

### **Valuation Summary**

- We are of the view that Stanbic Holdings is a “Hold” with a target price of Kshs 103.1 representing an upside of 0.1%, inclusive of a dividend yield of 6.4%, from the current price of Kshs 110.0 as of 6<sup>th</sup> March 2020,
- Stanbic Holdings is currently trading at a P/TBv of 1.1x and a P/E of 6.8x, vs an industry average of 1.4x and 7.2x, respectively.

### **Key Highlights FY'19**

- The bank accepted a voluntary retirement for 88 staff members aimed at increasing efficiency. The costs involved totalled Kshs 0.8 bn recorded as an exceptional item in the financial statements. Stanbic Holdings also incurred some restructuring costs in mid-2019, which cost Kshs 1.3 bn recorded as an exceptional item in the financial statements.

### **Income Statement:**

- Core earnings per share increased by 1.6% to Kshs 16.1 from Kshs 15.9 in FY'2018, below our expectations of a 14.3% increase to Kshs 18.2. The variance was due to the 12.2% growth in total operating income to Kshs 24.8 bn in FY'2019 from Kshs 22.1 bn in FY'2018 which was slower than our projections of Kshs 26.7 bn. The growth was however mitigated by a 25.6% increase in total operating expenses to Kshs 13.9 bn, from Kshs 11.1 bn in FY'2018 which outpaced the growth in Total Operating Income,
- Total operating income rose by 12.2% to Kshs 24.8 bn, from Kshs 22.1 bn in FY'2018, driven by a 14.7% increase in Non-Funded Income to Kshs 11.4 bn in FY'2019, from Kshs 10.0 bn in FY' 2018, coupled with a 10.0% increase in Net Interest Income to Kshs 13.4 bn, from Kshs 12.1 bn in FY'2018,
- Interest income from the bank unit rose by 8.1% to Kshs 20.4 bn in FY'2019, from Kshs 18.9 bn in FY'2018. This was largely driven by the interest income on loans and advances, which rose by 10.8% to Kshs 15.7 bn in FY'2019, from Kshs 14.2 bn in FY'2018. Interest income from government securities, however, declined by 6.0% to Kshs 4.1 bn, from Kshs 4.3 bn in FY'2018. The yield on interest-earning assets remained unchanged at 7.9% in FY'2019,
- Interest expense increased by 7.1% to Kshs 7.7 bn, from Kshs 7.2 bn in FY'2018, following a 16.6% increase in the interest expense on customer deposits to Kshs 5.3 bn, from Kshs 4.5 bn in FY'2018. The increase was however mitigated by the 27.7% decline in interest expense on deposits and placements from banking institutions, to Kshs 1.4 bn from Kshs 1.9 bn in FY'2018,
- Despite the rise in expenses, the cost of funds dropped to 3.3%, from 3.4% in FY'2018 as the average interest-bearing liabilities rose at a faster rate of 11.3% as compared to the interest expense, which rose by 6.9%. Net Interest Margin increased to 5.2%, from 5.0% in FY'2018 on the back of the faster 10.7% increase in Net Interest Income to Kshs 13.4 bn, from Kshs 12.1 bn in FY' 2018, which outpaced the 3.6% growth in average interest-bearing assets,
- Non-Funded Income (NFI) rose by 14.0% to Kshs 11.4 bn in FY'2019 from Kshs 10.0 bn in FY'2018. The growth in NFI was driven by a 59.1% increase in foreign exchange trading income to Kshs 4.9 bn from Kshs 3.1 bn in FY'2018, and an 11.0% rise in other fees and commissions to Kshs 4.1 bn from Kshs 3.7 bn. Fees and commissions on loans and advances increased by 20.9% to Kshs 0.3 bn from Kshs 0.2 bn in FY'2018. The current revenue mix stands at 54:46 funded to non-funded income in FY'2019 from the 55:45 ratio recorded in FY'2018, owing to a faster increase in NFI,
- Total operating expenses increased by 25.6% to Kshs 13.9 bn in FY'2019 from Kshs 11.1 bn in FY'2018, largely driven by a 50.8% increase in the loan loss provision to Kshs 2.6 bn from Kshs 1.7bn in FY'2018. Other operating expenses recorded a 20.9% increase to Kshs 11.3 bn from Kshs 9.4bn in FY'2018. Consequently, Cost to income ratio with LLP deteriorated to 56.2% in FY'2019 from 50.2% in FY'2018. Without LLP, the Cost to income ratio also deteriorated to 45.6% in FY'2019 from 42.3% in FY'2018,

- Profit before tax declined by 13.8% to Kshs 7.7 bn from Kshs 9.0 bn in FY'2018, while profit after tax (PAT) increased by 12.5% to Kshs 9.5 bn, from Kshs 8.3 bn in FY'2018, owing to a decrease in the effective tax rate to 17.2% from 29.8% in FY'2018,
- The bank recommends a final dividend of Kshs 5.80 per share, having already paid an interim dividend of Kshs 1.25 per share, translating to a total dividend payout of Kshs 7.05 per share in 2019, a 21.6% increase from the Kshs 5.8 paid in 2018, which translates to a dividend yield of 6.4%.

**Balance Sheet:**

- The balance sheet recorded an expansion as total assets increased by 4.5% to Kshs 303.6 bn from Kshs 290.6 bn in FY'2018. This growth was largely driven by a 9.3% increase in the loan book to Kshs 191.2 bn from Kshs 175.0 bn, and other assets and prepayments, which increased by 69.3% to stand at Kshs 21.2 bn from Kshs 12.5 bn in FY'2018. The growth was however slowed down by a sharp decline in placements by 21.8% to Kshs 2.3 bn from Kshs 2.2 bn in FY'2018,
- Total liabilities rose by 3.5% to Kshs 254.6 bn from Kshs 245.9 bn in FY'2018, largely driven by a 2.4% increase in customer deposits to Kshs 224.7 bn from Kshs 219.5 bn in FY'2018, and a 29.2% increase in borrowings to Kshs 9.1 bn in FY'2019 from Kshs 7.1 bn in FY' 2018,
- The faster increase in loans as compared to the deposits lead to the increase in the loan to deposit ratio to 85.1% in FY'2019 from 79.7% in FY'2018,
- Gross non-performing loans increased by 16.2% to Kshs 19.3 bn from Kshs 16.6 bn in FY'2018. The NPL ratio thus deteriorated to 9.6% in FY'2019 from 9.1% in FY'2018, owing to the faster growth in non-performing loans that outpaced growth in the gross loans. General Loan Loss Provisions (LLPs) increased by 50.8% to Kshs 2.6 bn from Kshs 1.7 bn in FY'2018. Consequently, the NPL coverage increased to 57.1% in FY'2019 from 53.4% in FY'2018,
- Shareholders' funds increased by 9.9% to Kshs 49.0 bn in FY'2019 from Kshs 44.6 bn in FY'2018, largely due to the 13.8% increase in the retained earnings to Kshs 30.0 bn from Kshs 26.4 bn in FY'2018,
- Stanbic Bank is currently sufficiently capitalized with a core capital to risk-weighted assets ratio of 15.2%, 4.7% points above the statutory requirement. In addition, the total capital to risk-weighted assets ratio was 18.3%, exceeding the statutory requirement by 3.8% points. Adjusting for IFRS 9, core capital to risk-weighted assets ratio was at 16.2% while total capital to risk-weighted assets was 18.1%,
- Stanbic Holdings currently has a return on average assets of 2.1% and a return on average equity of 13.6%.

**Key Take-Outs:**

- a. The bank recorded a relatively strong performance in both funded and NFI segments. The bank's aggressive lending has led to increased interest income, as well as the associated fees and commissions. The increased lending has, however, come at a cost as asset quality deteriorated, as shown by the rise in the NPL ratio to 9.6%, from 9.1% in FY'2018. The cost of risk rose to 10.6% from 7.8% in FY'2018, consequently, the coverage ratio rose to 57.1%, from 53.4% in FY'2018,
- b. Stanbic Holdings registered strong performance on NFI, which grew by 14.7% to Kshs 11.4 bn from Kshs 10.0 bn in FY' 2018, underpinning the importance of revenue diversification. The bank has been aggressive in generating non-funded income, which now accounts for 46.1% of its operating income.

Below is a summary of the bank's performance

Balance Sheet (bns)	FY'2018	FY'2019	y/y change	FY '2019e	Projected y/y change	Variance in growth vs projections
Net Loans and Advances	175.0	191.2	9.3%	194.6	11.2%	(1.9%)
<b>Total Assets</b>	<b>290.6</b>	<b>303.6</b>	<b>4.5%</b>	<b>317.5</b>	<b>9.3%</b>	<b>(4.8%)</b>
Customer Deposits	219.5	224.7	2.4%	240.4	9.5%	(7.1%)
<b>Total Liabilities</b>	<b>245.9</b>	<b>254.6</b>	<b>3.5%</b>	<b>268.9</b>	<b>9.4%</b>	<b>(5.9%)</b>
<b>Shareholders' Funds</b>	<b>44.6</b>	<b>49.0</b>	<b>9.9%</b>	<b>48.6</b>	<b>9.0%</b>	<b>(0.9%)</b>

Balance sheet ratios	FY'2018	FY'2019	% y/y change	FY'2019e	Projected y/y change	Variance in growth vs projections
Loan to Deposit Ratio	79.7%	85.1%	6.8%	81.0%	1.3%	5.5%
Return on average equity	14.3%	13.6%	(4.9%)	15.7%	1.4%	(3.5%)
Return on average assets	2.3%	2.1%	(8.7%)	2.4%	0.1%	(8.6%)

Income Statement(mns)	FY2018	FY'2019	y/y change	FY'2019e	Projected y/y change	Variance in growth vs projections
Net Interest Income	12.1	13.4	10.7%	14.7	21.5%	(10.8%)
Net non-Interest Income	10.0	11.4	14.0%	12.0	20.0%	(6.0%)
<b>Total Operating income</b>	<b>22.1</b>	<b>24.8</b>	<b>12.2%</b>	<b>26.7</b>	<b>20.8%</b>	<b>(8.6%)</b>
Loan Loss provision	1.7	2.6	52.9%	2.8	64.7%	(11.8%)
Total Operating expenses	11.1	13.9	25.2%	16.3	46.8%	(21.6%)
<b>Profit before tax</b>	<b>9.0</b>	<b>7.7</b>	<b>(14.4%)</b>	<b>10.5</b>	<b>16.7%</b>	<b>(31.1%)</b>
<b>Profit after tax</b>	<b>6.3</b>	<b>6.4</b>	<b>1.6%</b>	<b>7.3</b>	<b>15.9%</b>	<b>(14.3%)</b>

Income statement ratios	FY'2018	FY'2019	% y/y change
Yield from interest-earning assets	7.9%	7.9%	0.0%
Cost of funding	3.4%	3.3%	(2.9%)
Net Interest Margin	5.0%	5.2%	4.0%
Cost to Income	50.2%	56.2%	12.0%
Cost to Assets	3.2%	3.7%	15.6%
Net Interest Income as % of operating income	54.9%	53.9%	(1.8%)
Non-Funded Income as a % of operating income	45.1%	46.1%	2.2%

Capital Adequacy Ratios	FY'2018	FY'2019
Core Capital/Total Liabilities	16.5%	18.4%
Minimum Statutory ratio	8.0%	8.0%
<b>Excess</b>	<b>8.5%</b>	<b>10.4%</b>
Core Capital/Total Risk Weighted Assets	14.6%	15.2%
Minimum Statutory ratio	10.5%	10.5%
<b>Excess</b>	<b>4.1%</b>	<b>4.7%</b>
Total Capital/Total Risk Weighted Assets	17.4%	18.3%
Minimum Statutory ratio	14.5%	14.5%
<b>Excess</b>	<b>2.9%</b>	<b>3.8%</b>
Liquidity Ratio	57.9%	58.4%
Minimum Statutory ratio	20.0%	20.0%
<b>Excess</b>	<b>37.9%</b>	<b>38.4%</b>
<b>Adjusted Core Capital/Total Liabilities</b>	<b>17.3%</b>	<b>19.7%</b>
<b>Adjusted Core Capital/Total RWA</b>	<b>15.3%</b>	<b>16.2%</b>
<b>Adjusted Total Capital/Total RWA</b>	<b>19.4 %</b>	<b>18.1%</b>