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CFC Stanbic Holdings Limited
Brief Note
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COMPANY OVERVIEW

CfC Stanbic Bank Limited (CfC or the Bank) was formed in June 2008 following the merger of Stanbic Bank Kenya Limited and CfC Bank Limited, a transaction that created one of Kenya's largest banks by assets. CfC is a wholly owned subsidiary of CfC Stanbic Holdings Limited (CFCB or the Company) which is Listed on the Nairobi Securities Exchange (NSE). Standard Bank Group (the Group), a leading pan-African financial services provider with a global presence in over 18 countries holds a 60% stake in the Company.

Following the merger, CFCB's holdings also included CfC Life Assurance Company Limited (100%), the Heritage Insurance Company Limited (64%) and CfC Financial Services Limited (100%). In 2009, CFCB embarked on a business restructuring process that culminated in the 2011 consolidation of the insurance businesses under a single holding company, CfC Insurance Holdings (CFCI). CFCI was thereafter separately listed on the NSE and in 2012 renamed Liberty Kenya Holdings Limited.

CFCB is organised around two divisions: Personal and Business Banking (PBB), the Bank's core business and Corporate and Investment Banking (CIB), provided by CfC Financial Services, a wholly owned subsidiary.

In 2009, CfC embarked on an aggressive expansion drive to grow its countrywide foot print and gain market share in the under-penetrated low income market segment. The Bank widened its target client base to cover low income areas such as Kariobangi and Gikomba. This ongoing expansion is expected to grow CfC's local branch network to 24 outlets by close of 2013. CfC also ventured into South Sudan in 2012, where it plans to open four additional branches in 2013.

CfC's expansion efforts have been funded by the Bank's KES 5.0bn corporate bond which was issued in two equal tranches (in 2009 and 2010) and the KES 4.01bn rights issue (RI) in 2012 which was 12% oversubscribed. Part of the RI proceeds were also used to shore up the bank's core capital, thereby facilitating an increase in the Bank's aggregate deposits and risk weighted assets.

COMPARATIVE ANALYSIS OF CFCB AND ITS PEERS

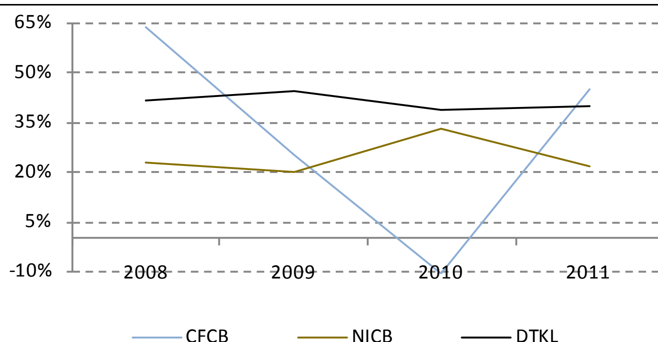
Following the 2008 merger, CFCB's profitability came under pressure from the insurance business' losses following rising insurance claims and growing expenses against declining insurance premiums. This is what triggered CFCB's decision to focus on its core banking and financial services businesses by offloading CFCI from its fold.

Following the successive changes to CFCB's business structure over the four year period to 2011, CFCB lacks true comparables with whom performance can be benchmarked like-for-like. We have therefore selected potential peers on the sole basis of market capitalisation (market cap) as at 11 January 2013 (CFCB's market cap was KES 17.88bn). These are:

- NIC Bank Limited (NICB): KES 23.76bn
- Diamond Trust Bank Limited (DTKL): KES 28.39bn).

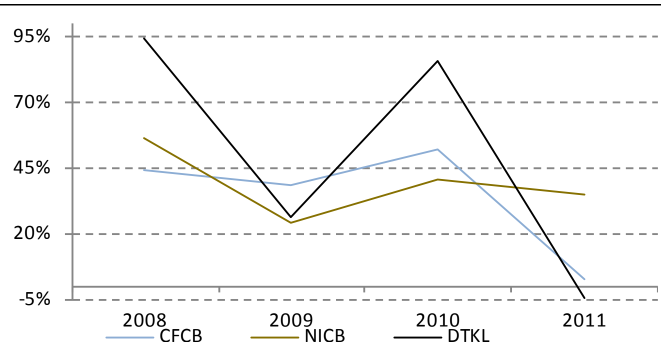
Using audited annual reports that have been adjusted to improve relative comparability, we review CFCB's financial performance for the period FY07 – 11 against that of the two peer companies.

Table 1: Net Interest Income Growth (%)



Source: *CFCB, NICB & DTKL 2011 Annual Reports and Dyer & Blair estimates*

Table 2: Non Interest Income Growth (%)



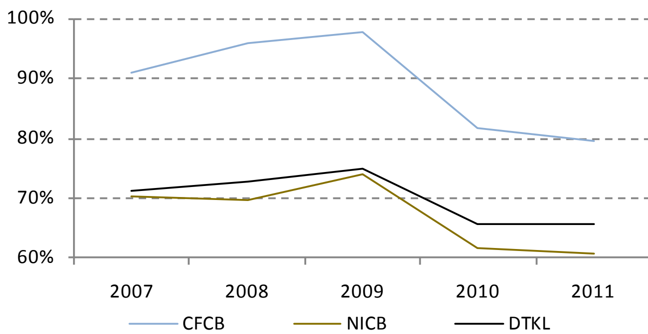
Source: *CFCB, NICB & DTKL 2011 Annual Reports and Dyer & Blair estimates*

CFCB's financial performance is largely determined by the banking business, which as at 31 December 2011 contributed 99% of the Company's total profitability.

While NICB and DTKL experienced relative stability in net interest income growth for the three year period to 2010, CFCB was on a downtrend as growth in interest income was outpaced by rising interest expenses. Part of these financing costs stemmed from the KES 5.0bn corporate bond: the 2009 tranche was priced at 12.5% (fixed rate component) and 1.75% + six-month Treasury Bill rate (floating rate portion), while the 2010 tranche was fixed at 7.5%. Net interest income recovery in 2011 was occasioned by the successive hikes in the Central Bank Rate (CBR) that served to reverse the declining growth.

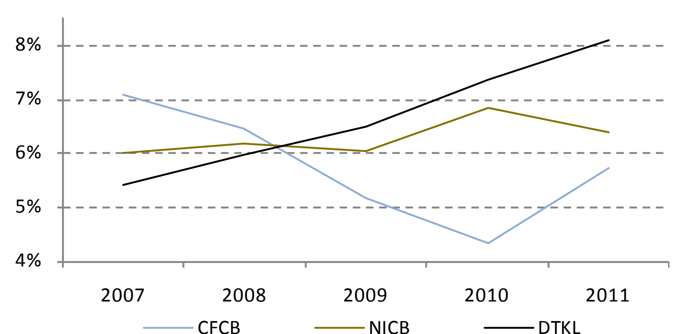
The 2011 drop in CFCB's non interest income was attributed to a reduction in corporate advisory fees due to the challenging operating environment, although high foreign exchange trading income and gains from government securities did provide some respite.

Table 3: Cost to Income Ratio (%)



Source: *CFCB, NICB & DTKL 2011 Annual Reports and Dyer & Blair estimates*

Table 4: Net Income margin (NIM)[1] (%)



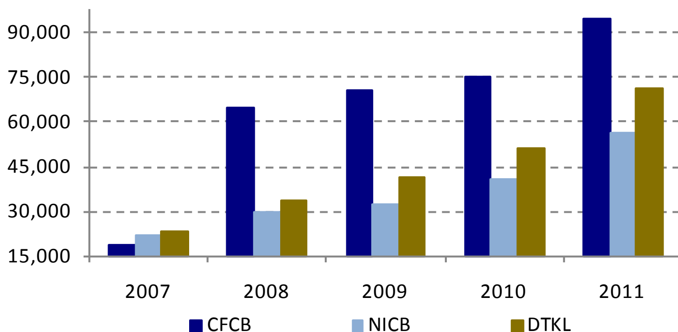
Source: *CFCB, NICB & DTKL 2011 Annual Reports and Dyer & Blair estimates*

CFCB's non-interest expenses as a proportion of total expenses averaged 75% during the four year period to 2011, against 55% for NICB and 54% for DTKL.

This significant disparity in costs was brought about by a number of factors: CFCB's business consolidation costs during the 2008 merger, restructuring costs during the 2011 insurance businesses' spin-off, impairment of available for sale financial investments due to the bearish equity market environment, high corporate bond financing cost and the acquisition of a new core banking system in 2009. In spite of these, the business restructuring exercise seems to have positively impacted the cost-to-income ratio, pushing it from a high of 97.8% in 2009 to 79.4% in 2011.

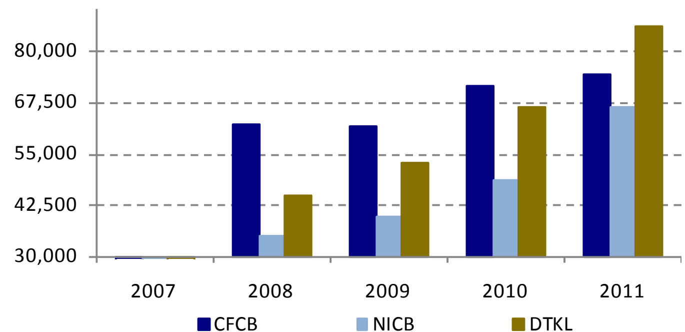
CFCB's NIM was higher than that of its peers between 2007 and 2008, although this rate came under considerable pressure from the prevailing high interest environment, pushing the NIM to a low of 4.3% in 2010.

Table 5: Loans and Advances (KES m)



Source: *CFCB, NICB & DTKL 2011 Annual Reports and Dyer & Blair estimates*

Table 6: Customer Deposits (KES m)



Source: *CFCB, NICB & DTKL 2011 Annual Reports and Dyer & Blair estimates*

Since 2008, CFCB's total loans have been relatively higher than its peers despite lower NIMs, indicating that the Bank has not competitively deployed its loan book to earn higher interest income. The decline in lending income was further compounded by the negative growth experienced in CFCB's loan book during FY10. Increased lending in 2011 translated to a 23.8% growth in total loans, with injection of additional Tier 1 capital following the 2012 RI expected to result in further loan book growth.

[1] Net interest margin (NIM) = Net interest income / Average interest bearing assets

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CFCB's profit before tax for the six month period to 30Th June 2012 increased by 36.51% to KES 1.78bn from KES 1.3bn the previous year, pointing to potentially strong full year numbers.

STOCK MARKET PERFORMANCE

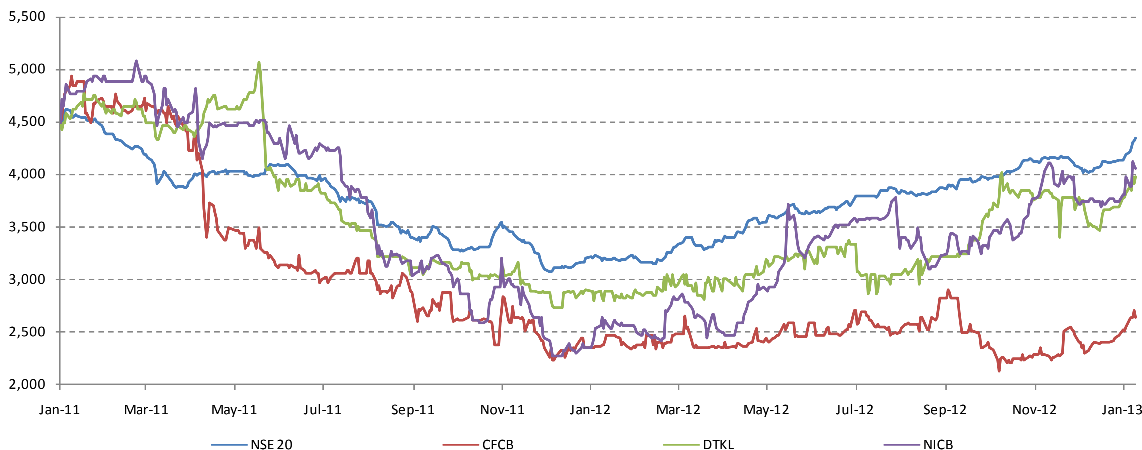
Following the effects of the global economic recession, CFCB's share price declined by 36.64% between January and June 2011, with the NSE20 Share Index (NSE20 or the Index) dipping by 21.24% over the same period. The share price has remained relatively stable since then, with the effects of the 2012 RI resulting in slight price volatility between September and November 2012.

CFCB's poor financial performance relative to other banks (CfC's profitability declined during a period when other Kenyan banks were increasing profitability), low dividend payout policy (dividends as a proportion comprehensive income has averaged 14.1% during the last four years to 2011), underperformance (relative to the market as proxied by the NSE20) and low free float (the top 10 shareholders collectively hold 90.07% of the issued shares) have over time resulted in investor apathy towards the stock.

The expected release of strong 1H2012 numbers and loan book expansion following the RI could however positively impact share price performance during the year.

Table 7: Share Price Performance of CFCB and Peer Companies

Base = 4,495.41, the NSE20 share index value on 3 January 2011



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