

DYER & BLAIR INVESTMENT BANK

EARNINGS UPDATE

Founder Member of the Nairobi Securities Exchange

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DYER & BLAIR
INVESTMENT BANK

WE KNOW. YOU KNOW.

I&M HOLDINGS 3Q18 EARNINGS UPDATE

Dear All,

I&M Holdings released their 3Q18 results, recording an **18.3% y-o-y rise in PAT to KES 5.9 BN**. Profit Before Tax (PBT) rose 11.9% y-o-y to KES 8.3 BN. Attributable income went up 21.4% y-o-y to KES 5.5 BN. EPS for the period stands at KES 13.36 (up 21.4% y-o-y) while trailing EPS stands at KES 18.72 (up 32.7% y-o-y). Annualized ROA and ROE declined 4 bps and 51 bps y-o-y to 2.7% and 15.7%.

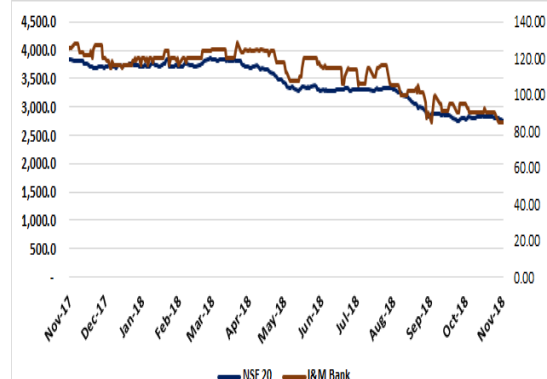
Below please find key highlights:

I&M Holdings' 3Q18 net interest income declined 4.9% y-o-y to KES 10.3 BN as net interest margin declined 60 bps y-o-y to 5.8%. Interest expense rose 16.8% y-o-y to KES 7.6 BN surpassing a 3.3% y-o-y growth in interest income to KES 17.9 BN. The increase in interest expense was occasioned by a 14.5% and 114.8% y-o-y increase in interest on customer deposits and interest on deposits and placements from banking institutions to KES 6.4 BN and KES 467.0 MN respectively. Annualized cost of funds declined 96 bps y-o-y to 3.7%. The 3.3% y-o-y increase in total interest income was on account of a 4.0% y-o-y rise in interest on customer loans and advances to KES 13.7 which was hampered by a 0.9% y-o-y drop in interest on government securities to KES 4.0 BN. Annualized yield on interest earning assets declined 156 bps y-o-y to 9.5%.

Non-funded income grew 38.4% y-o-y to KES 5.6 BN. Total fees and commission rose 30.1% y-o-y to KES 3.1 BN, to contribute 55.3% of total non funded income down from a 58.9% contribution in the same period last year. Forex income rose 42.6% y-o-y to KES 1.9 BN as other operating income increased 84.0% y-o-y to KES 559.0 MN. Non funded income reliance rose by 800 bps y-o-y to 35.1%. This is in line with the bank's strategy that is focused on growing non funded income by double digits.

Operating expenses (less loan loss provisions) grew 7.5% y-o-y to KES 10.0 BN. Staff costs rose 8.3% y-o-y to KES 3.1 BN while other operating expenses increased 6.3% y-o-y to KES 2.2 BN.

I&M HOLDINGS 52 WEEK PRICE PERFORMANCE



(Source: NSE, DBIB Research)

PRICE	ABSOLUTE	EXCESS
RETURN	RETURN	RETURN
3 months	-19.3%	-4.3%
6 months	-21.5%	-4.4%
12 months	-33.8%	-6.3%

KEY METRICS

Current Price (KES)	84.75
52 week Range (KES)	129.00-84.75
YTD Return (%)	-26.9
Issued Shares (Mn)	413.4
Market Cap (USD Mn)	341.9

Recommendation	BUY
Trailing EPS (KES)	16.77
NAV (KES)	120.42
P/E (x)	5.05
P/B (x)	0.70
Div Yld (%)	4.1

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Cost to income ratio edged up 23 bps y-o-y (- 69 bps q-o-q) to 39.7%. Bad debt charge declined 1.1% y-o-y to KES 1.9 BN.

Gross non-performing loans (NPLs) increased 94.2% y-o-y (-1.2% q-o-q) to KES 22.1 BN. Interest in suspense increased 48.1% y-o-y (+21.1% q-o-q) to KES 5.0 BN. Total NPL rose 113.6% y-o-y to KES 17.1 BN. Loan loss provisions grew 59.0% y-o-y (+5.4% q-o-q) to KES 5.9 BN. This brings NPLs to KES 11.2 BN, representing a 160.6% y-o-y (-11.4% q-o-q) increase. NPL ratio stands at 11.9% (up 489 bps y-o-y) while NPL coverage ratio stands at 3.2%(up 89 bps y-o-y)

Regional performance breakdown; Kenya, Tanzania and Rwanda contributed 77.7% (down 74 bps h-o-h), 6.6% (-16 bps h-o-h) and 14.6% (-89 bps h-o-h) respectively to total income in 3Q18. During the period, Kenya contributed 75.6% of the group's profit, down from a 96.2% contribution in the corresponding period last year. This shows the rapid growth of regional subsidiaries.

Total assets rose 22.4% y-o-y to KES 289.6 BN. This was mainly on account of a 3.9x y-o-y increase in deposits due from banks to KES 34.1 BN. Customer loans and advances rose 8.6% y-o-y to KES 163.3 BN as investment securities declined 13.0% y-o-y to KES 43.4 BN. Funded income generating potential declined 154 bps y-o-y (118 bps q-o-q) to 86.8%.

Customer deposits grew 27.6% y-o-y (-0.9% q-o-q) to KES 209.0 BN. In 1H18, customer deposits grew 22.9% y-o-y to KES 210.9 BN which we previously pointed out may have been as a result of the previous deadline on the amnesty programme prior to its extension to 30th June 2019. Borrowed funds declined 2.2% y-o-y to KES 12.0 BN. Loans to deposits ratio declined 1,370 bps y-o-y (93 bps q-o-q) to 78.1% while loans to deposits and borrowed funds ratio decreased 1,154 bps y-o-y (+79 bps q-o-q) to 73.9%

Capital adequacy: Core capital to total risk weighted assets (TRWA) declined 739 bps y-o-y to 15.3% against a statutory minimum of 10.5%. Total capital to TRWA stands at 16.9% (793 bps y-o-y), 240 bps above the statutory minimum. Liquidity ratio rose from 45.5% in 1H18 to 47.8% in 3Q18.

In 2017, I&M Holdings adopted a new strategy, 'Imara', that is focused on customers and supported by process optimization, digitization and automation. We are of the view that the new strategy's focus on product diversification through innovation will help grow non funded income. In addition, the upgrade of the bank's core banking system across Kenya, Tanzania, Rwanda and Mauritius is expected to drive efficiency going forward. **On a trailing basis:** I&M Holdings is trading at **P/E** and **P/B** multiple of 5.1x and 0.7x against an industry median **P/E** and **P/B** multiples of **6.3x** and **1.1x** respectively. Trailing ROE and ROA stands at 17.4% and 2.8% against an industry median of 16.5% and 2.2% respectively. We issue a **BUY** recommendation.

PROFIT AND LOSS SUMMARY (KES MN)

Year End: December	9M18	9M17	y-y% ch	3Q18	2Q18	3Q17	y-y% ch	q-q % ch
Interest income	17,880	17,314	3.3	6,225	6,034	4,079	52.6	3.2
Interest expense	(7,595)	(6,501)	16.8	(2,807)	(2,440)	(1,656)	69.5	15.0
Net interest income	10,285	10,814	(4.9)	3,419	3,594	2,423	41.1	(4.9)
Other operating income	559	304	84.0	79	225	(1,149)	(106.9)	(64.8)
Fees and commission income	3,077	2,365	30.1	1,080	965	655	64.9	11.9
Net income from forex dealings	1,924	1,349	42.6	681	649	1,066	(36.1)	5.0
Total non-interest income	5,560	4,018	38.4	1,840	1,839	572	221.9	0.1
Total income	15,845	14,831	6.8	5,259	5,433	2,995	75.6	(3.2)
Less operating expenses	(6,290)	(5,854)	7.5	(2,015)	(2,131)	(798)	152.5	(5.4)
Operating profit	9,555	8,978	6.4	3,244	3,302	2,196	47.7	(1.7)
Bad debt charge	(1,898)	(1,919)	(1.1)	(486)	(833)	(910)	(46.6)	(41.6)
Exceptional items	635	351	80.6	135	377	(245)	(155.0)	(64.2)
Profit before tax	8,291	7,410	11.9	2,893	2,845	1,040	178.0	1.7
Less tax	(2,440)	(2,462)	(0.9)	(910)	(790)	(537)	69.4	15.2
Profit after tax	5,851	4,948	18.3	1,983	2,056	503	294.0	(3.6)
Non controlling interest	326	396	(17.6)	88	348	245	(64.2)	(74.8)
Attributable Income	5,525	4,552	21.4	1,895	1,928	748	153.3	(1.7)
EPS (KES)	13.36	11.01	21.4	5	4.66	1.91	140.4	(1.6)

(Source: Company, DBIB Research)

BALANCE SHEET SUMMARY (KES MN)

Year End: December	3Q18	1H18	3Q17	y-y % ch	q-q % ch
Total shareholder's equity	47,009	45,084.9	43,232	8.7	4.3
Minority interest	2,771	2,729.6	2,579	7.5	1.5
Total Equity	49,780	47,815	45,811	8.7	4.1
Deposits due to other banks	12,360	7,421.9	9,317	32.7	66.5
Customer deposits	209,041	210,898	163,847	27.6	(0.9)
Borrowed funds	12,029	11,886.8	12,298	(2.2)	1.2
Other liabilities	6,386	5,049.2	5,362	19.1	26.5
Total equity and liabilities	289,595	283,070	236,635	22.4	2.3
Central bank balances	15,776	12,881.7	10,370	52.1	22.5
Deposits due from banks	34,111	39,779.7	8,640	294.8	(14.2)
Investment Securities	43,389	36,131.3	49,891	(13.0)	20.1
Financial assets at FV via P & L	10,471	10,233.7	-	N/A	2.3
Customer loans and advances	163,327	162,823.3	150,460	8.6	0.3
Other assets	11853.405	11,125.3	8,384	41.4	6.5
Intangible assets	4,378	4,146.2	4,025	8.8	5.6
Fixed assets	6,289	5,949.0	4,864	29.3	5.7
Total assets	289,595	283,070	236,635	22.4	2.3

(Source: Company, DBIB Research)

INVESTMENT RETURN

	3Q18	1H18	3Q17	y-y bps ch	q-q bps ch
ROA (%)*	2.7	2.7	2.8	(4)	(9)
ROIC (%)*	12.6	13.0	11.0	(34)	157
ROE (%)*	15.7	16.2	14.4	(51)	127

(Source: Company, DBIB Research)

*Annualized

OPERATING PERFORMANCE

	3Q18	1H18	3Q17	y-y bps ch	q-q bps ch
Yield on interest earning assets (%)*	9.5	9.4	11.0	(156)	12
Cost of funds (%)*	3.7	4.2	4.7	(96)	(45)
Net Interest Margin (%)*	5.8	5.2	6.4	(60)	57
Loan -to -Deposits ratio (%)	78.1	77.2	91.8	(1,370)	93
Loan - to -Dep .&Borrowed Funds ratio (%)	73.9	73.1	85.4	(1,154)	79
Funded Income Generating Potential (%)	86.8	88.0	88.3	(154)	(118)
Funded Income Reliance (%)	64.9	64.9	72.9	(800)	5
Cost to income ratio (%)	39.7	40.4	39.5	23	(69)
Pre-tax margin (%)	52.3	51.0	50.0	236	133
PAT margin (%)	36.9	36.5	33.4	357	39

*Annualized

(Source: Company, DBIB Research)

CAPITAL ADEQUACY, LIQUIDITY & ASSET QUALITY

	3Q18	1H18	3Q17	y-y bps ch	q-q bps ch
Core capital/TRWA (%)	15.3	16.5	22.7	(739)	(118)
Min. Statutory Ratio (%)	10.5	10.5	10.5	-	-
Total capital/TRWA (%)	16.9	18.2	24.8	(793)	(133)
Min. Statutory Ratio (%)	14.5	14.5	14.5	-	-
Liquidity Ratio (%)	47.8	45.5	39.5	828	231
Min. Statutory Ratio (%)	20.0	20.0	20.0	-	-
Leverage Ratio (%)	17.2	16.9	19.4	(217)	30
Equity -to -Loans Ratio (%)	30.5	29.4	30.4	3	111
NPL Ratio (%)	11.9	12.1	7.0	489	(16)
NPL Coverage Ratio (%)	3.2	3.0	2.3	89	16
Long Term Debt to Total Liabilities and Equity (%)	4.2	4.2	5.2	(104)	(5)
NTA/share (KES)	2.2	2.1	2.1	12	7
Book value/share (KES)	120.4	115.7	110.8	960	475

**Exclusive of Inter-bank lending

(Source: Company, DBIB Research)

APPENDIX

COMPANY INVESTMENT RATINGS

Buy: Share price may generate more than 15.0% upside over the next 12 months

Overweight: Share price may generate between 5.0% and 15.0% upside over the next 12 months

Hold: Share price may fall within the range of <+5.0/ -10.0% over the next 12 months

Take Profit: Target price has been attained. Look to accumulate at lower levels. Company fundamentals however remain strong

Underweight: Share price may generate between 10.0% and 15.0% downside over the next 12 months

Sell: Share price may generate more than 15.0% downside over the next 12 months, significant business and/or financial risks present, industry concerns

Not Rated: Counter is not within regular research coverage

SECTOR INVESTMENT RATINGS

Overweight: Industry performance better than that of the whole market

Equal weight: Industry performance about the same as that of the whole market

Underweight: Industry performance worse than that of the whole market

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