so far,

- **Leveraging on Micro, Small and Medium Enterprises (MSMEs)**. The lender revealed its desire to strengthen its MSMEs segment through funding these entities. The lender disclosed that under its Business and commercial Banking business segment, it had issued a cumulative of Kshs 33.0 bn to these entities as at the end of December 2022. Also, it had disbursed Kshs 76.0 mn in grants and catalytic funding to over 400 MSMEs in the country.

- In our view, as the group prepares to unveil its next three year strategy later this year, the sustained digital transformation, inclusion and diversification through leveraging on MSMEs will be critical drivers of its growth.

Valuation Summary

- We are of the view that Stanbic bank is a "buy" with a target price of Kshs 119.5 representing an upside of 21.4%, from the current price of 108.8 as of 10th March 2023, inclusive of a dividend yield of 11.6%,
- Stanbic Bank is currently trading at a P/TBV of 0.8x and a P/E of 4.7x vs an industry average of 0.7x and 6.6x, respectively.