

Valuation Summary

- We recommend an Accumulate for the Standard Chartered Bank stock with a target price of Kshs 207.2 representing an upside of 12.7%, from the current price of Kshs 195.0, as at Wednesday, 25th May 2016, inclusive of a dividend yield of 6.4%
- Standard Chartered Bank is currently trading at a P/B of 1.5x and a P/E of 8.6x, versus an industry average of 1.6x and 7.4x, respectively

Key highlights during the quarter

- Standard Chartered launched a new banking application “SC Mobile” and unveiled a revamped online platform as the bank commenced the first phase of its “Digital by Design” business model
- The Bank granted customers a loan repayment break. Customers signing up for a Standard Chartered unsecured loan will enjoy a one-month repayment break of amounts up to Kshs 6.0 mn payable over 72 months

Income Statement

- Core earnings per share grew by an impressive 42.7% to Kshs 8.4 per share in Q1'2016 from Kshs 5.9 per share in Q1'2015, driven by a 24.0% growth in operating revenue in Q1'2016 outpacing the marginal growth in operating expenses of 6.6% in Q1'2016
- Operating revenue grew by 24.0% to Kshs 7.2 bn in Q1'2016 from Kshs 5.8 bn in Q1'2015 driven by a 66.2% increase in non-interest income to Kshs 2.4 bn from Kshs 1.4 bn in Q1'2015 and a 10.4% increase in net interest income to Kshs 4.9 bn from Kshs 4.4 bn in Q1'2015. Net interest margin increased to 9.7% in Q1'2016 from 9.64% in Q1'2015. Interest expenses rose by 47.8% to Kshs 1.5 bn in Q1'2016 from Kshs 1.0 bn in Q1'2015 supported by a 12.9% growth in deposits. The rise in interest expenses highlights the high cost of deposits during the quarter on account of spill-over effects of high interest environment from the second half of 2015
- Non funded income grew 66.2% supported by: i) 171.6% growth in foreign exchange trading income to Kshs 826.0 mn from Kshs 304.1 mn in Q1 2015, which however is not sustainable due to volatility in the exchange rates, ii) a 10.1% growth in fees and commissions to 76.9 mn from Kshs 69.8 mn, and iii) a 352.3% growth in other income to Kshs 557.5 mn from Kshs 123.2 mn in Q1'2015
- Operating expenses grew by a marginal 6.6% to Kshs 3.6 bn in Q1'2016 from Kshs 3.3 bn in Q1'2015 driven by a 9.5% rise in staff costs and supported by an 11.6% decrease in loan loss provision charge. The slower growth in expenses resulted in a significant decrease in cost to income ratio to 49.0% from 57.0% in Q1'2015
- Q1'2016 PAT growth came in higher than our expectations (42.8% growth to Kshs 2.6 bn from Kshs 1.8 bn compared to our projection of a 5.1% growth)

Balance Sheet

- The balance sheet recorded a relatively slow growth with total assets increasing by 7.2% to Kshs 249.7 bn from Kshs 233.0 bn in Q1'2015 compared to our projections of a 3.5% growth
- Customer deposits increased by 12.9% to Kshs 184.5 bn, and the growth can be attributed to the aggressive mobilization campaigns rolled out in Q4 to grow deposits. Loans disbursed decreased by 3.7% to Kshs 109.8 bn from Kshs 114.1 bn in Q1'2015 showing a conservative approach to lending leading to a decrease in the loan to deposit ratio to 59.5% from 69.8% in Q1'2015, lower than the industry average of 82.5%
- Gross non-performing loans grew by 84.5% to Kshs 15.4 bn from Kshs 8.4 bn in Q1'2015 compared to a decrease in gross loans of 2.5% which led to an increase in NPL ratio to 13.5% from 7.1% in Q1'2015. This is a trend that has been witnessed across the banking sector in FY'2015 results on account of high interest on loans in Q4'2015
- The yield on interest earning assets increased to 12.5% from 11.8% in Q1'2015 with the cost of funds increasing to 3.0% from 2.6%
- Standard Chartered Bank is currently sufficiently capitalized with a core capital to risk weighted assets ratio at 17.6%, 7.1% above the statutory requirement

Standard Chartered Bank's growth going forward will be propelled by:

- Managing their non-performing loans which are growing despite a stagnation in the loan book growth through more risk based loan supervision
- Growing core business as forex income and other income growth may not be sustainable going forward

Below is a summary of the key line items in the balance sheet and income statement

Figures in Kshs billions unless otherwise stated

Balance Sheet Items	FY'2015	Q1'2015	Q1'2016	y/y change	Q1'2016e	% y/y change	Variance in Growth Actual vs. Expected
Government Securities	73.6	65.4	74.0	13.2%	58.5	(10.6%)	23.8%
Net Loans and Advances	115.1	114.1	109.8	(3.7%)	127.6	11.9%	(15.6%)
Total Assets	234.0	233.0	249.7	7.2%	241.1	3.5%	3.7%
Customer Deposits	172.0	163.4	184.5	12.9%	177.2	8.4%	4.5%
Total Liabilities	192.7	190.4	205.5	7.9%	198.2	4.1%	3.8%
Shareholders' Funds	41.3	42.4	44.3	4.4%	42.8	1.0%	3.4%

Balance Sheet Ratios	FY'2015	Q1'2015	Q1'2016	y/y change
Loan to Deposit Ratio	66.9%	69.8%	59.5%	(10.3%)
Return on average equity	15.5%	4.4%	6.0%	1.5%
Return on average assets	2.8%	0.8%	1.1%	(0.3%)

Income Statement	FY'2015	Q1'2015	Q1'2016	y/y change	FY'2016e	% y/y change	Variance in Growth Actual vs. Expected
Net Interest Income	18.1	4.4	4.9	10.4%	5.0	13.2%	(2.8%)
Net non-Interest Income	7.2	1.4	2.4	66.2%	1.8	26.6%	39.6%
Total Operating income	25.4	5.8	7.2	24.0%	6.8	16.5%	7.5%
Loan Loss provision	(4.9)	(0.8)	(0.7)	(11.6%)	(1.5)	76.8%	(88.4%)
Total Operating expenses	(16.2)	(3.3)	(3.6)	6.6%	(4.1)	22.8%	(16.2%)
Profit before tax	9.2	2.5	3.7	46.9%	2.7	8.0%	39.0%
Profit after tax	6.3	1.8	2.6	42.8%	1.9	5.1%	37.7%
Core EPS	20.2	5.9	8.4	42.7%	5.5	(5.4%)	48.1%

Ratios	FY'2015	Q1'2015	Q1'2016	y/y change
Yield from interest-earning assets	12.1%	11.8%	12.5%	0.7%
Cost of funding	2.9%	2.6%	3.0%	0.4%
Net Interest Margin	9.6%	9.6%	9.7%	0.2%
Cost to Income	63.9%	57.0%	49.0%	(8.0%)
Net Interest Income as % of operating income	71.4%	75.7%	67.4%	(8.3%)
Non-Funded Income as a % of operating income	28.6%	24.3%	32.6%	8.3%

Capital Adequacy Ratios	Q1'15	Q1'16
Core Capital/Total Liabilities	19.3%	18.6%
Minimum Statutory ratio	10.5%	10.5%
Excess	8.8%	8.1%
Core Capital/Total Risk Weighted Assets	17.6%	17.6%
Minimum Statutory ratio	10.5%	10.5%
Excess	7.1%	7.1%
Total Capital/Total Risk Weighted Assets	21.7%	21.3%
Minimum Statutory ratio	14.5%	14.5%
Excess	7.2%	6.8%
Liquidity Ratio	56.2%	60.7%
Minimum Statutory ratio	20.0%	20.0%
Excess	36.2%	40.7%