Standard Chartered Bank of Kenya Plc - H1'2021

27th August 2021

Below is a summary of Standard Chartered Bank of Kenya Plc H1'2021 performance;

Balance Sheet Items (Kshs bn)	H1'2020	H1'2021	y/y change
Net loans	134.3	130.3	(3.0%)
Total Assets	**327.2**	**345.6**	**5.6%**
Customer Deposits	256.5	278.2	8.5%
Total Liabilities	275.5	293.9	6.7%
Shareholder's Funds	**51.7**	**51.7**	**0.0%**

Balance Sheet Ratios	H1'2020	H1'2021	y/y % points change
Loan to deposit ratio	52.4%	46.8%	(5.6%)
Return on Average Equity	13.7%	13.7%	0.0%
Return on Average Assets	2.2%	2.1%	(0.1%)

Income Statement (Kshs bn)	H1'2020	H1'2021	y/y change
Net Interest Income	9.4	9.1	(3.0%)
Net non-Interest Income	4.4	5.0	13.5%
Total Operating income	**13.8**	**14.1**	**2.3%**
Loan Loss provision	1.6	0.6	(60.7%)
Total Operating expenses	8.7	7.3	(15.8%)
Profit before tax	5.1	6.8	33.1%
Profit after tax	**3.2**	**4.9**	**50.9%**
Core EPS (Kshs)	**9.4**	**12.9**	**37.5%**

Income Statement Ratios	H1'2020	H1'2021	y/y % points change
Yield from interest-earning assets	8.8%	7.7%	(1.1%)
Cost of funding	2.2%	1.5%	(0.7%)
Net Interest Spread	6.6%	6.2%	(0.4%)
Net Interest Margin	6.9%	6.4%	(0.5%)
Cost of Risk	11.8%	4.5%	(7.3%)
Net Interest Income as % of operating income	68.1%	64.6%	(3.5%)
Non-Funded Income as a % of operating income	31.9%	35.4%	3.5%
Cost to Income Ratio	63.0%	51.8%	(11.2%)

Capital Adequacy Ratios	H1'2020	H1'2021
Core Capital/Total Liabilities	15.6%	15.1%
Minimum Statutory ratio	8.0%	8.0%
Excess	**7.6%**	**7.1%**
Core Capital/Total Risk Weighted Assets	15.8%	15.9%
Minimum Statutory ratio	10.5%	10.5%
Excess	**5.3%**	**5.4%**
Total Capital/Total Risk Weighted Assets	18.4%	18.3%
Minimum Statutory ratio	14.5%	14.5%
Excess	**3.9%**	**3.8%**
Liquidity Ratio	66.8%	70.1%
Minimum Statutory ratio	20.0%	20.0%
Excess	**46.8%**	**50.1%**
Adjusted core capital/ total deposit liabilities	15.7%	15.2%
Adjusted core capital/ total risk weighted assets	15.8%	15.9%
Adjusted total capital/ total risk weighted assets	18.5%	18.3%

Income Statement

- Core Earnings Per Share (EPS) increased by 37.5% to Kshs 12.9, from Kshs 9.4 recorded in H1'2020, not in line with our projections of a 18.5% increase to Kshs 11.2. The increase was mainly driven by a 15.8% decline in total operating expenses to Kshs 7.3 bn, from Kshs 8.7 bn recorded in H1'2020, coupled with a 2.3% increase in total operating income to Kshs 14.1 bn, from Kshs 13.8 bn recorded in H1'2020. The increase in core earnings per share was higher than our expectations of an 18.5% increase, with the variance being mainly attributable to the total operating income growing by 2.3% against our expectation of a 0.4% decline in H1'2021,
- Total operating income rose by 2.3% to Kshs 14.1 bn, from Kshs 13.8 bn recorded in H1'2020. This was driven by an 13.5% increase in Non-Funded Income (NFI) to Kshs 5.0 bn, from Kshs 4.4 bn in H1'2020. The increase was however weighed down by a 3.0% decline in Net Interest Income (NII) to Kshs 9.1 bn, from Kshs 9.4 bn in H1'2020,
- Interest income declined by 7.5% to Kshs 11.0 bn, from Kshs 11.9 bn in H1'2020 driven by a 9.6% decline in interest income on loans and advances to Kshs 5.7 bn, from Kshs 6.3 bn in H1'2020, coupled with a 2.8% decline in interest income from government securities to Kshs 4.6 bn, from Kshs 4.8 bn in H1'2020. The decline in interest income was however mitigated by a 5.1% growth in interest income from deposits and placements with banking institutions to Kshs 0.72 bn, from Kshs 0.69 bn in H1'2020. Consequently, the Yield on Interest-Earning Assets (YIEA), declined to 7.7%, from 8.8% in H1'2020, attributable to a 6.7% decline in the trailing interest income, coupled with the 6.5% growth in the average interest-earning assets. Trailing Interest Income refers to the performance of the interest income for the past 12 consecutive months,
- Interest expense declined by 24.5% to Kshs 1.9 bn, from Kshs 2.5 bn in H1'2020, following a 24.9% decline in interest expense on customer deposits to Kshs 1.7 bn, from Kshs 2.3 bn in H1'2020, coupled with a 21.9% decline in other interest expenses to Kshs 0.1 bn, from Kshs 0.2 bn in H1'2020. Cost of funds consequently declined by 0.7% points to 1.5%, from 2.2% in H1'2020, owing to the 26.7% decline in the trailing interest expense, coupled with a 9.7% growth 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) declined to 6.4% from 6.9% in H1'2020, attributable to a 1.0% decline in the trailing Net Interest Income (NII), coupled with the 6.5% growth in average interest-earning assets,
- Non-Funded Income (NFI) increased by 13.5% to Kshs 5.0 bn, from Kshs 4.4 bn in H1'2020. The increase was mainly driven by a 14.8% rise in Foreign Exchange Trading income to Kshs 1.7 bn in H1'2021, from Kshs 1.5 bn in H1'2020, coupled with a 21.8% increase in income from other Fees and Commissions to Kshs 2.6 bn, from Kshs 2.1 bn in H1'2020. Fees and commissions on loans and advances, on the other hand, declined by 7.6% to Kshs 0.1 bn, from Kshs 0.2 bn in H1'2020. The bank's total fees and commissions increased by 19.8% to Kshs 2.7 bn, from Kshs 2.3 bn in H1'2020. As a result, the revenue mix shifted to 65:35 from 68:32 in H1'2020, funded to non-funded income, owing to the 13.5% increase in Non-Funded Income (NFI), compared to the 3.0% decline in Net Interest Income (NII),
- Total operating expenses declined by 15.8% to Kshs 7.3 bn in H1'2021, from Kshs 8.7 bn in H1'2020, mainly attributable to a 60.7% decline in Loss Provisions (LLPs) to Kshs 0.6 bn, from Kshs 1.6 bn recorded in H1'2020 partly attributable to the improved business environment, coupled with a 3.8% decline in Staff costs to Kshs 3.2 bn in H1'2021, from Kshs 3.3 bn in H1'2020,
- Cost to Income Ratio (CIR) improved to 51.8%, from 63.0% in H1'2020, owing to the 2.3% growth in total operating income compared to the 15.8% decline in total operating expenses. Without LLP, cost to income ratio improved as well to 47.3%, from 51.2% in H1'2020, an indication of improved efficiency levels, and,
- Profit before tax increased by 33.1% to Kshs 6.8 bn, from Kshs 5.1 bn in H1'2020. Profit after tax increased by 50.9% to Kshs 4.9 bn in H1'2021, from Kshs 3.2 bn recorded in H1'2020, with the effective tax rate decreasing to 28.2% from 36.7% in H1'2020.

Balance Sheet

- The balance sheet recorded an expansion as total assets grew by 5.6% to Kshs 345.6 bn, from Kshs 327.2 bn in H1’2020. This growth was largely driven by a 50.6% increase in placements from banking institutions to Kshs 70.9 bn, from Kshs 47.1 bn in H1’2020. The loan book, however, decreased by 3.0% to Kshs 130.3 bn, from Kshs 134.3 bn recorded in H1’2020, indicating the bank’s risk averseness and hesitancy to lend due to the credit risks involved,
- Total liabilities rose by 6.7% to Kshs 293.9 bn, from Kshs 275.5 bn in H1’2020, driven by an 8.5% increase in customer deposits to Kshs 278.2 bn, from Kshs 256.5 bn in H1’2020. Placements, however, declined by 74.2% to Kshs 0.6 bn in H1’2021, from Kshs 2.3 bn in H1’2020. Deposits per branch rose by 8.5% to Kshs 7.7 bn, from Kshs 7.1 bn in H1’2020 with the number of branches remaining unchanged at 36,
- The faster 8.5% growth in customer deposits compared to the 3.0% decline in loans led to a decline in the loans to deposit ratio to 46.8%, from 52.4% recorded in H1’2020,
- Gross Non-Performing Loans (NPLs) increased by 6.9% to Kshs 22.3 bn in H1’2021, from Kshs 20.9 bn recorded in H1’2020. Consequently, the NPL ratio rose to 15.1%, from 13.9% recorded in H1’2020. The asset quality deterioration is attributable to the 6.9% growth in Gross Non-Performing Loans (NPLs), coupled with a 1.7% decline in gross loans,
- General Loan Loss Provisions increased by 8.8% to Kshs 8.8 bn, from Kshs 8.1 bn in H1’2020. The NPL coverage thus increased to 80.1%, from 78.2% in H1’2020, as the provisions (after adding back interest in suspense) increased by 9.5% in H1’2021, outpacing the 6.9% rise in the Gross Non-Performing Loans during the same period. The increase in the NPL Coverage to 80.1% in H1’2021, from 78.2% in H1’2020, suggests sufficient provisioning,
- Shareholders’ funds remained unchanged at Kshs 51.7 bn in H1’2021, same as recorded in H1’2020, compared to an 8.0% growth in retained earnings to Kshs 36.4 bn, from Kshs 33.7 bn in H1’2020,
- Standard Chartered is currently 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 was 18.3%, exceeding the statutory requirement by 3.8% 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 18.3%, and,
- The bank currently has a Return on Average Assets (ROaA) of 2.1%, and a Return on Average Equity (ROaE) of 13.7%.

Key Take-Outs:

1. **Asset Quality** – the bank’s asset quality deteriorated owing to the increase in NPL ratio to 15.1% in H1’2021, from 13.9% recorded in H1’2020. The NPL ratio also declined q/q by 1.3% points, to 15.1% from 16.4% recorded in Q1’2021. The NPL ratio deterioration is attributable to the 6.9% growth in Gross Non-Performing Loans (NPLs), coupled with a 1.7% decline in gross loans. The gross loans level has increased by 9.0% from Q1’2021 to H1’2021, which was the first q/q growth since H1’2020 and points to the improved business environment and reducing credit risk,
2. **Provisions** – the bank’s Loans Loss Provisions (LLPs) declined by 60.7% to Kshs 0.6 bn, from Kshs 1.6 bn recorded in H1’2020 attributable to the improved business environment coupled with the fact that they have taken on minimal new risks as their loan book shrunk by 3.0% to Kshs 130.3 bn, from Kshs 134.3 bn recorded in H1’2020, indicating the bank’s risk averseness, and,
3. **Operating Efficiency** - There was an increase in the bank’s operating efficiency as the cost to income ratio without LLP improved to 47.3%, from 51.2% in H1’2020. The improvement was largely attributable to the decrease of Staff Costs by 3.8% to Kshs 3.2 bn in H1’2021, from Kshs 3.3 bn recorded in H1’2020.

Going forward, we expect the bank’s growth to be driven by:

I. Continued focus on promoting the usage of the bank’s alternative channels which is likely to continue boosting the company’s Non-Funded Income (NFI). Revenue expansion coupled with cost containment will be key in boosting the bank’s bottom line.

Valuation Summary

- We are of the view that Standard Chartered is an “***Accumulate***” with a target price of Kshs 149.1 representing an upside of 14.1%, from the current price of Kshs 140.0 as of 27th August 2021, inclusive of a dividend yield of 8.6%,
- Standard Chartered Bank is currently trading at a P/TBV of 1.1x and a P/E of 7.4x vs an industry average of 1.2x and 6.7x, respectively.