Cytonn INVESTMENTS

Stanbic Bank – Q3'2022
25th November, 2022

Below is a summary of Stanbic Bank's Q3'2022 performance:

Balance Sheet	Q3'2021	Q3'2022	y/y change
Net Loans and Advances	176.6	236.9	34.1%
Government Securities	45.6	63.0	38.3%
Total Assets	**295.0**	**371.4**	25.9%
Customer Deposits	212.9	267.3	25.6%
Deposits per Branch	8.5	10.7	25.6%
Total Liabilities	**250.3**	**321.0**	28.3%
Shareholders' Funds	**44.7**	**50.4**	12.6%

Key Ratios	Q3'2021	Q3'2022	% point change
Loan to Deposit ratio	83.0%	88.6%	5.7%
Return on average equity	27.3%	25.1%	(2.2%)
Return on average assets	3.7%	3.4%	(0.3%)

Income Statement	Q3'2021	Q3'2022	y/y change
Net interest Income	10.0	12.7	26.8%
Net non-interest income	7.5	10.3	37.5%
Total Operating income	**17.5**	**23.0**	**31.4%**
Loan loss provision	(1.5)	(2.9)	88.7%
Total Operating expenses	**(10.5)**	**(13.3)**	**27.2%**
Profit before tax	7.0	9.7	37.7%
Profit after tax	**5.1**	**7.0**	**36.8%**
Core EPS	**12.9**	**17.7**	**36.8%**

Income Statement Ratios	Q3'2021	Q3'2022	y/y change
Yield from interest-earning assets	6.6%	6.4%	(0.2%)
Cost of funding	2.9%	3.0%	0.1%
Net Interest Margin	6.2%	5.6%	(0.6%)
Net Interest Income as % of operating income	57.4%	55.4%	(2.0%)
Non-Funded Income as a % of operating income	42.6%	44.6%	2.0%
Cost to Income Ratio	59.8%	57.9%	(1.9%)
CIR without LLP	51.1%	45.4%	(5.7%)
Cost to Assets	3.0%	2.8%	(0.2%)

Capital Adequacy Ratios	Q3'2021	Q3'2022	% points change
Core Capital/Total Liabilities	19.5%	17.2%	(2.3%)
Minimum Statutory ratio	8.0%	8.0%	
Excess	**11.5%**	**9.2%**	**(2.3%)**
Core Capital/Total Risk Weighted Assets	15.5%	13.4%	(2.1%)
Minimum Statutory ratio	10.5%	10.5%	
Excess	**5.0%**	**2.9%**	**(2.1%)**
Total Capital/Total Risk Weighted Assets	17.5%	16.2%	(1.3%)
Minimum Statutory ratio	14.5%	14.5%	

Excess	**3.0%**	**1.7%**	**(1.3%)**
Liquidity Ratio	44.2%	39.9%	(4.3%)
Minimum Statutory ratio	20.0%	20.0%	
Excess	**24.2%**	**19.9%**	**(4.3%)**
Adjusted Core Capital/Total Deposit Liabilities	**19.6%**	**17.2%**	**(2.4%)**
Adjusted Core Capital/Total Risk Weighted Assets	**15.6%**	**13.4%**	**(2.2%)**
Adjusted Total Capital/Total Risk Weighted Assets	**17.6%**	**16.2%**	**(1.4%)**

Income Statement

- Core earnings per share rose by 36.8% to Kshs 17.7, from Kshs 12.9 in Q3’2021, higher than our expectations of an 18.5% increase to Kshs 15.3. The performance was driven by the 31.4% growth in total operating income to Kshs 23.0 bn, from Kshs 17.5 bn in Q3’2021, which outpaced the 27.2% growth in total operating expenses to Kshs 13.3 bn, from Kshs 10.5 bn in Q3’2021,
- Total operating income increased by 31.4% to Kshs 23.0 bn, from Kshs 17.5 bn in Q3’2021, driven by a 26.8% increase in Net Interest Income (NII) to Kshs 12.7 bn, from Kshs 10.0 bn in Q3’2021, coupled with a 37.5% increase in Non-Funded Income (NFI) to Kshs 10.3 bn, from Kshs 7.5 bn in Q3’2021,
- Interest income grew by 19.2% to Kshs 17.6 bn, from Kshs 14.8 bn in Q3’2021, mainly driven by a 23.8% increase in interest income from loans and advances to Kshs 13.4 bn, from Kshs 10.9 bn in Q3’2021. However, it was weighed down by 1.9% decline in interest from government securities to Kshs 3.5 bn from Kshs 3.6 bn recorded in Q3’2022. The Yield on Interest-Earning Assets (YIEA) declined to 6.4% from 6.6% recorded in Q3’2021,mainly due to a slower increase in interest income by 19.2 % to Kshs 17.6 bn, from Kshs 14.8 bn in Q3’2021 compared to a 23.7% increase in average interest earning assets to Kshs 275.8 bn, from Kshs 222.9 bn,
- Interest expenses rose by 6.3% to Kshs 4.8 bn, from Kshs 4.5 bn in Q3’2021, driven by 92.0% increase in interest expense on deposits and placements to Kshs 0.7 bn, from Kshs 0.3 bn in Q3’2021, while interest expense from customer deposits remained relatively unchanged at Kshs 4.1 bn in Q3’2022 as was recorded in Q3’2021. Cost of funds (COF) increased by 0.1% points to 3.0%, from 2.9% recorded in Q3’2021, following a 15.0% increase in Trailing interest expense, to Kshs 7.7 bn from Kshs 6.7 bn recorded in Q3’2022.Trailing interest expense refers to the performance of the interest expense for the past 12 consecutive months. Net Interest Margin (NIM) declined marginally by 0.6% points to 5.6% from 5.0% in Q3’2021, attributable to a 23.7% increase in average interest earning assets to Kshs 275.8 bn, from kshs 222.9 bn inQ3’2022, which outpaced the 11.5% growth in trailing net interest income to Kshs 15.5 bn, Kshs 13.9 bn in Q3’2021,
- Non-Funded Income (NFI) increased by 37.5% to Kshs 10.3 bn, from Kshs 7.5 bn in Q3’2021, mainly driven by a 69.3% increase in the group’s foreign exchange trading income to Kshs 6.9 bn, from Kshs 4.1 bn in Q3’2021, highlighting the group’s increased foreign exchange margins. However NFI was weighed down by a 24.4% decline in fees and commissions on loans and advances to Kshs 0.1 bn from Kshs 0.2 bn recorded in Q3’2022. Notably, total fees and commissions recorded an 8.1% increase to Kshs 2.9 bn, from Kshs 2.7 recorded in Q3’2021. The revenue mix moved to 55:45 from 57:43 for the funded to non-funded income owing to the 37.5% growth in Non-Funded income which outpaced 26.8% growth in the Net Interest Income,
- Total operating expenses increased by 27.2% to Kshs 13.3 bn, from Kshs 10.5 bn in Q3’2021, driven by a 14.4% increase in staff costs to Kshs 5.1 bn in Q3’2022, from Kshs 4.5 bn in Q3’2021. Additionally, loan loss provisions increased by 88.7% to Kshs 2.9 bn from Kshs 1.5 bn recorded in Q3’2022,
- Cost to Income Ratio (CIR) declined to 57.9%, from 59.8% in Q3’2021, owing to the 31.4% increase in total operating income, which outpaced the 27.2% increase in total operating expenses. Notably, CIR without LLP declined by 5.7% points to 45.4% from 51.1 bn recorded in Q3’2021an indication of improved efficiency, and,
- Profit before tax increased by 37.7% to Kshs 9.7 bn, from Kshs 7.0 bn in Q3’2021, similarly, tax expenses increased to Kshs 2.7 bn in Q3’2022 from Kshs 1.9 bn recorded in Q3’2021 leading to a 36.8% increase in profit after tax to Kshs 7.0 bn in Q3’2022, from Kshs 5.1 bn in Q3’2021.

Balance Sheet

- The balance sheet recorded an expansion as total assets grew by 25.9% to Kshs 371.4 bn, from Kshs 295.0 bn in Q3’2021, driven by a 34.1% growth in the loan book to Kshs 236.9 bn, from Kshs 176.6 bn in Q3’2021, coupled with a 38.8% increase in government securities to Kshs 63.0 bn, from Kshs 45.6 bn in Q3’2021,
- Total liabilities rose by 28.3% to Kshs 321.0 bn, from Kshs 250.3 bn in Q3’2021, driven by a 25.6% growth in customer deposits to Kshs 267.3 bn, from Kshs 212.9 bn in Q3’2022, coupled with a 24.6% increase in borrowings to 13.6 bn from Kshs 10.9 bn recorded in Q1’2021. With 25 branches countrywide, deposits per branch increased by 25.6% to Kshs 10.7 bn, from Kshs 8.5 bn in Q3’2021,
- The 34.1% growth in loans as compared to the 25.6% growth in deposits led to an increase in the loan to deposits ratio to 88.6%, from 83.0% in Q3’2021,
- The bank’s Asset Quality improved, with NPL ratio declining to 10.1% in Q3’2022, from 11.5% in Q3’2021, attributable to 34.2% increase in Gross loans to kshs 253.2 bn, from Kshs 218.2 bn in Q2’2022, which outpaced the 18.0% increase in gross non-performing loans to Kshs 25.6 bn, from Kshs 21.7 bn recorded in Q3’2021,
- General Provisions (LLP) increased by 35.6% y/y to Kshs 11.1 bn in Q3’2022, from Kshs 8.2 bn in Q3’2021. The NPL coverage increased to 63.4% in Q3’2022, from 54.9% in Q3’2021, attributable to a 35.6% increase in provision coupled with 37.6% increase in interest in suspense to Kshs 5.2 bn, from 3.8 bn in Q3’2021, which outpaced 18.0% increase in gross non-performing loans,
- Shareholders’ funds increased by 12.6% to Kshs 50.4 bn in Q3’2022, from Kshs 44.7 bn in Q3’2021, supported by a 15.5% increase in retained earnings to Kshs 45.4 bn, from Kshs 39.3 bn in Q3’2021,
- Stanbic bank remains capitalized with a core capital to risk-weighted assets ratio of 13.4%, 2.9% points above the statutory requirement of 10.5%. In addition, the total capital to risk-weighted assets ratio came in at 16.2%, exceeding the statutory requirement of 14.5% by 1.7% points. Adjusting for IFRS 9, the core capital to risk-weighted assets stood at 13.4%, while total capital to risk-weighted assets came in at 16.2%, and,
- The bank currently has a Return on Average Assets (ROaA) of 3.4%, and a Return on Average Equity (ROaE) of 25.1%.

Key Take-Outs:

1. **Increased Provisioning** – On the back of high credit risk, which has seen the bank’s gross non-performing loans increase by 18.0% to Kshs 25.6 bn in Q3’2022, from Kshs 21.7 bn in Q3’2021, the bank increased its provisions holdings to cover for the anticipated losses in the future, with its provisions increasing by 35.6% to Kshs 11.1 bn from Kshs 8.2 bn recorded in Q3’2021. Consequently, the NPL coverage increased to 63.4%, from 54.9% recorded in Q3’2021, and,
2. **Revenue diversification** - The bank’s NFI recorded a y/y increase of 37.5% to Kshs 10.3 bn in Q3’2022 mainly attributable to significant increase in Foreign Exchange income by 162.9% to Kshs 9.2 bn from Kshs 3.5 bn recorded in Q3’2022. The increase in foreign exchange income is partly attributable to the bank’s increased foreign exchange margins emanating from shortage of foreign currency in the country.

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

- **Digital transformation**. The bank improvement in its financial performance is attributable to its digital transformation strategy through mobile banking which has led to increase in transactions. Through mobile banking the banks has been able to grow its customer base which has been driving its profitability. In our view, we expect the inclusivity and wide customer reach through mobile banking will be a key driver in the bank’s growth

Valuation Summary

- We are of the view that Stanbic bank is a “buy” with a target price of Kshs 110.6, representing an upside of 16.4%, from the current price of 95.0 as of 25th November 2022, inclusive of a dividend yield of 8.4%,
- Stanbic Bank is currently trading at a P/TBV of 0.7x and a P/E of 3.3x vs an industry average of 0.6x and 4.3x, respectively.