IMARA INVESTING IN AFRICA

Securities

**LETSHEGO HOLDINGS LTD- H1 16 RESULTS**

**Price: BWP 2.09**
**PBV: 1.11x**
**PER (TTM): 6.07x**
**Earnings Yield (TTM): 16.27%**
**Dividend Yield (TTM): 7.52%**
**Recommendation: BUY**

# Equity Research
## Botswana
## September 2016
## Results Scorecard

**Operational expenses weigh down profits……**

**Total revenue exceeds BWP 1.0bn:** An 11.17% increase in Letshego's interest income to BWP 952.3m (H1 15: BWP 859.6m) underpinned the group's 8.86% growth in total revenues to BWP 1.1bn (H1 15: BWP 992.8m). NIR, contrastingly, shed 3.54% due to a 13.31% decline in income from other operations, the latter as sundry income in particular shed 69.16% to BWP 7.2m. After accounting for the interest expense of BWP 178.2m (H1 15: BWP 171.3m), operating income fell to BWP 902.6m (H1 15: BWP 821.5m). The acquisition of *FBN Microfinance Bank Limited* (Nigeria) contributed the most (33.16%) to the group's 9.87% y-o-y growth in operating income. On a like for like basis, (i.e. excluding the Nigeria acquisition), growth would have been 6.60% y-o-y. Operations in Tanzania registered a 21.29% y-o-y growth and Letshego's home market, Botswana, which contributed 34.38% to operating income, exhibited a slower growth rate of 4.09% against the backdrop of a tough economic and low interest rate environment. The depreciation of the metical saw the Mozambican division record a 15.20% decrease in net operating income; while the Namibia, Other Southern Africa, and Other East Africa segments grew net income by 6.79%, 14.63%, and 9.70%, respectively.

**Higher asset yields improve NIMs:** Our calculated NIMs improved by 361bps to 25.20% from 21.59% at H1 15, mainly attributable to greater calculated net interest spreads y-o-y of 17.31% at H1 16 vs. 12.46% at H1 15. Our derived average asset yields increased by 4.56pp to 30.75%, while average cost of funding remained relatively flat, down by 0.29pp to 13.44% at H1 16.

**Operational expenses weigh down earnings:** A 52.80% increase in wages and salaries partly attributable to the group's larger labour force subsequent to the East and West Africa acquisitions, resulted in higher employee costs (+51.28%). This, in concert with a 50.61% rise in other operational expenses, (partly attributed by management to the introduction of USSD mobile banking in Mozambique and Rwanda and the introduction of a technology-driven agency banking model that uses biometric authentication in Mozambique), saw total operational costs increase by 59.66% to BWP 345.0m. This translated into a notable 10pp increase in the cost to income ratio to 38%, above the company's 35% long term target. Impairment charges decreased by 2.48% y-o-y to BWP 68.6m and thus cost of risk was marginally lower at 2.40% (H1 15: 2.50%). PBT declined by 6.42% to BWP 489.1m.

**EPS shrinks by 4.32%:** The effective tax rate declined by 238bps to 20.65%, moderating the PAT drop relative to PBT, as the former fell by 3.55% to BWP 388.0m. TTM ROaE and ROaA thus closed at 18.46% and 10.99% vs. 18.89% and 12.45% at H1 15, respectively. H1 16 EPS fell by 4.32% to 17.7t vs. 18.5t at H1 15. However, attributable earnings remained relatively flat (-0.47% y-o-y) at BWP 369.3m, courtesy of a higher reduction in earnings due to minorities. The company declared an interim dividend of 9t per share, maintaining the company's 50% pay-out ratio. The LDR for the dividend is 16 September 2016 and it will be paid on 23 September 2016.

| Income Statement (BWP'm) | H1 16 | H1 15 | %change |
|---|---|---|---|
| Net interest income | 774.12 | 688.31 | 12.47% |
| Non-interest income | 128.50 | 133.21 | -3.54% |
| Total income | 902.61 | 821.52 | 9.87% |
| Impairments | -68.58 | -70.33 | -2.48% |
| Operating expenses | -344.97 | -228.60 | 50.91% |
| Profit before tax | 557.64 | 592.92 | -5.95% |
| Attributable earnings | 387.96 | 402.23 | -3.55% |
| EPS (thebe)* | 34.40 | 34.20 | 0.58% |
| DPS (thebe) | 9.00 | 9.00 | 0.00% |
| NAV/share (thebe) | 187.98 | 186.11 | 1.01% |
| **Balance sheet** | **H1 16** | **FY 15** | |
| Cash on hand | 385.30 | 526.29 | -26.79% |
| PP&E | 72.93 | 76.03 | -4.08% |
| Loans and Advances | 6,202.97 | 6,311.68 | -1.72% |
| Total Assets | 7,270.74 | 7,462.44 | -2.57% |
| Deposits | 173.51 | 231.86 | -25.17% |
| Cash collateral | 42.95 | 44.67 | -3.85% |
| Borrowings | 2,751.73 | 2,768.41 | -0.60% |
| Shareholders funds | 4,109.29 | 4,182.03 | -1.74% |
| **Ratios** | **H1 16** | **H1 15** | |
| Net interest margin* | 25.20% | 21.59% | |
| Cost-income | 38.22% | 27.83% | |
| non interest- total income | 14.24% | 16.22% | |
| Cost of risk | 2.40% | 2.50% | |
| RoaE* | 18.46% | 18.89% | |
| RoaA* | 10.99% | 12.45% | |
| Div cover (x) | 3.82 | 3.80 | |
| Payout ratio | 52.33% | 52.63% | |

*Source: Company Financial Statements and Imara Capital Securities Botswana*

**Table 1: Regional PBT Portfolio**

| | H1 16 (BWP'm) | H1 15 (BWP'm) |
|---|---|---|
| Botswana | 251.7 | 216.4 |
| Namibia | 163.4 | 156.2 |
| Mozambique | 58.5 | 73.9 |
| *Other Southern Africa | 28.4 | 30.0 |
| Tanzania | 55.9 | 49.7 |
| *Other East Africa | 27.1 | 46.2 |
| West Africa | - | (7.3) |
| Holding Company/eliminations | (49.8) | (88.6) |
| **Total** | **489.1** | **522.6** |

*Source: Company Financial Statements*

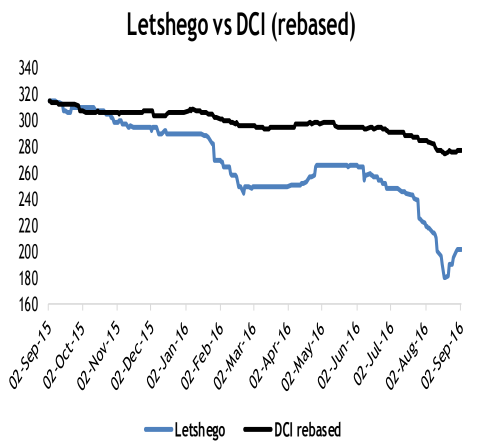
**Balance sheet remains solid:** During the period under review, total assets decreased by 2.57% to BWP 7.3bn vs. BWP 7.5bn at FY 15, mainly on the back of a 1.72% decline in advances to customers. The latter accounted for 85.31% of total assets. The drop was largely attributable to the 2.92% decrease in the Southern Africa segment's customer loans and advances which offset the 2.46% growth attained in the East and West Africa segments (as shown in Table 2). The group non-performing loans ratio remained relatively flat at 8.48% (FY 15: 8.41%). The Southern Africa region's NPL ratio rose 20bps to 8.0% while East - West Africa's improved to 10.0% vs. 10.6% at FY 15. Customer deposits fell by 39.99% ytd to BWP 92.7m, attributed to the timing of the maturity of some corporate deposits. Borrowings were flat ytd, registering a marginal 0.60% decline to BWP 2.8bn, with note programmes accounting for 51.46% of the total. The loans to deposits and borrowings ratio stood at 221.02% (FY 15: 218.76%), while loans to capital was relatively flat at 157.33% (FY 15: 156.94%).

**We maintain our BUY recommendation; Target Price under review**. Having fallen by 28.18% year-to-date, Letshego's current share price of BWP 2.09 puts it on PER and PBV ratios of 6.07x and 1.11x, respectively, which are generally lower than its deposit taking peers in Botswana as has been the historical trend given its perceived higher risk business model. Going forward, the naira devaluation will negatively impact *FBN Microfinance Bank Limited's* numbers, more specifically when translating the segment's earnings into pula terms, however, the segment currently only contributes 2.98% and 0.79% to group operating profits and net advances, respectively and therefore should have minimal impact on overall group earnings. Overall, we expect Letshego's mainstay operation Botswana to continue being the key driver to the group's PBT growth while other operations improve earnings. We also expect group CIR to remain elevated above the target range in the short to medium term while the company expands operations, but to normalise over time when the acquisitions' revenues catch up with costs. Letshego continues to expand its income streams by pursuing geographic, customer and product mix diversification. Subsequent to the period end, Letshego Namibia was awarded a deposit taking license, taking the group's deposit taking licenses to 5. Generally, we are positive on the company's growth and diversification story and thus maintain our **BUY** call.

**Table 2: Regional Loan Book Portfolio**

| | H1 16 (BWP'm) | FY 15 (BWP'm) |
|---|---|---|
| Botswana | 2 110.2 | 2 147.7 |
| Namibia | 1 470.6 | 1 391.5 |
| Mozambique | 803.9 | 1 065.3 |
| *Other Southern Africa | 472.0 | 393.9 |
| Tanzania | 433.5 | 395.8 |
| *Other East Africa | 863.7 | 847.6 |
| West Africa | 49.2 | 69.8 |
| | | |
| **Total** | **6 203.0** | **6 311.7** |

***Source: Company Financial Statements***




***Source: BSE***

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