Standard Chartered Bank Kenya – H1’2023

Below is a summary of Standard Chartered Bank Kenya H1’2023 performance:

Balance Sheet Items	H1'2022	H1'2023	y/y change
Net loans	128.5	145.4	13.2%
Government Securities	103.6	70.7	(31.7%)
Total Assets	**364.3**	**361.7**	**(0.7%)**
Customer Deposits	286.9	283.7	(1.1%)
Deposits per Branch	8.0	8.9	11.2%
Total Liabilities	**307.9**	**304.5**	**(1.1%)**
Shareholder's Funds	**56.4**	**57.1**	**1.2%**

Balance Sheet Ratios	H1'2022	H1'2023	% y/y change
Loan to Deposit Ratio	44.8%	51.3%	6.5%
Government Securities to Deposit ratio	36.1%	24.9%	(11.2%)
Return on average equity	17.7%	23.9%	6.2%
Return on average assets	2.7%	3.7%	1.0%

Income Statement	H1'2022	H1'2023	y/y change
Net Interest Income	10.0	13.9	38.3%
Net non-Interest Income	5.5	7.0	26.8%
Total Operating income	**15.6**	**20.9**	**34.2%**
Loan Loss provision	0.1	2.0	1781.5%
Total Operating expenses	**8.0**	**11.2**	**40.7%**
Profit before tax	7.6	9.6	27.4%
Profit after tax	**5.4**	**6.9**	**27.7%**
Core EPS	**14.3**	**18.3**	**27.7%**

Income Statement Ratios	H1'2022	H1'2023	y/y change
Yield from interest-earning assets	7.3%	9.1%	1.8%
Cost of funding	1.08%	1.14%	0.06%
Net Interest Spread	6.3%	7.9%	1.6%
Net Interest Margin	6.4%	8.0%	1.6%
Cost of Risk	0.7%	9.7%	9.0%
Net Interest Income as % of operating income	64.4%	66.3%	1.9%
Non-Funded Income as a % of operating income	35.6%	33.7%	(1.9)%
Cost to Income Ratio	51.3%	53.8%	2.5%
Cost to Income Ratio without LLP	50.6%	44.1%	(6.5%)
Cost to Assets	2.2%	2.5%	0.3%

Capital Adequacy Ratios	H1'2022	H1'2023	% points change
Core Capital/Total Liabilities	14.6%	17.0%	2.5%
Minimum Statutory ratio	8.0%	8.0%	0.0%
Excess	**6.6%**	**9.0%**	2.5%
Core Capital/Total Risk Weighted Assets	15.4%	16.9%	1.4%
Minimum Statutory ratio	10.5%	10.5%	0.0%
Excess	**4.9%**	**6.4%**	**1.4%**
Total Capital/Total Risk Weighted Assets	17.7%	17.3%	(0.5%)
Minimum Statutory ratio	14.5%	14.5%	0.0%
Excess	**3.2%**	**2.8%**	**(0.5%)**
Liquidity Ratio	73.6%	73.8%	0.1%
Minimum Statutory ratio	20.0%	20.0%	0.0%
Excess	**53.6%**	**53.8%**	**0.1%**

Income Statement

- Core earnings per share rose by 27.7% to Kshs 18.3, from Kshs 14.3 in H1’2022, higher than our expectations of a 19.7% increase, with the variance stemming from the 34.2% increase in total operating income to kshs 20.9 bn, which was higher than our projection of a 19.8% increase to Kshs 18.6 bn in H1’2023. The overall performance was weighed down by the 40.7% growth in total operating expenses to Kshs 11.2 bn, from Kshs 8.0 bn in H1’2022, against our relatively lower 17.8% expenses growth projection to Kshs 9.4 bn in H1’2023,
- The 34.2% growth in total operating income was mainly driven by a 38.3% growth in Net Interest Income to Kshs 13.9 bn, from Kshs 10.0 bn in H1’2022, coupled with a 26.8% growth in Non funded Income (NFI) to Kshs 7.0 bn, from Kshs 5.5 bn in H1’2022,
- Interest income grew by 33.4% to Kshs 15.4 bn from Kshs 11.5 bn in H1’2022, mainly driven by a 34.4% growth in interest income from loans and advances to Kshs 8.0 bn from Kshs 6.0 bn in H1’2022, coupled with a significant 241.4% growth in interest from deposits and placements in other banking institutions to kshs 2.5 bn, from kshs 0.7 bn in H1’2022. Consequently, the Yield on Interest-Earning Assets (YIEA) increased to 9.1% from 7.3% in H1’2022, attributable to the 28.8% growth in trailing interest income, which outpaced the 4.3% growth in Average Interest Earning Assets (AIEA) to kshs 323.8 bn, from kshs 310.4 bn in H1’2022. Trailing Interest Income refers to the performance of the interest income for the past 12 consecutive months,
- Interest expenses increased marginally by 0.9% to Kshs 1.52 bn, from Kshs 1.51 bn in H1’2022, driven by the 276.8% increase in interest expense from deposits and placements to Kshs 0.10 bn, from Kshs 0.03 bn in H1’2022 despite the 13.8% decrease in interest expense from customer deposits to Kshs 1.2 bn in H1’2023, from Kshs 1.3 bn recorded in H1’2022. Consequently, Cost of funds (COF) increased by 0.1% points to 1.14% from 1.08% recorded in H1’2022, owing to a faster 6.5% increase in Trailing interest expense to Kshs 3.3 bn, from Kshs 3.1 bn recorded in H1’2022, compared to a 1.4% increase in average interest bearing liabilities to Kshs 287.1 bn from Kshs 283.0 bn in H1’2022.Trailing interest expense refers to the performance of the interest expense for the past 12 consecutive months. Net Interest Margin (NIM) increased by 1.7% points to 7.9%, from 6.3% recorded in H1’2022, owing to the faster 32.2% growth in trailing Net Interest Income to kshs 26.1 bn, from kshs 19.7 bn in H1’2022 which outpaced the 4.3% increase in average interest-earning assets,
- Non-Funded Income (NFI) increased by 26.8% to Kshs 7.0 bn from Kshs 5.5 bn in H1’2022, mainly driven by a 96.5% increase in the foreign exchange trading income to Kshs 4.5 bn from Kshs 2.3 bn in H1’2022, highlighting the bank’s increased foreign exchange margins. Total fees and commissions increased by 11.7% to Kshs 2.8 bn, from Kshs 2.5 bn in H1’2022. The revenue mix shifted to 66:34 from 64:36 for the funded to Non-funded income owing to the 38.3% growth in Funded Income which outpaced the 26.8% growth in the Non Funded Income,
- Total operating expenses increased by 40.7% to Kshs 11.2 bn from Kshs 8.0 bn in H1’2022, driven by 1781.5% increase in loan loss provisions to Kshs 2.0 bn from Kshs 0.1 bn recorded in H1’2022, coupled with a 13.2% increase in staff costs to Kshs 4.1 bn from Kshs 3.6 bn in H1’2022. The increase in provisioning is partly attributable to rising credit risk as a result deterioroted economic environment as evidenced by the average Purchasing Managers Index (PMI) of 48.7 in H1’2023, down from an average of 49.3 in H1’2022,
- Cost to Income Ratio (CIR) increased to 53.8% from 51.3% in H1’2022, owing to the 40.7% increase in total operating expense, which outpaced the 34.2% increase in total operating income. Notably, CIR without LLP decreased by 6.6% points to 44.1% from 50.6% recorded in H1’2022, and,
- Profit before tax increased by 27.4% to Kshs 9.6 bn from Kshs 7.6 bn in H1’2022, with effective tax rate declining to 28.4% in H1’2023 from 28.5% in H1’2022. Similarly, profit after tax increased by 27.7% to Kshs 6.9 bn in H1’2023, from Kshs 5.4 bn in H1’2022.

Balance Sheet

- The balance sheet recorded a contraction as total assets declined marginally by 0.7% to Kshs 361.7 bn, from Kshs 364.3 bn in H1’2022, driven by a 31.7% decline in government securities to kshs 70.7 bn, from kshs 103.6 bn in

H1’2022. However, growth was supported by a 13.2% loan book expansion to Kshs 145.4 bn, from Kshs 128.5 bn in H1’2022,

- Total liabilities also declined by 1.1% to Kshs 304.5 bn from Kshs 307.9 bn in H1’2022, mainly attributable to a 1.1% decrease in customer deposits to Kshs 283.7 bn, from Kshs 286.9 bn in H1’2022,
- The 13.2% growth in loans as compared to the 1.1% decline in deposits led to an increase in the loan to deposits ratio to 51.3%, from 44.8% in H1’2022,
- The bank’s Asset Quality improved, with the NPL ratio declining to 14.4% in H1’2023, from 15.4% in H1’2022, attributable to the 12.2% growth in gross loans to kshs 165.6 bn, from kshs 147.6 bn in H1’2022, which outpaced the 4.6% increase in gross non-performing loans to kshs 23.8 bn, from kshs 22.7 bn in H1’2022.
- General Provisions (LLP) increased by 6.4% to Kshs 10.5 bn in H1’2023 from Kshs 9.9 bn in H1’2022. The NPL coverage increased to 84.8% in H1’2023, from 83.9% in H1’2022, attributable the 6.4% increase in General Provisions (LLP) to Kshs 10.5 bn, from Kshs 9.9 bn recorded in H1’2022, coupled with a 5.2% increase in interest suspense to Ksh 9.7 bn, from Kshs 9.2 bn in H1’2022, which outpaced the 4.6% increase in Gross Non-Performing Loans,
- Shareholders’ funds increased marginally by 1.2% to Kshs 57.1 bn in H1’2023, from Kshs 56.4 bn in H1’2022, supported by a 16.8% increase in retained earnings to Kshs 44.1 bn, from Kshs 37.8 bn in H1’2022,
- Standard Chartered Bank Kenya remains sufficiently capitalized with a core capital to risk-weighted assets ratio of 16.9%, 6.4% points above the statutory requirement of 10.5%. The total capital to risk-weighted assets ratio came in at 17.3%, exceeding the statutory requirement of 14.5% by 2.8% points, but was a 0.4% points decline from 17.7% recorded in H1’2022. Adjusting for IFRS 9, the core capital to risk-weighted assets stood at 16.9%, while total capital to risk-weighted assets came in at 17.3%, and,
- The bank currently has a Return on Average Assets (ROaA) of 3.7%, and a Return on Average Equity (ROaE) of 23.9%.

Key Take-Outs:

1. **Strong earnings growth -** Core earnings per share (EPS) grew by 27.7% to Kshs 18.3, from Kshs 14.3 in H1’2022, driven by the 34.2% growth in total operating income to Kshs 20.9 bn, from Kshs 15.6 bn in H1’2022. The performance was however weighed down by the 40.7% increase in the total operating expenses to Kshs 11.2 bn in H1’2023, from Kshs 8.0 bn in H1’2022,
2. **Improvement in Asset Quality -** The group’s asset quality improved significantly, with the NPL ratio improving to 14.4% in H1’2023, from 15.4% recorded in H1’2022. The improvement in asset quality was attributable to the 12.2% growth in gross loans, which outpaced the 4.6% increase in gross non-performing loans to kshs 23.8 bn, from kshs 22.7 bn in H1’2022**.**
3. **Increased Provisioning** - H1’2023 was characterized by increased provisioning, attributable to the high credit risks brought about by the deteriorated business environment. As such, Standard Chartered Bank Kenya increased its loan loss provisions to kshs 2.0 bn in H1’2023, up from Kshs 0.1 bn provisioning recorded in H1’2022. Additionally, General Provisions (LLP) increased by 6.4% to Kshs 10.5 bn, from Kshs 9.9 bn recorded in H1’2022.

Going forward, the factors that would drive the bank’s growth would be:

- **Digitalization** – Standard Chartered Bank Kenya is taking advantage of technology to improve its digital presence having digitalized 97.0% of its banking procedures as of FY’2022, consequently limiting the use of brick and mortar branches, especially with the SC Mobile App, the SC Shilling fund and enhanced product delivery to its clients.

Valuation Summary

- We are of the view that Standard Chartered is an “Buy” with a target price of Kshs 185.1 representing an upside of 24.1%, from the current price of Kshs 159.3 as of 25th August 2023, inclusive of a dividend yield of 13.8%,
- Standard Chartered Bank is currently trading at a P/TBV of 1.1x and a P/E of 5.1x vs an industry average of 0.8x and 3.5x, respectively