Standard Chartered Bank Kenya – Q3'2022
25th November, 2022

Below is a summary of Standard Chartered Bank Kenya Q3'2022 performance:

Balance Sheet Items	Q3'2021	Q3'2022	y/y change
Net loans	131.7	136.1	3.3%
Government Securities	99.0	112.0	13.2%
Total Assets	**330.7**	**366.1**	**10.7%**
Customer Deposits	258.4	286.1	10.7%
Deposits per Branch	7.2	13.0	81.2%
Total Liabilities	**277.6**	**310.6**	**11.9%**

Balance Sheet Ratios	Q3'2021	Q3'2022	% y/y change
Loan to deposit ratio	51.0%	47.6%	(3.4%)
Return on Average Equity	14.5%	21.0%	6.5%
Return on Average Assets	2.3%	3.3%	1.0%

Income Statement	Q3'2021	Q3'2022	y/y change
Net Interest Income	14.7	15.8	7.3%
Net non-Interest Income	7.6	8.8	16.1%
Total Operating income	**22.3**	**24.6**	**10.3%**
Loan Loss provision	2.7	0.6	(76.8%)
Total Operating expenses	**13.4**	**12.3**	**(8.3%)**
Profit before tax	8.9	12.3	38.2%
Profit after tax	**6.4**	**8.7**	**37.1%**
Core EPS	**16.8**	**23.1**	**37.1%**

Income Statement Ratios	Q3'2021	Q3'2022	y/y change
Yield from interest-earning assets	8.0%	7.3%	(0.7%)
Cost of funding	1.5%	1.1%	(0.4%)
Net Interest Spread	6.5%	6.2%	(0.3%)
Net Interest Margin	6.7%	6.3%	(0.4%)
Cost of Risk	12.0%	2.5%	(9.5%)
Net Interest Income as % of operating income	66.1%	64.3%	(1.8%)
Non-Funded Income as a % of operating income	33.9%	35.7%	1.8%
Cost to Income Ratio	60.1%	49.9%	(10.2%)

Capital Adequacy Ratios	Q3'2021	Q3'2022	% points change
Core Capital/Total Liabilities	16.2%	14.5%	(1.7%)
Minimum Statutory ratio	8.0%	8.0%	
Excess	**8.2%**	**6.5%**	**(1.7%)**
Core Capital/Total Risk Weighted Assets	15.6%	15.4%	(0.2%)
Minimum Statutory ratio	10.5%	10.5%	
Excess	**5.1%**	**4.9%**	**(0.2%)**
Total Capital/Total Risk Weighted Assets	17.7%	17.7%	(0.0%)
Minimum Statutory ratio	14.5%	14.5%	
Excess	**3.2%**	**3.2%**	**(0.0%)**
Liquidity Ratio	67.4%	71.9%	4.5%
Minimum Statutory ratio	20.0%	20.0%	
Excess	**47.4%**	**51.9%**	**4.5%**
Adjusted core capital/ total deposit liabilities	16.2%	14.5%	(1.7%)
Adjusted core capital/ total risk weighted assets	15.6%	15.5%	(0.2%)
Adjusted total capital/ total risk weighted assets	17.7%	17.7%	-

Income Statement

- Core earnings per share rose by 37.1% to Kshs 23.1, from Kshs 16.8 in Q3'2021, lower than our expectations of a 50.1% increase to Kshs 25.2, with the variance stemming from the 10.3% increase in total operating income, which was lower than our projection of a 27.5% increase. The performance was driven by the 10.3% growth in total operating income to Kshs 24.6 bn, from Kshs 22.3 bn in Q3'2021, coupled with an 8.3% decline in total operating expenses to Kshs 12.3 bn, from Kshs 13.4 bn in Q3'2021,
- Total operating income increased by 10.3% to Kshs 24.6 bn, from Kshs 22.3 bn in Q3'2021, driven by a 7.3% increase in Net Interest Income (NII) to Kshs 15.8 bn, from Kshs 14.7 bn in Q3'2021, coupled with a 16.1% increase in Non-Funded Income (NFI) to Kshs 8.8 bn, from Kshs 7.6 bn in Q3'2021,
- Interest income grew by 4.1% to Kshs 18.2 bn, from Kshs 17.5 bn in Q3'2021, mainly driven by a 9.5% increase in interest income from government securities, to Kshs 7.6 bn, from Kshs 6.9 bn in Q3'2021 coupled with a 43.7% increase in interest income earned from deposits and placements with banking institutions, to Kshs 1.5 bn, from Kshs 1.0 bn in Q3'2021. However, interest income from loans and advances declined by 4.1% to Kshs 9.1 bn from Kshs 9.5 bn recorded in Q3'2021. The Yield on Interest-Earning Assets (YIEA) declined to 7.3% from 8.0% in Q3'2021, attributable to a 7.7% growth in Average Interest Earning Assets (AIEA) adding to a marginal decline of 1.2% in trailing interest income. Trailing Interest Income refers to the performance of the interest income for the past 12 consecutive months,
- Interest expenses declined by 12.6% to Kshs 2.4 bn, from Kshs 2.8 bn in Q3'2021, following a 19.6% decline in interest expense on customer deposits to Kshs 2.0 bn, from Kshs 2.5 bn in Q3'2021. Consequently, the Cost of funds (COF) declined by 0.4% points to 1.1%, from 1.5% recorded in Q3'2021, following a 17.2% decline in Trailing interest expense, compared to the 8.3% 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 by 0.4% points to 6.3%, from 6.7% in Q3'2021 due to the faster 7.7% increase in average interest-earning assets outpacing the 1.8% growth in trailing Net Interest Income,
- Non-Funded Income (NFI) increased by 16.1% to Kshs 8.8 bn, from Kshs 7.6 bn in Q3'2021, driven by a significant 66.0% increase in the group's foreign exchange trading income to Kshs 4.2 bn, from Kshs 2.5 bn in Q3'2021, highlighting the group's increased foreign exchange margins, coupled with a 9.8% increase in other income to Kshs 1.0 bn, from Kshs 0.9 bn in Q3'2021. Notably, total fees and commissions declined by 13.4% to Kshs 3.5 bn, from the Kshs 4.0 bn recorded in Q3'2021 while fees and commissions from loans and advances declined by 8.5% to Kshs 0.0 bn, from Kshs 0.22 bn recorded in Q3'2021. The revenue mix shifted to 64:36 from 66:34 funded to non-funded income, owing to the faster 16.1% growth in NFI compared to the 7.3% growth of Net Interest Income (NII),
- Total operating expenses declined by 8.3% to Kshs 12.3 bn, from Kshs 13.4 bn in Q3'2021, largely driven by a 76.8% decrease in Loan Loss Provision (LLP) to Kshs 0.6 bn, from Kshs 2.7 bn in Q3'2021. The reduction in provisioning can be attributed to reduced credit risk in the country following the conclusion of the August 2022 general elections, evidenced by the reduction in the banking sector NPL ratio to 13.8% in October from 14.2% in August 2022. The decline in expenses was, however, weighed down by a 6.3% increase in staff costs, to Kshs 5.2 bn, from Kshs 4.9 bn in Q3'2021,
- Cost to Income Ratio (CIR) improved to 49.9%, from 60.1% in Q3'2021, owing to the 10.3% increase in total operating income, coupled with the 8.3% decline in total operating expenses. Without LLP, Cost to Income ratio improved marginally to 47.4% from 48.0% in Q3'2021, an indication of sustained efficiency, and,
- Profit before tax increased by 38.2% to Kshs 12.3 bn, from Kshs 8.9 bn in Q3'2021, with the effective tax rate rising slightly to 29.1%, from 28.6% in Q3'2021. Similarly, Profit after tax increased by 37.1% to Kshs 8.7 bn in Q3'2022, from Kshs 6.4 bn in Q3'2021.

Balance Sheet

- The balance sheet recorded an expansion as total assets grew by 10.7% to Kshs 366.1 bn, from Kshs 330.7 bn in Q3'2021, driven by a 13.2% increase in government securities to Kshs 112.0 bn, from Kshs 99.0 bn in Q3'2021, coupled with a 3.3% loan book expansion to Kshs 136.1 bn, from Kshs 131.7 bn in Q3'2021,
- Total liabilities rose by 11.9% to Kshs 310.6 bn, from Kshs 277.6 bn in Q3'2021, driven by a 10.7% growth in customer deposits to Kshs 286.1 bn, from Kshs 258.4 bn. Deposits per branch increased by 81.2% to Kshs 13.0 bn, from Kshs 7.2 bn in Q3'2021, with the number of branches declining to 22, from 36 in Q3'2021,
- The slower 3.3% growth in loans as compared to the 10.7% growth in deposits led to a decline in the loan to deposits ratio to 47.6%, from 51.0% in Q3'2021,
- Gross non-performing loans grew by 4.4% to Kshs 24.0 bn, from Kshs 23.0 bn in Q3'2021. Consequently, the group's Asset Quality deteriorated, with the NPL ratio increasing marginally to 15.4% in Q3'2022, from 15.3% in Q3'2021, attributable to the faster 4.4% growth in Non-Performing loans, which outpaced the 3.4% growth in gross loans,
- General Provisions (LLP) increased by 4.6% y/y to Kshs 10.3 bn in Q3'2022, from Kshs 9.8 bn in Q3'2021. The NPL coverage decreased slightly to 82.4% in Q3'2022, from 82.8% in Q3'2021,
- Shareholders' funds increased by 4.5% to Kshs 55.5 bn in Q3'2022, from Kshs 53.1 bn in Q3'2021, supported by a 5.4% increase in retained earnings to Kshs 38.4 bn, from Kshs 36.5 bn in Q3'2021,
- Standard Chartered Bank Kenya remains sufficiently capitalized with a core capital to risk-weighted assets ratio of 15.4%, 4.9% points above the statutory requirement of 10.5%. In addition, the total capital to risk-weighted assets ratio remained unchanged came at 17.7% recorded in Q3'2021, exceeding the statutory requirement of 14.5% by 3.2% points. Adjusting for IFRS 9, the core capital to risk-weighted assets stood at 15.5%, while total capital to risk-weighted assets came in at 17.7%, and,
- The bank currently has a Return on Average Assets (ROaA) of 3.3%, and a Return on Average Equity (ROaE) of 21.0%.

Key Take-Outs:

1. **Deterioration of the Asset Quality** - The group's asset quality deteriorated slightly, with the NPL ratio increasing to 15.4% in Q3'2022, from 15.3% in Q3'2021. The decline in asset quality was attributable to the faster 4.4% increase on gross non-performing loans as compared to the 3.4% growth in gross loans. This is despite the easing credit risk in the country with the banking sector Gross NPL ratio easing slightly to 13.8% in October from 14.2% in August 2022. Key to note, on a q/q basis, Standard Chartered Bank's Asset quality remained unchanged at 15.4% recorded in Q2'2022,
2. **Cautious Lending** – Q3'2022 was characterized by a faster 16.4% growth in government securities as compared to the 3.3% rise in net loans , highlighting the bank preference to government lending in light of the high credit risks among corporate and individuals in the economy.

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

I. **Revenue Diversification** – We expect the bank to continue to grow its revenue through the non-funded income as evidenced by the 16.1% growth of non-funded income to Kshs 8.8 bn, from 7.6 bn in Q3'2021, on the back of 66.0% increase in foreign exchange trade income to Kshs 4.2 bn, from Kshs 2.5 bn in Q2'2021, coupled with the introduction of SC shilingi fund evidenced by a 9.8% growth in other incomes to Kshs 1.0 bn, from Kshs 0.9 bn.

Valuation Summary

- We are of the view that Standard Chartered is an "Accumulate" with a target price of Kshs 169.3 representing an upside of 18.4%, from the current price of Kshs 143.0 as of 25th November 2022, inclusive of a dividend yield of 9.8%,
- Standard Chartered Bank is currently trading at a P/TBV of 0.9x and a P/E of 12.3x vs an industry average of 0.9x and 5.2x, respectively.