I&M Holdings Plc – FY'2020
1st April, 2021

Below is a summary of the bank's performance;

Balance Sheet Items	FY'2019	FY' 2020	y/y change	FY'2020e	Expected y/y change	Variance in Growth Actual vs. Expected
Government Securities	53.9	101.7	88.6%	99.0	83.5%	(5.1%)
Net Loans and Advances	175.3	187.4	6.9%	183.9	4.9%	(2.0%)
Total Assets	**315.3**	**358.1**	**13.6%**	**353.8**	**12.2%**	**(1.4%)**
Customer Deposits	229.7	262.7	14.3%	260.4	13.4%	(0.9%)
Total Liabilities	254.4	290.0	14.0%	289.4	13.8%	(0.2%)
Shareholders' Funds	**57.7**	**64.2**	**11.2%**	**61.0**	**5.6%**	**(5.6%)**

Balance Sheet Ratios	FY'2019	FY'2020	% point change
Loan to Deposit Ratio	76.3%	71.3%	(5.0%)
Return on average equity	19.5%	13.2%	(6.3%)
Return on average assets	3.4%	2.3%	(1.1%)

Income Statement	FY'2019	FY'2020	y/y change	FY2020e	Expected y/y change	Variance in Growth Actual vs. Expected
Net Interest Income	15.5	15.6	0.6%	16.3	5.0%	4.4%
Net non-Interest Income	8.3	8.6	4.3%	8.4	1.4%	(2.9%)
Total Operating income	**23.8**	**24.2**	**1.9%**	**24.7**	**3.7%**	**1.8%**
Loan Loss provision	(0.6)	(2.5)	288.5%	(2.8)	335.5%	47.0%
Total Operating expenses	(10.1)	(12.6)	24.8%	(12.4)	23.1%	(1.7%)
Profit before tax	14.6	11.0	(25.0%)	11.7	(20.0%)	5.0%
Profit after tax	**10.8**	**8.4**	(21.9%)	**8.2**	(24.1%)	(2.2%)
Core EPS	**13.0**	**10.2**	(21.9%)	**9.9**	(24.1%)	(2.2%)

Income Statement Ratios	FY'2019	FY'2020	% point change
Yield from interest-earning assets	10.3%	9.6%	(0.7%)
Cost of funding	4.8%	4.6%	(0.2%)
Net Interest Margin	5.9%	5.4%	(0.5%)
Net Interest Income as % of operating income	65.2%	64.4%	(0.8%)
Non-Funded Income as a % of operating income	34.8%	35.6%	0.8%
Cost to Income Ratio	42.4%	52.0%	9.6%
CIR without LLP	39.8%	41.8%	2.0%
Cost to Assets	3.0%	2.8%	(0.2%)

Capital Adequacy Ratios	FY'2019	FY' 2020
Core Capital/Total Liabilities	22.7%	22.5%
Minimum Statutory ratio	8.0%	8.0%
Excess	**14.7%**	**14.5%**
Core Capital/Total Risk Weighted Assets	17.3%	18.6%
Minimum Statutory ratio	10.5%	10.5%
Excess	**6.8%**	**8.1%**
Total Capital/Total Risk Weighted Assets	21.2%	22.0%

Minimum Statutory ratio	14.5%	14.5%
Excess	**6.7%**	**7.5%**
Liquidity Ratio	46.3%	50.5%
Minimum Statutory ratio	20.0%	20.0%
Excess	**26.3%**	**30.5%**
Adjusted Core Capital/Total Liabilities	***22.5%***	***22.6%***
Adjusted Core Capital/Total RWA	***17.2%***	***18.7%***
Adjusted Total Capital/Total RWA	***21.0%***	***22.0%***

Key Highlights FY'2020

- I&M Holdings plc issued a circular to its shareholders on 3rd November 2020 revealing it would pay Kshs 3.6 bn to acquire 90.0% of Orient Bank Limited Uganda (OBL) share capital. The amount would be subject to adjustments on account of several factors including exchange rate fluctuations and amounts raised from the sale of the Ugandan bank's property in Kampala (Orient Plaza). The shares will be bought from Hemlata Karia, Jay Karia, Morka Holdings Limited, Zhong Shuang Quan, Cornerstone M8 Limited and the bank's Vice Chairman and founder, Dr Ketan Morjaria. Dr Morjaria, who currently holds a 7.9% stake in Orient Bank, is only selling a 2.4% stake to remain with a 5.5% stake in what will be I&M's Ugandan subsidiary. The announcement came 4 months after the two banks started negotiations, in July 2020.

Income Statement

- Core earnings per share declined by 21.9% to Kshs 10.2, from Kshs 13.0 in FY'2019, better than our projections of a 24.1% decline to Kshs 9.9. The performance was driven by a 24.8% increase in total operating expenses to Kshs 12.6 bn from Kshs 10.1 bn in FY'2019. The growth in the total operating expenses was mainly driven by a 288.5% growth in Loan Loss Provisions (LLP) to Kshs 2.5 bn from Kshs 0.6 in FY'2019. The variance in core earnings per share decline to Kshs 10.2 against our expectation of Kshs 9.9 was largely due to the 288.5% increase in Loan Loss Provisions (LLP), lower than our 335.5% projected increase,
- Total operating income increased by 1.9% to Kshs 24.2 bn, from Kshs 23.8 bn in FY'2019 driven by a 4.3% increase in Non-Funded Income (NFI) to Kshs 8.6 bn, from Kshs 8.3 bn in FY'2019, coupled with a 0.6% increase in Net Interest Income (NII) to Kshs 15.6 bn, from Kshs 15.5 bn in FY'2019,
- Interest income rose by 2.5% to Kshs 27.8 bn, from Kshs 27.2 bn in FY'2019. This was driven by a 35.9% growth in interest income from government securities to Kshs 5.6 bn, from Kshs 4.1 bn in FY'2019. The growth in interest income was however weighed down by a 2.1% decline in interest income from loans and advances to Kshs 21.9 bn from Kshs 22.4 bn in FY'2019, coupled with a 44.5% decline in placements income to Kshs 0.4 bn, from Kshs 0.7 bn in FY'2019. The Yield on Interest-Earning Assets declined to 9.6% from 10.3% in FY'2019, largely attributable to the 10.4% growth in average interest earning assets which grew faster than the 2.5% growth in trailing Interest Income. Trailing Interest Income refers to the performance of the interest income for the past 12 consecutive months,
- Interest expense rose by 5.1% to Kshs 12.2 bn, from Kshs 11.7 bn in FY'2019, following a 4.7% rise in Interest expense on deposits to Kshs 10.6 bn, from Kshs 10.1 bn in FY'2019, coupled with a 58.7% growth in the interest expense on placements to Kshs 0.9 bn, from Kshs 0.5 bn in FY'2019. Cost of funds declined by 0.2% points to 4.6% from 4.8% recorded in FY'2019, following a 10.7% increase in average interest bearing liabilities, which outpaced the 5.1% increase in trailing interest expense. Trailing interest expense refers to the performance of the interest expense for the past 12 consecutive months. Net Interest Margin (NIM) on the other hand, declined by 0.5% points to 5.4%, from 5.9% in FY'2019, despite the 0.6% increase in NII and the 10.4% increase in average interest-earning assets as a result of increased allocation to lower-yielding government securities during the period,
- Non-Funded Income grew by 4.3% to Kshs 8.6 bn, from Kshs 8.3 bn in FY'2019, driven by a 5.5% growth in income from other fees and commissions to Kshs 2.2 bn, from Kshs 2.1 bn in FY'2019, coupled with a 3.2% increase in

fees and commissions from loans and advances to Kshs 1.93 bn from Kshs 1.87 bn in FY'2019. The growth in NFI was however weighed down by a 26.9% decline in Foreign Exchange Trading income to Kshs 1.9 bn, from Kshs 2.6 bn in FY'2019. Notably, income from Total Fees and Commissions increased by 4.4% to Kshs 4.2 bn, from Kshs 4.0 bn recorded in FY'2019 despite the waiver on bank fees seen during the year. The revenue mix shifted to 64:36 funded to non-funded income, from 65:35, owing to the 4.3% increase in NFI, which outpaced to the 0.6% increase in NII,

- Total operating expenses rose by 24.8% to Kshs 12.6 bn from Kshs 10.1 bn in FY'2019, largely driven by a 288.5% increase in Loan Loss Provisions (LLP) to Kshs 2.5 bn, from Kshs 0.6 bn in FY'2019, on account of the poor operating environment brought about by COVID-19 which has adversely affected individuals and businesses' ability to repay loans. Staff costs on the other hand, declined by 4.3% to Kshs 4.5 bn in FY'2020, from Kshs 4.7 bn in FY'2019,
- Cost to Income Ratio (CIR) deteriorated to 52.0%, from 42.4% in FY'2019 attributable to the 288.5% increase in Loan Loss Provisions to Kshs 2.5 bn from Kshs 0.6 bn in FY'2019. Without LLP, cost to income ratio deteriorated as well to 41.8% from 39.8% in FY'2019, an indication of reduced efficiency,
- Profit before tax declined by 25.0% to Kshs 11.0 bn, down from Kshs 14.6 bn in FY'2019. Profit after tax declined by 21.9% to Kshs 8.4 bn, down from Kshs 10.8 bn in FY'2019, with the effective tax rate increasing to 34.6%, from 34.2% in FY'2019,
- The Board of Directors recommended a final Dividend per Share (DPS) of Kshs 2.25, translating to a total dividend payout of Kshs 1.9 bn. At the current price of Kshs 49.0, this translates to a dividend yield of 4.6%, and,
- The Board of Directors recommended the issuance of bonus share of one new fully paid up bonus share of a par value of Kshs 1.0 for every one ordinary share of par value Kshs 1.0 to be issued to shareholders registered on the company's register as at close of business on 10th May 2021. Subject to receipt of requisite approvals, shareholders will be credited with the bonus shares on 21st May 2021. Key to note, the bonus shares will not be entitled to receive any declared dividend for the year.

Balance Sheet

- The balance sheet recorded an expansion as total assets grew by 13.6% to Kshs 358.1 bn, from Kshs 315.3 bn in FY'2019. The growth was supported by an 88.6% increase in government securities to Kshs 101.7 bn, from Kshs 53.9 bn in FY'2019, coupled with a 6.9% loan book expansion to Kshs 187.4 bn, from Kshs 175.3 bn in FY'2019. The increased allocation to government securities seen during the period was partly attributable to the elevated credit risk on the back of the adverse effects of the ongoing pandemic on Kenyans' income levels and profitability of firms,
- Total liabilities rose by 14.0% to Kshs 290.0 bn, from Kshs 254.4 bn in FY'2019, driven by a 14.3% rise in customer deposits to Kshs 262.7 bn, from Kshs 229.7 bn in FY'2019. The growth was however mitigated by a 15.5% decline in placements liabilities to Kshs 6.8 bn, from Kshs 8.0 bn in FY'2019. Deposits per branch increased by 14.3% to Kshs 3.9 bn from Kshs 3.4 bn in FY'2019, with the number of branches remaining unchanged at 67 branches,
- The slower 6.9% growth in loans as compared to the 14.3% growth in deposits led to a decline in the loan to deposit ratio to 71.3% from 76.3% in FY'2019,
- Gross non-performing loans increased by 10.7% to Kshs 23.6 bn in FY'2020, from Kshs 21.3 bn in FY'2019. Consequently, the NPL ratio, rose to 11.6% in FY'2020, from 11.3% in FY'2019, attributable to the faster 10.7% increase in Gross Non-Performing Loans, which outpaced the 8.1% growth in gross loans. The NPL coverage on the other hand improved to 66.8% in FY'2020, from 59.1% in FY2019, as general Loan Loss Provisions increased by 25.7% to Kshs 10.8 bn from Kshs 8.6 bn in FY'2019,
- Shareholders' funds increased by 11.2% to Kshs 64.2 bn in FY'2020, from Kshs 57.7 bn in FY'2019, supported by a 16.8% increase in retained earnings to Kshs 39.6 bn, from Kshs 33.9 bn in FY'2019,
- I&M Holdings Plc remains sufficiently capitalized with a core capital to risk-weighted assets ratio of 18.6%, 8.1% points above the statutory requirement. In addition, the total capital to risk-weighted assets ratio came in at 22.0%, exceeding the statutory requirement by 7.5% points. Adjusting for IFRS 9, the core capital to risk-weighted assets stood at 18.7%, while total capital to risk-weighted assets came in at 22.0%, and,

- The bank currently has a Return on Average Assets (ROaA) of 2.3%, and a Return on Average Equity (ROaE) of 13.2%.

Key Take-Outs:

1. Due to the weakened business environment on account of the COVID-19 pandemic, the bank took a proactive stance in its provisioning levels as Loan Loss Provisions (LLP) increased by 288.5% to Kshs 2.5 bn in FY'2020, from Kshs 0.6 bn in FY'2019,
2. The bank's asset quality deteriorated, with the NPL ratio increasing to 11.6%, from 11.3% in FY'2019. NPL improved to 66.8% in FY'2020 from 59.1% in FY'2019, as general Loan Loss Provisions increased by 25.7% to Kshs 10.8 bn from Kshs 8.6 bn in FY'2019, with gross non-performing loans increasing by 10.7%,
3. NFI increased by 4.3% to 8.6 bn from 8.3 bn, mainly attributable to a a 5.5% increase in income from other fees and commissions to Kshs 2.2 bn from Kshs 2.1 bn in FY'2019 coupled with a 3.2% increase in fees and commissions from loans and advances to Kshs 1.93 bn from Kshs 1.87 bn in FY'2019. The growth in NFI was despite the waiver on bank fees seen during the year,
4. There was a decline in efficiency levels as the Cost to Income Ratio (CIR) deteriorated to 52.0%, from 42.4% in FY'2019, attributable to the 288.5% increase in Loan Loss Provisions to Kshs 2.5 bn from Kshs 0.6 bn in FY'2019. Without LLP, cost to income ratio deteriorated as well to 41.8% from 39.8% in FY'2019, an indication of reduced efficiency.

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

I. Geographical Diversification – The bank has been aggressively expanding into other regions, namely Tanzania, Rwanda, and Uganda. On this front, the bank is set to acquire 90.0% of the share capital of Orient Bank Limited Uganda (OBL). This will see the bank expand its operations in the Ugandan Market thus reducing its reliance on the Kenyan Market. This is also expected to drive growth in the near future.

Valuation Summary

- We are of the view that I&M Holdings Plc is a "***Buy***" with a target price of Kshs 58.3, representing an upside of 23.5%, from the current price of Kshs 49.0 as of 31st March, 2021, inclusive of a dividend yield of 4.6%,
- I&M Holdings Plc is currently trading at a P/TBV of 0.7x and a P/E of 5.0x vs an industry average of 0.7x and 7.3x, respectively.