Standard Chartered Bank of Kenya Plc – Q3'2021

19th Nov 2021

Below is a summary of Standard Chartered Bank of Kenya Plc Q3'2021 performance;

Balance Sheet Items (Kshs bn)	Q3'2020	Q3'2021	y/y change
Net loans	131.7	131.7	0.1%
Total Assets	**314.4**	**330.7**	**5.2%**
Customer Deposits	242.8	258.4	6.4%
Total Liabilities	264.2	277.6	5.1%
Shareholder's Funds	**50.2**	**53.1**	**5.8%**

Balance sheet ratios	Q3'2020	Q3'2021	y/y % point change
Loan to Deposit Ratio	54.2%	51.0%	(3.2%)
Return on average equity	12.9%	14.5%	1.6%
Return on average assets	2.1%	2.3%	0.2%

Income Statement (Kshs bn)	Q3'2020	Q3'2021	y/y change
Net Interest Income	14.3	14.7	2.8%
Net non-Interest Income	6.3	7.6	19.1%
Total Operating income	**20.7**	**22.3**	**7.8%**
Loan Loss provision	2.73	2.68	(1.6%)
Total Operating expenses	14.1	13.4	(5.1%)
Profit before tax	6.6	8.9	35.5%
Profit after tax	**4.3**	**6.4**	**46.7%**
Core EPS	**12.6**	**16.9**	**33.7%**

Income Statement Ratios	Q3'2020	Q3'2021	y/y % points change
Yield from interest-earning assets	8.9%	8.0%	(0.9%)
Cost of funding	2.1%	1.5%	(0.6%)
Net Interest Spread	6.7%	6.5%	(0.2%)
Net Interest Margin	7.0%	6.7%	(0.3%)
Cost of Risk	13.2%	12.0%	(1.2%)
Net Interest Income as % of operating income	69.3%	66.1%	(3.2%)
Non-Funded Income as a % of operating income	30.7%	33.9%	3.2%
Cost to Income Ratio	68.2%	60.1%	(8.1%)

Capital Adequacy Ratios	Q3'2020	Q3'2021
Core Capital/Total Liabilities	16.7%	16.2%
Minimum Statutory ratio	8.0%	8.0%
Excess	**8.7%**	**8.2%**
Core Capital/Total Risk Weighted Assets	16.1%	15.6%
Minimum Statutory ratio	10.5%	10.5%
Excess	**5.6%**	**5.1%**
Total Capital/Total Risk Weighted Assets	18.7%	17.7%
Minimum Statutory ratio	14.5%	14.5%
Excess	**4.2%**	**3.2%**
Liquidity Ratio	65.7%	67.4%
Minimum Statutory ratio	20.0%	20.0%
Excess	**45.7%**	**47.4%**
Adjusted Core Capital/Total Liabilities	16.8%	16.2%
Adjusted Core Capital/Total RWA	16.1%	15.6%
Adjusted Total Capital/Total RWA	18.8%	17.7%

Income Statement

- Core earnings per share increased by 33.7% to Kshs 16.9, from Kshs 12.6 recorded in Q3'2020 driven by a 7.8% increase in total operating income to Kshs 22.3 bn, from Kshs 20.7 bn recorded in Q3'2020, coupled with a 5.1% decline in total operating expenses to Kshs 13.4 bn, from Kshs 14.1 bn recorded in Q3'2020,
- Total operating income rose by 7.8% to Kshs 22.3 bn, from Kshs 20.7 bn recorded in Q3'2020 driven by a 19.1% increase in Non-Funded Income (NFI) to Kshs 7.6 bn, from Kshs 6.3 bn in Q3'2020, coupled with a 2.8% gain in Net Interest Income (NII) to Kshs 14.7 bn, from Kshs 14.3 bn in Q3'2020,
- Interest income declined by 2.5% to Kshs 17.5 bn, from Kshs 19.9 bn in Q3'2020, driven by a 4.0% decline in interest income from government securities to Kshs 6.9 bn, from Kshs 7.2 bn in Q3'2020. The decline in interest income was however mitigated by a 1.6% growth in interest income from loans and advances to Kshs 9.5 bn, from Kshs 9.4 bn in Q3'2020. Consequently, the Yield on Interest-Earning Assets (YIEA), declined to 8.0%, from 8.9% in Q3'2020, attributable to the faster 7.6% growth in the average interest earning assets, which outpaced the 3.6% decline in the trailing interest income. Trailing Interest Income refers to the performance of the interest income for the past 12 consecutive months,
- Interest expense declined by 23.3% to Kshs 2.8 bn, from Kshs 3.6 bn in Q3'2020, following a 25.6% decline in interest expense on customer deposits to Kshs 2.5 bn, from Kshs 3.3 bn in Q3'2020. The decline was however weighed down by a 12.6% increase in interest expenses on deposits and placements with banking institutions to Kshs 57.2 mn, from Kshs 50.8 mn in Q3'2020. Cost of funds, on the other hand, declined by 0.6% points to 1.5%, from 2.1% in Q3'2020, owing to a 7.6% growth in average interest-bearing liabilities which outpaced the 25.2% decline in the trailing interest expense. Trailing interest expense refers to the performance of the interest expense for the past 12 consecutive months. Net Interest Margin (NIM) declined to 6.7%, from 7.0% in Q3'2020 attributable to a faster 7.6% growth in average interest-earning assets, which outpaced the 2.1% increase in the trailing Net Interest Income (NII),
- Non-Funded Income (NFI) increased by 19.1% to Kshs 7.6 bn, from Kshs 6.3 bn in Q3'2020. The increase was mainly driven by a 33.8% rise in Foreign Exchange Trading income to Kshs 2.5 bn in Q3'2021, from Kshs 1.9 bn in Q3'2020 coupled with a 19.3% increase in other Fees and Commission income to Kshs 3.9 bn, from Kshs 3.2 bn in Q3'2020. Fees and commissions on loans and advances, on the other hand, declined by 3.1% to Kshs 220.2 mn, from Kshs 227.2 mn in Q3'2020. The bank's total fees and commissions also increased by 17.9% to Kshs 4.1 bn, from Kshs 3.5 bn in Q3'2020 attributable to the expiry of the waiver on mobile banking fees. As a result, the revenue mix shifted to 66:34 from 69:31 in Q3'2020, funded to non-funded income, owing to the 19.1% increase in Non-Funded Income (NFI), compared to the slower 2.8% increase in Net Interest Income (NII),
- Total operating expenses declined by 5.1% to Kshs 13.4 bn in Q3'2021, from Kshs 14.1 bn in Q3'2020, mainly attributable to a 10.2% decline in Staff Costs to Kshs 4.9 bn, from Kshs 5.4 bn recorded in Q3'2020. Additionally, Loan Loss Provisions (LLPs) declined by 1.6% to Kshs 2.68 bn in Q3'2021, from Kshs 2.73 bn in Q3'2020 partly attributable to the improved business environment,
- Cost to Income Ratio (CIR) improved to 60.1%, from 68.2% in Q3'2020, owing to the 7.8% growth in total operating income compared to the 5.1% decline in total operating expenses. Without LLP, cost to income ratio improved as well to 48.0%, from 55.0% in Q3'2020, an indication of improved efficiency levels,
- Profit before tax increased by 35.5% to Kshs 8.9 bn, from Kshs 6.6 bn in Q3'2020. Profit after tax increased by 46.7% to Kshs 6.4 bn in Q3'2021, from Kshs 4.3 bn recorded in Q3'2020 with the effective tax rate decreasing to 28.6% from 34.0% in Q3'2020, and,
- The bank recommended an interim dividend per share of Kshs 5.0, per ordinary share in addition to an interim dividend on non-redeemable, non-cumulative, non-voting, non-participating and non-convertible preference shares for the period 31st December 2020 to 29th June 2021 at a rate of 6.0% per annum on the issue price of each share. This translates to a dividend yield of 9.3%.

Balance Sheet

- The balance sheet recorded an expansion as total assets grew by 5.2% to Kshs 330.7 bn in Q3’2021, from Kshs 314.4 bn in Q3’2020. This growth was largely driven by a 48.8% increase in placements from banking institutions to Kshs 69.3 bn, from Kshs 46.6 bn in Q3’2020, coupled with a 0.1% increase in the loan book to Kshs 131.74 bn, from Kshs 131.65 bn recorded in Q3’2020. The performance was however weighed down by a 6.8% decline in investments in government and other securities to Kshs 99.0 bn, from Kshs 106.2 bn recorded in Q3’2020,
- Total liabilities rose by 5.1% to Kshs 277.6 bn, from Kshs 264.2 bn in Q3’2020 driven by a 38.0% increase in Placements held to Kshs 2.8 bn in Q3’2021, from Kshs 2.0 bn in Q3’2020. Customer deposits increased by 6.4% to Kshs 258.4 bn, from Kshs 242.8 bn in Q3’2020. Deposits per branch rose by 6.4% to Kshs 7.2 bn, from Kshs 6.7 bn in Q3’2020 with the number of branches remaining unchanged at 36,
- The faster 6.4% growth in customer deposits compared to the marginal 0.1% increase in loans led to a decline in the loans to deposit ratio to 51.0%, from 54.2% recorded in Q3’2020,
- Gross Non-Performing Loans (NPLs) increased by 4.8% to Kshs 23.0 bn in Q3’2021, from Kshs 22.0 bn recorded in Q3’2020. Consequently, the NPL ratio rose to 15.3%, from 14.8% recorded in Q3’2020. The Asset Quality deterioration is attributable to the faster 4.8% growth in Gross Non-Performing Loans (NPLs), compared to the relatively slower 1.3% increase in gross loans,
- General Loan Loss Provisions increased by 16.8% to Kshs 9.8 bn, from Kshs 8.4 bn in Q3’2020. The NPL coverage thus increased to 82.8%, from 78.2% in Q3’2020, as the provisions (after adding back interest suspense) increased by 10.9% in Q3’2021, outpacing the 4.8% rise in the Gross Non-Performing Loans during the same period. The increase in the NPL Coverage to 82.8% in Q3’2021, from 78.2% in Q3’2020, suggests sufficient provisioning,
- Shareholders’ funds increased by 5.8% to Kshs 53.1 bn, from Kshs 50.2 bn recorded in Q3’2020. The increase can be attributed to the 4.5% increase in Retained earnings to Kshs 36.5 bn, from Kshs 34.9 bn in Q3’2020,
- Standard Chartered is currently sufficiently capitalized with a core capital to risk-weighted assets ratio of 15.6%, 5.1% points above the statutory requirement. In addition, the total capital to risk-weighted assets ratio was 17.7%, exceeding the statutory requirement by 3.2% points. Adjusting for IFRS 9, the core capital to risk-weighted assets stood at 15.6% while total capital to risk-weighted assets came in at 17.7%, and,
- The bank currently has a Return on Average Assets (ROaA) of 2.3%, and a Return on Average Equity (ROaE) of 14.5%.

Key Take-Outs:

1. **Asset Quality** – The bank’s asset quality deteriorated owing to the increase in NPL ratio to 15.3% in Q3’2021, from 14.8% recorded in Q3’2020. The NPL ratio deterioration is attributable to the 4.8% growth in Gross Non-Performing Loans (NPLs), which outpaced the 1.3% increase in gross loans. Given that the bank mainly lends to retail banking, which was most affected by the pandemic, the growth in Gross Non-Performing Loans (NPLs) is driven by the adverse effects of the pandemic on this sector,
2. **Provisions** – The bank’s Loans Loss Provisions (LLPs) declined by 1.6% to Kshs 2.68 bn, from Kshs 2.73 bn recorded in Q3’2020. The marginal decline in Loans Loss Provisions (LLPs) can be attributed to the bank’s high exposure to the retail banking sector whose credit risk has remained during the pandemic period,
3. **Operating Efficiency** - There was an increase in the bank’s operating efficiency as the Cost to Income ratio without LLP improved to 48.0%, from 55.0% in Q3’2020. The improvement was largely attributable to the 10.2% decrease in Staff Costs by to Kshs 4.9 bn in Q3’2021, from Kshs 5.4 bn recorded in Q3’2020.

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 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 138.6 representing an upside of 7.7%, from the current price of Kshs 128.8 as of 19th November 2021, inclusive of a dividend yield of 9.3%,
- Standard Chartered Bank is currently trading at a P/TBV of 1.0x and a P/E of 6.8x vs an industry average of 1.1x and 6.2x, respectively.