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Barclays Bank of Kenya: 1H2013 Results Note

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RECOMMENDATION:	NEUTRAL
Market Price (07.08.13)	17.2
Forecasted BVPS: 2013	6.37
3-yr average historical P/B	2.67
Target Price	**17.02**
Upside/ (Downside)	**-1.1%**

Share Statistics

Issued Shares (Mn)	5,432
Market Cap (KES Mn)	93,430
Market Cap (USD)	1,069

Source: NSE

Summary

We remain **NEUTRAL** in our recommendation for the stock. We maintain our earlier FY2013 BVPS forecast of KES 6.37. This gives a **price target KES 17.02**, based on a 3 year historical average P/B.

Key results highlight include the following:

- **Dip in profitability:** The bank reported a 0.8% drop in profit before tax from KES 6.3 billion (1H2012) to KES 6.2 billion (1H2013)
- **Restructuring caps growth in OpEx:** The total operating expense dropped marginally by 0.6% to KES 6.9 billion. However, despite the staff rationalization, we note that staff costs went up by KES 37 million during the period in review
- **Reduced momentum in loan book growth in 2Q2013:** We observe that the momentum that had begun in 1Q2013 slowed down coming into 2Q2013
- **A hit on asset quality:** The gross non-performing loans (GNPLs) grew by 4.8% to KES 3.9 billion (2Q2013) despite the fact that the loan book shrank during the same period
- **Interim dividend slashed:** As we have alluded to in previous communications on the bank, we note that the interim dividend was slashed from KES 0.30 (1H2012) to KES 0.20 (1H2013)

Year to 31 Dec	2011A	2012A	2013F
Net Income (Kshs Mn)	8,073	8,741	9,266
EPS (Kshs)	1.49	1.61	1.71
BVPS (Kshs)	5.38	5.45	6.37
P/E x	8.78	9.79	10.08
P/B x	2.4	2.9	2.7
ROE	27.6%	29.5%	26.8%
ROA	4.8%	4.7%	4.7%
C/I Ratio	51.6%	52.0%	50.0%

Key Results Highlights

Income Statement (KES '000)	1H2012	1H2013	% Change
Interest income	10,634,460	10,457,145	-1.7%
Interest expense	1,661,076	1,225,780	-26.2%
Net Interest Income	**8,973,384**	**9,231,365**	**2.9%**
Non-interest income	4,723,014	4,491,906	-4.9%
Total Income	**13,696,398**	**13,723,271**	**0.2%**
Operating expenses	6,923,791	6,879,108	-0.6%
Loan loss provision	458,922	581,154	26.6%
PBT	**6,313,685**	**6,263,009**	**-0.8%**
PAT	**4,267,039**	**3,732,269**	**-12.5%**
EPS	***0.79***	***0.69***	
DPS	***0.30***	***0.20***	
Cost/Income Ratio	***50.6%***	***50.1%***	

Source: Company Release

Balance Sheet (KES '000)	FY2012	1H2013	% Change
ASSETS			
Kenya government securities	34,344,765	42,978,449	25.1%
Loans & advances to customers	104,204,295	107,050,039	2.7%
Total Assets	**184,825,892**	**184,583,217**	**-0.1%**
LIABILITIES			
Customer deposits	137,915,391	138,684,868	0.6%
Deposits from local & foreign institutions	157,028	186,054	-
Other liabilities	11,604,562	10,709,757	-7.7%
Total Liabilities	**155,242,443**	**155,375,028**	**0.1%**
Shareholders' Funds	**29,583,448**	**30,187,302**	**2.0%**
Loan /deposit Ratio	***74.6%***	***77.1%***	
Total Capital/Total Risk-Weighted Assets	**25.8%**	**16.0%**	
Liquidity Ratio	**46.8%**	**44.9%**	

Source: Company Release

PBT dips by 0.8%

Dip in profitability: The bank reported a 0.8% drop in profit before tax from KES 6.3 billion (1H2012) to KES 6.2 billion (1H2013). Profit after tax dipped by 12.5% to KES 3.7 billion after accounting for the restructuring costs amounting to KES 788 million.

Funded income continue being under pressure

Sustained decline in funded income: Total interest income dropped by 1.7% from KES 10.6 billion (1H2012) to KES 10.5 billion (1H2013). This was mainly attributed to a decline in interest income on loans and advances (-0.6%), a drop in interest income from government securities (-1.2%) and a 15.5% drop in other interest income. The yield on loans dropped by 44 bps (from 7.3% to 6.8%).

Yield on government securities down by 134 bps

Yield on government securities also declined by 134 bps from 6.4% (1H2012) to 5.1% (1H2013). Consequently, interest income derived from government securities dropped by 1.2% to KES 2.3 billion.

Going forward, we are still not convinced about the bank's efforts in growing the funded income.

Interest expense down by 26.2%

Lower interest expense: The total interest expense declined by 26.2% to KES 1.2 billion in 1H2013 compared to KES 1.7 billion in a similar period in 2012. This was mainly driven by a 14.5% drop in expenses on customer deposits, 78.7% decline in expenses on wholesale funds as well as a 49.4% decline in other interest expenses.

Cost of customer deposits down by 24 bps

The cost of customer deposits was down 24 bps to 0.8%, which resulted in the drop in interest expenses on customer deposits. The bank benefited from the overall decline in the cost of funds in the economy, with the Central Bank Rate (CBR) dropping from 9.5% in January 2013 to 8.5% by end of June 2013.

The cost of wholesale funds was down 79 bps to 1.1%.

29.1% drop in forex trading income pushes down non-funded income

Non-funded income down by 4.9%: The total non-funded income was down by 4.9% to KES 4.5 billion. This was mainly attributed to a 29.1% drop in forex trading income from KES 1.4 billion (1H2012) to KES 969 million (1H2013).

The growth of 19.9% in fee and commission income from loans was not sufficient to cover for the drop. As a matter of fact, the loan book shrank by KES 1.2 billion in 2Q2013, implying no additional loans were written during this period.

OpEx down by 0.6%

Restructuring caps growth in OpEx: The total operating expense dropped marginally by 0.6% to KES 6.9 billion. However, despite the staff rationalization, we note that staff costs went up by KES 37 million during the period in review. Management indicated that they will increase head count within their sales and marketing department. This may see staff costs rise, albeit marginally. In addition, management intends to continue re-balancing between their front office and back office staff.

Reduced momentum in loan book growth

Reduced momentum in loan book growth in 2Q2013: We observe that the momentum that had begun in 1Q2013 slowed down coming into 2Q2013. From a funding perspective, the bank was not able to marshal enough loanable funds.

Deterioration of asset quality

A hit on asset quality: A quarter/quarter analysis reveals that the asset quality of the bank deteriorated. The gross non-performing loans (GNPLs) grew by 4.8% to KES 3.9 billion (2Q2013) despite the fact that the loan book shrank during the same period.

Capital adequacy ratios come under pressure

Pressure on capital adequacy ratios: The total capital/total risk-weighted assets dropped significantly from 25.8% (FY2012) to 16.0% (1H2013). This is only 2.5% above the minimum statutory requirement by the Central Bank of Kenya (CBK). The ratio of core capital/total risk weighted assets was only 4.3% above the minimum required ratio of 10.5%.

The bank will need to match growth in profitability with any significant growth in loan book and other 'risky'assets because of the shrinking capital adequacy levels. Absent of a significant growth in profitability, we expect the bank to source for additional capital injection in the medium term.

Interim dividend slashed

Interim dividend slashed: As we have alluded to in previous communications on the bank, we note that the interim dividend was slashed from KES 0.30 (1H2012) to KES 0.20 (1H2013). Previously, the bank slashed the effective annual dividend declared in F2012 to KES 1.00 compared to KES 1.50 declared in FY2011. Going forward, we still maintain that the bank may face challenges in terms of dividend distributions if profitability does not improve, especially in light of the additional capital requirements by CBK.

Outlook

We are still concerned about bank's ability to grow funded income

We remain concerned about the ability of the bank to grow its income, especially the funded income. Barclays has a wide network coverage in terms of ATMs (230) and branches (119 by the end of 2012).

We are still not optimistic of the bank's strategy, or lack of it thereof, in growing this top line income. Management alluded to intentions of looking for new business opportunities in bancassurance, SMEs, corporate and investment banking (especially in the energy and oil industry).

In addition, we are yet to see the impact the integration of African operations will have on the local outfit.

We remain NEUTRAL in our recommendation

Based on the foregoing, we remain **NEUTRAL** in our recommendation for the stock. We maintain our earlier FY2013 BVPS forecast of KES 6.37. This gives a **price target KES 17.02**, based on a 3 year historical average P/B.