

### Valuation Summary

- We are of the view that I&M Holdings stock is a **“Buy”** with a target price of Kshs 147.5, representing an upside of 21.9%, from the current price of Kshs 124.0, as at 1<sup>st</sup> September, inclusive of a dividend yield of 2.9%
- I&M Holdings is currently trading at a P/TBV of 1.6x and a P/E of 8.0x, vs an industry average of 1.6x and 8.7x, respectively

### Key highlights during H1'2017

- In February, I&M Holdings announced the successful completion of a 100.0% acquisition of Giro Commercial Bank Limited (GCBL) for Kshs 5.0 bn and 21.0 mn shares to be part of I&M Bank Limited (IMBL), in a bid to increase the bank's footprint and market share in the country

### Income Statement

- Core earnings per share (EPS) registered a 16.8% decline, coming in at Kshs 7.9 from Kshs 9.5 in H1'2016, driven by an increase of 18.3% in operating expenses from H1'2016 with the operating income remaining flat. Without adjusting for the additional shares issued to Giro Bank, the EPS could have declined by 8.0%,
- Total operating income remained flat at Kshs 9.6 bn from H1'2016, despite a growth of 12.3% in Non-Funded Income (NFI), which was offset by a decline of 4.4% in the Net Interest Income (NII),
- NII dropped by 4.4% to Kshs 6.8 bn from Kshs 7.1 bn in H1'2016, following a 6.2% decline in interest income to Kshs 11.1 bn from Kshs 11.8 bn on account of interest rate caps, despite a 9.0% decline in interest expense to Kshs 4.2 bn from Kshs 4.6 bn in H1'2016,
- NFI improved by 12.3% to Kshs 2.7 bn from Kshs 2.4 bn in H1'2016, attributed to a 16.7% rise in fees and commissions on loans and advances to Kshs 1.4 bn from Kshs 1.2 bn in H1'2016. The current revenue mix shifted to 72:28 from 75:25 funded to non-funded income,
- Total operating expenses increased by 21.1% to Kshs 4.8 bn, from Kshs 4.0 bn in H1'2016, which was driven by an increase of 34.2% in loan loss provision (LLP) to Kshs 1.0 bn from Kshs 0.7 bn, and an 11.4% growth in staff costs to Kshs 1.9 bn from Kshs 1.7 bn in H1'2016,
- Cost to income ratio worsened to 50.7% from 41.7% in H1'2016. Without LLP, cost to income ratio stood at 40.6% from 34.2% in H1'2016,
- Profit before tax declined by 14.8% to Kshs 5.0 bn from Kshs 5.8 bn, while profit after tax declined by 16.8% to Kshs 3.4 bn from Kshs 4.2 bn in H1'2016.

### Balance Sheet

- The balance sheet recorded an expansion in H1'2017, with total assets increasing by 9.0% to Kshs 229.2 bn, from Kshs 210.3 bn in H1'2016, driven by a rise of 9.1% in the loan book to Kshs 144.5 bn from Kshs 132.5 bn in H1'2016
- Total liabilities increased by 6.4% to Kshs 184.9 bn from Kshs 173.8 bn in H1'2016, while shareholders' funds increased by 22.6% to Kshs 41.9 bn, from Kshs 34.2 bn in H1'2016,
- Customer deposits grew by 10.3% to Kshs 161.5 bn from Kshs 146.4 bn in H1'2016. Consequently, the faster growth in deposits compared to loans resulted in the loan to deposit ratio (LDR) declining marginally to 89.5% from 90.0% in H1'2016,
- Gross non-performing loans for the bank grew by 50.2% to Kshs 8.9 bn from Kshs 5.9 bn in H1'2016, leading to a rise in the Gross NPL ratio to 6.0%, from 4.3% in H1'2016,
- The yield on interest earning assets decreased to 12.0% from 13.1% in H1'2016, while the cost of funds came in at 4.9%, from 6.0% in H1'2016,
- I&M Holdings is currently sufficiently capitalized with a core capital to risk weighted assets ratio of 16.1%, 5.6% above the statutory requirement, with total capital to total risk weighted assets exceeding statutory requirement by 2.8% to close the period at 17.3%,
- I&M Holdings currently has a return on assets of 3.0%, while return on equity stands at 17.2%, a decline from 20.9% and 3.3% in H1'2016, respectively.

**Key Take outs:**

- a) Following the dismal performance, the Board of Directors did not recommend the payment of an interim dividend similar as last year, we expect the dividend payout to decrease by 8.5% this year,
- b) The 34.2% growth in loan loss provisions was mainly attributed to the Kenyan operations, which grew substantively due to partial adoption of IFRS 9, which requires banks to provide for non-performing loans more conservatively

**Going forward, we expect I&M Holdings growth to be propelled by;**

- i) Continued investment in the innovation and digitization of systems, processes and solutions in a bid enhance efficiency as well as to provide their customers with convenient access to products and solutions
- ii) Revenue diversification with new business lines such as the acquired Giro Bank and Burbridge Capital, which the bank will leverage on to spur growth
- iii) Expansion and increased growth in regional subsidiaries across Uganda, Tanzania, Mauritius and Rwanda

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

**Figures in Kshs bn unless otherwise stated**

Balance Sheet	HY'2016	HY'2017	y/y change	HY'2017e	Expected y/y change	Variance in Actual Growth vs. Expected
Government Securities	51.9	50.4	(3.0%)	51.9	0.0%	(3.0%)
Net Loans and Advances	132.5	144.5	9.1%	136.5	3.1%	6.1%
<b>Total Assets</b>	<b>210.3</b>	<b>229.2</b>	<b>9.0%</b>	<b>219.6</b>	<b>4.4%</b>	<b>4.6%</b>
Customer Deposits	146.4	161.5	10.3%	151.7	3.6%	6.7%
Total Liabilities	173.8	184.9	6.4%	176.2	1.4%	5.0%
<b>Shareholders' Funds</b>	<b>34.2</b>	<b>41.9</b>	<b>22.6%</b>	<b>41.0</b>	<b>19.7%</b>	<b>2.8%</b>

Balance sheet ratios	HY'2016	HY'2017	% y/y change
Loan to Deposit Ratio	90.5%	89.5%	(1.0%)
Return on average equity	20.9%	17.2%	(3.7%)
Return on average assets	3.3%	3.0%	(0.3%)

Income Statement	HY'2016	HY'2017	y/y change	HY'2017e	Expected y/y change	Variance in Actual Growth vs Expected
Net Interest Income	7.2	6.9	(4.4%)	7.4	2.8%	(7.3%)
Net non-Interest Income	2.4	2.7	12.3%	2.6	9.2%	3.2%
<b>Total Operating income</b>	<b>9.6</b>	<b>9.6</b>	<b>(0.2%)</b>	<b>10.0</b>	<b>4.4%</b>	<b>(4.6%)</b>
Loan Loss provision	(0.7)	(1.0)	34.2%	(0.8)	12.1%	22.0%
Total Operating expenses	(4.0)	(4.8)	21.1%	(4.4)	9.8%	11.4%
<b>Profit before tax</b>	<b>5.8</b>	<b>5.0</b>	<b>(14.8%)</b>	<b>5.6</b>	<b>(3.5%)</b>	<b>(11.2%)</b>
<b>Profit after tax</b>	<b>4.2</b>	<b>3.4</b>	<b>(16.8%)</b>	<b>3.9</b>	<b>(5.8%)</b>	<b>(11.0%)</b>
<b>Core EPS</b>	<b>9.5</b>	<b>7.9</b>	<b>(16.8%)</b>	<b>10.0</b>	<b>5.8%</b>	<b>(22.6%)</b>

Income statement ratios	HY'2016	HY'2017	% y/y change
Yield from interest-earning assets	13.1%	12.0%	(0.9%)
Cost of funding	6.0%	4.9%	(0.5%)
Net Interest Margin	3.7%	3.4%	(0.3%)
Cost to Income	41.7%	50.7%	8.9%
Cost to Assets	1.6%	1.7%	0.1%
Net Interest Income as % of operating income	74.9%	71.7%	(3.2%)
Non-Funded Income as a % of operating income	25.1%	28.3%	3.2%

Capital Adequacy Ratios	HY'2016	HY'2017
Core Capital/Total Liabilities	21.6%	20.2%
Minimum Statutory ratio	8.0%	8.0%
<b>Excess</b>	<b>13.6%</b>	<b>12.2%</b>
Core Capital/Total Risk Weighted Assets	17.0%	16.1%
Minimum Statutory ratio	10.5%	10.5%
<b>Excess</b>	<b>6.5%</b>	<b>5.6%</b>
Total Capital/Total Risk Weighted Assets	18.8%	17.3%
Minimum Statutory ratio	14.5%	14.5%
<b>Excess</b>	<b>4.3%</b>	<b>2.8%</b>
Liquidity Ratio	38.2%	35.9%
Minimum Statutory ratio	20.0%	20.0%
<b>Excess</b>	<b>18.2%</b>	<b>15.9%</b>