# I&M Holdings Plc – H1'2021

**3rd September, 2021**

**Below is a summary of the I&M Holdings H1'2021 performance;**

| Balance Sheet Items | H1'2020 | H1'2021 | y/y change |
|---|---|---|---|
| Government Securities | 72.2 | 103.5 | 43.3% |
| Net Loans and Advances | 184.6 | 204.5 | 10.8% |
| **Total Assets** | **340.6** | **382.6** | **12.3%** |
| Customer Deposits | 252.5 | 276.8 | 9.6% |
| Total Liabilities | 278.6 | 312.5 | 12.2% |
| **Shareholders' Funds** | **58.7** | **65.9** | **12.2%** |

| Balance Sheet Ratios | H1'2020 | H1'2021 | % point change |
|---|---|---|---|
| Loan to Deposit Ratio | 73.1% | 73.9% | 0.8% |
| Return on average equity | 16.3% | 14.5% | (1.8%) |
| Return on average assets | 2.8% | 2.5% | (0.3%) |

| Income Statement | H1'2020 | H1'2021 | y/y change |
|---|---|---|---|
| Net Interest Income | 6.9 | 8.9 | 28.1% |
| Net non-Interest Income | 4.2 | 3.9 | (6.4%) |
| **Total Operating income** | **11.1** | **12.8** | **15.1%** |
| Loan Loss provision | (1.0) | (1.1) | 2.1% |
| Total Operating expenses | (6.1) | (7.2) | 19.0% |
| Profit before tax | 4.5 | 5.9 | 30.5% |
| **Profit after tax** | **3.2** | **4.2** | 33.2% |
| **Core EPS** | **1.8** | **2.4** | 32.2% |

| Income Statement Ratios | H1'2020 | H1'2021 | % point change |
|---|---|---|---|
| Yield from interest-earning assets | 9.8% | 9.5% | (0.3%) |
| Cost of funding | 4.6% | 4.1% | (0.5%) |
| Net Interest Margin | 5.5% | 5.7% | 0.2% |
| Net Interest Income as % of operating income | 62.2% | 69.2% | 7.0% |
| Non-Funded Income as a % of operating income | 37.8% | 30.8% | (7.0%) |
| Cost to Income Ratio | 54.4% | 56.3% | 1.9% |
| CIR without LLP | 45.1% | 48.1% | 3.0% |
| Cost to Assets | 1.5% | 1.6% | 0.1% |

| Capital Adequacy Ratios | H1'2020 | H1'2021 |
|---|---|---|
| Core Capital/Total Liabilities | 19.9% | 20.7% |
| Minimum Statutory ratio | 8.0% | 8.0% |
| **Excess** | **11.9%** | **12.7%** |
| Core Capital/Total Risk Weighted Assets | 16.3% | 15.9% |
| Minimum Statutory ratio | 10.5% | 10.5% |
| **Excess** | **5.8%** | **5.4%** |
| Total Capital/Total Risk Weighted Assets | 21.4% | 20.7% |
| Minimum Statutory ratio | 14.5% | 14.5% |
| **Excess** | **6.9%** | **6.2%** |
| Liquidity Ratio | 47.0% | 48.3% |
| Minimum Statutory ratio | 20.0% | 20.0% |
| **Excess** | **27.0%** | **28.3%** |
| ***Adjusted Core Capital/Total Liabilities*** | ***20.0%*** | ***20.8%*** |

| | | |
|---|---|---|
| ***Adjusted Core Capital/Total RWA*** | ***16.4%*** | ***15.9%*** |
| ***Adjusted Total Capital/Total RWA*** | ***21.5%*** | ***20.8%*** |

**Key Highlights H1'2021**

- I&M Holdings PLC announced that it has completed the 90.0% acquisition of Orient Bank Limited Uganda (OBL) share capital, after receiving all the required regulatory approvals. As highlighted in our Cytonn Weekly #50/2020, I&M Holdings was set to pay Kshs 3.6 bn for the deal; which translated to a Price to Book Value (P/Bv) of 1.1x. Additionally, I&M Holdings will take over 14 branches from OBL, taking its total branches to 80, from 66 branches as at the end of 2020, and,

- I&M Holdings received a Tier 2 subordinated loan of USD 50.0 mn (Kshs 5.4 bn) long-term loan from the International Finance Corporation (IFC)and The Dutch Entreprenurial Development Bank (FMO) to boost it's capital and enhance its lending capacity ot SMEs. The loan will have a maturity of up to 7 years with a grace period of 5 years, conforming with the Central Bank of Kenya's Tier 2 capital requirements.

**Income Statement**

- Core earnings per share increased by 32.2% to Kshs 2.4, from Kshs 1.8 in H1'2020, higher than our expectations of a 25.8% increase to Kshs 2.3. The increase was mainly driven by a 28.1% increase in Net Interest Income (NII) to Kshs 8.9 bn, from Kshs 6.9 bn in H1'2020. The increase in core earnings per share was higher than our expectations of a 25.8% increase, with the variance being mainly attributable to the 28.1% increase in Net Interest Income, against our expectation of a 21.4% increase,
- Total operating income increased by 15.1% to Kshs 12.8 bn, from Kshs 11.1 bn in H1'2020, driven by a 28.1% increase in Net Interest Income (NII) to Kshs 8.9 bn, from Kshs 6.9 bn in H1'2020. The increase in NII was however weighed down by a 6.4% decline in Non-Funded Income (NFI) to Kshs 3.9 bn, from Kshs 4.2 bn in H1'2020,
- Interest income rose by 11.6% to Kshs 14.6 bn, from Kshs 13.1 bn in H1'2020 driven by a 92.6% growth in interest income from government securities to Kshs 4.1 bn, from Kshs 2.1 bn in H1'2020. The growth in interest income was however weighed down by a 38.5% decline in interest income from placements to Kshs 0.1 bn, from Kshs 0.2 bn in H1'2020, coupled with a 3.6% decline in interest income from loans and advances to Kshs 10.4 bn, from Kshs 10.8 bn in H1'2020. The Yield on Interest-Earning Assets (YIEA) declined to 9.5%, from 9.8% in H1'2020, largely attributable to the 9.5% growth in average interest earning assets, which grew faster than the 6.4% growth in trailing Interest Income. Trailing Interest Income refers to the performance of the interest income for the past 12 consecutive months,
- Interest expense declined by 6.9% to Kshs 5.8 bn, from Kshs 6.2 bn in H1'2020, following an 11.8% decline in Interest expense on deposits to Kshs 4.8 bn, from Kshs 5.4 bn in H1'2020. The decline in interest expense was however weighed down by a 55.2% growth in the interest expense on placements to Kshs 0.5 bn, from Kshs 0.4 bn in H1'2020. Cost of funds declined by 0.5% points to 4.1%, from 4.6% recorded in H1'2020, following a 3.0% decline in trailing interest expense, coupled with a 9.3% increase in average interest bearing liabilities. 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, rose by 0.2% points to 5.7%, from 5.5% in H1'2020, attributable to the 13.8% increase in NII, which outpaced the 9.5% increase in average interest-earning assets,
- Non-Funded Income declined by 6.4% to Kshs 3.9 bn, from Kshs 4.2 bn in H1'2020, driven by an 18.2% decline in foreign exchange trading income to Kshs 0.8 bn, from Kshs 0.9 bn in H1'2020, coupled with a 20.1% decline in other income to Kshs 1.0 bn, from Kshs 1.2 bn in H1'2020. Fees and commissions on loans and advances also recorded a decline, decreasing by 5.2% to Kshs 0.9 bn, from Kshs 1.0 bn in H1'2020. Notably, income from Total Fees and Commissions decreased by 6.4% to Kshs 3.9 bn, from Kshs 4.2 bn recorded in H1'2020. The revenue mix shifted to 69:31 funded to non-funded income, from 62:38, owing to the 28.1% increase in NII, compared to the 6.4% decline in NFI,

- Total operating expenses rose by 19.0% to Kshs 7.2 bn, from Kshs 6.1 bn in H1’2020, largely driven by a 17.0% increase in staff costs to Kshs 2.7 bn, from Kshs 2.3 bn in H1’2020. Loan Loss Provisions (LLP) increased by 2.1% to Kshs 1.1 bn, from Kshs 1.0 bn, on account of the bank’s exposure to Real Estate and Personal/Household loans, which continue to be adversely affected by the poor operating environment brought about by COVID-19,
- Cost to Income Ratio (CIR) deteriorated to 56.3%, from 54.4% in H1’2020 driven by the 17.0% increase in staff costs to Kshs 2.7 bn in H1’2021, from Kshs 2.3 bn in H1’2020. Without LLP, cost to income ratio deteriorated as well to 48.1%, from 45.1% in H1’2020, an indication of reduced efficiency, and,
- Profit before tax increased by 30.5% to Kshs 5.9 bn, from Kshs 4.5 bn in H1’2020. Profit after tax rose by 33.2% to Kshs 4.2 bn, from Kshs 3.2 bn in H1’2020, with the effective tax rate decreasing to 27.6%, from 29.1% in H1’2020.

**Balance Sheet**

- The balance sheet recorded an expansion as total assets grew by 12.3% to Kshs 382.6 bn, from Kshs 340.6 bn in H1’2020. The growth was supported by a 43.3% increase in government securities to Kshs 103.5 bn, from Kshs 72.2 bn in H1’2020, coupled with a 10.8% loan book expansion to Kshs 204.5 bn, from Kshs 184.6 bn in H1’2020. The increased allocation to government securities seen during the period was partly attributable to the elevated credit risk associated with lending to customers following the adverse effects of the ongoing pandemic on the operating environment,
- Total liabilities rose by 12.2% to Kshs 312.5 bn, from Kshs 278.6 bn in H1’2020, driven by an 86.7% increase in borrowings to Kshs 18.6 bn, from Kshs 10.0 bn in H1’2020, with the increase in borrowings mainly attributable to a USD 50.0 mn (Kshs 5.4 bn) and USD 10.0 mn (Kshs 1.1 bn) loan from The International Finance Corporation (IFC) to I&M Bank Kenya and I&M Bank Rwanda respectively, coupled with a 9.6% rise in customer deposits to Kshs 276.8 bn, from Kshs 252.5 bn in H1’2020. The growth was however mitigated by an 8.4% decline in placements liabilities to Kshs 8.7 bn, from Kshs 9.5 bn in H1’2020. Deposits per branch increased by 11.3% to Kshs 4.2 bn from Kshs 3.8 bn in H1’2020, with the number of branches declining to 66 from 67 branches in H1’2020,
- The faster 10.8% growth in loans as compared to the 9.6% growth in deposits led to an increase in the loan to deposit ratio to 73.9%, from 73.1% in H1’2020,
- Gross non-performing loans increased by 3.8% to Kshs 22.9 bn in H1’2021, from Kshs 22.1 bn in H1’2020. The banks’ asset quality improved, with the NPL ratio declining to 10.4% in H1’2021, from 11.1% in H1’2020, attributable to the faster 10.8% increase in Gross Loans, which outpaced the 3.8% growth in gross Non-Performing loans. The NPL coverage also improved to 67.2% in H1’2021, from 63.1% in H1’2020, as general Loan Loss Provisions increased by 19.1% to Kshs 11.6 bn, from Kshs 9.8 bn in H1’2020,
- Shareholders’ funds increased by 12.2% to Kshs 65.9 bn in H1’2021, from Kshs 58.7 bn in H1’2020, supported by a 20.8% increase in retained earnings to Kshs 40.4 bn, from Kshs 33.3 bn in H1’2020,
- I&M Holdings Plc remains sufficiently capitalized with a core capital to risk-weighted assets ratio of 15.9%, 5.4% points above the statutory requirement. In addition, the total capital to risk-weighted assets ratio came in at 20.7%, exceeding the statutory requirement by 6.2% points. Adjusting for IFRS 9, the core capital to risk-weighted assets stood at 15.9%, while total capital to risk-weighted assets came in at 20.8%, and,
- The bank currently has a Return on Average Assets (ROaA) of 2.5%, and a Return on Average Equity (ROaE) of 14.5%.

**Key Take-Outs:**

1. On account of the bank’s exposure to the Real Estate and Personal/Household sectors’ loans which continue to be adversely affected by the poor operating environment brought about by COVID-19, the bank took a proactive stance in its provisioning levels as Loan Loss Provisions (LLP) increased by 2.1% to Kshs 1.1 bn in H1’2021, from Kshs 1.0 bn in H1’2020,
2. The bank’s asset quality improved, with the NPL ratio declining to 10.4%, from 11.1% in H1’2020. Key to note, this is the first time I&M’s asset quality has improved since Q2’2020, signaling a recovery in the bank’s loan book

performance. The NPL coverage improved to 67.2% in H1’2021 from 63.1% in H1’2020, as general Loan Loss Provisions increased by 19.1% to Kshs 11.6 bn from Kshs 9.8 bn in H1’2020, with gross non-performing loans increasing by 3.8%. Cost of risk also recorded a decrease, declining to 8.2%, from 9.3% in H1’2020 attributable to the 15.1% increase in total operating income, which grew faster than the 2.1% increase in Loan Loss Provisions,

3. Non-Funded Income decreased by 6.4% to Kshs 3.9 bn, from Kshs 4.2 bn in H1’2020, driven by a 20.1% decline in other income to Kshs 1.0 bn, from Kshs 1.2 bn in H1’2020, coupled with an 18.2% decline in foreign exchange trading income to Kshs 0.8 bn, from Kshs 0.9 bn in H1’2020. Fees and commissions on loans and advances also recorded a decline, decreasing by 5.2% to Kshs 0.9 bn, from Kshs 1.0 bn in H1’2020. Key to note, I&M Bank launched its Wealth Management and Advisory Business on 1st July 2021, targeting high net worth and premium customers. The move to offer wealth management and advisory services, which is in line with I&M’s strategic direction of diversification, will complement the bank’s investment and custodial services, provide holistic financial solutions to clients and boost the bank’s Non-Funded Income revenue through fees and commissions, and,
4. There was a decline in efficiency levels as the Cost to Income Ratio (CIR) deteriorated to 56.3%, from 54.4% in H1’2020 attributable to the 17.0% increase in staff costs to Kshs 2.7 bn, from Kshs 2.3 bn in H1’2020. Without LLP, cost to income ratio deteriorated as well to 48.1%, from 45.1% in H1’2020. Key to note, I&M’s Cost to Income ratio has been increasing y/y since Q2’2019, indicating the group’s reduced efficiency. I&M should consider reducing operating expenses such as staff costs, which recorded a 17.0% y/y growth, in order to prevent further deterioration of efficiency going forward.

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

I. Revenue Diversification – The bank launched its Wealth Management and Advisory Business, which will be provided through I&M Capital, a subsidiary of I&M Group PLC targeting high net worth and premium customers. The move to offer wealth management and advisory services, is expected to boost the bank’s Non-Funded Income revenue through fees and commissions charged and reduce I&M’s reliance on funded income.

**Valuation Summary**

- We are of the view that I&M Holdings Plc is a “***Buy***” with a target price of Kshs 28.3 representing an upside of 35.7%, from the current price of Kshs 22.8 as of 3rd September, 2021, inclusive of a dividend yield of 11.2%,
- I&M Holdings Plc is currently trading at a P/TBV of 0.6x and a P/E of 4.2x vs an industry average of 0.7x and 4.2x, respectively.