

### Equity research | Botswana | Banks and Financial Services

## 1H11 RESULTS NOTE

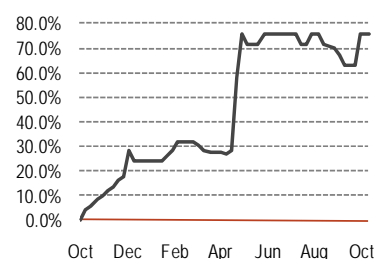
Letshego Holdings (Letshego) released its 1H11 results (July 2010) reporting increases of 33% y/y (-1.7% h/h) and 34.4% y/y (-2.4% h/h) in basic and diluted EPS to BWP 0.121 and BWP 0.118 respectively, slightly above our diluted EPS forecast of BWP 0.11 (in our Trading Update on 14 September 2010). The key drivers of the performance were Botswana and Namibia. No interim dividend was declared, in line with the preceding two reporting periods.

- Impressive 1H results with EPS rising substantially on solid performance in key markets.** Net interest income increased by 29.1% to BWP 325.4m, on the back of a 23.8% increase and 28.9% reduction in interest income and interest expense respectively. The growth was underpinned by a 22% y/y (10.7% h/h) increase in loans and advances to BWP 1.9bn, while a 23.6% y/y (7.6% h/h) decrease in borrowings resulted in the reduction in the interest expense. Due to low rates, the net interest margin expanded by 520bp to 36% and is probably at its highest due to a low gearing. Letshego's loans are fixed rate, whereas borrowings are mostly floating rate. Total operating income thus grew by 24.9%. Operating expenses declined by 3.9%, against a 15% reduction and 10% increase in staff costs and other operating expenses respectively. We believe the reduction in staff costs was largely due to the sale of Legal Guard, which was concluded at the close of FY10. As a result, the cost-to-income ratio reduced by 600bp to 19.9%. Impairments declined by 18.5%, reducing the impairment ratio by 110bp to 1.8% of average loans. Operating profit increased by 39.8%, while PAT growth was lower at 38.5% on the back of a higher effective tax charge (25.4% versus 24.7% in 1H09). EPS growth was however reduced by a 4.1% share dilution during the period. Important to note is that 1H10 results include the Legal Guard business whereas 1H11 results do not. Legal Guard contributed BWP 7.5m to PBT in 1H09 and was disposed off at the end of FY10.
- Botswana continues to shine, albeit with slowing growth.** Despite an intensely competitive market, a consumer under debt strain and a large market share, Botswana still managed to register growth of 22% and 41% y/y in loans and PBT respectively. However, on a h/h basis, loan growth is showing signs of slowing since 1H10. 2H11 loan growth may benefit from the recent increase in civil service salaries (by between 9.5%-10%), however, management state in their commentary there has been "a significant increase in the competitive environment during August and September 2010". There have been no further developments regarding new regulations by the Non-Bank Financial Institutions Regulatory Authority (NBFIRA), although management indicates that the proposed levies and fees are an area of concern.
- Namibia proving to be a good investment.** Letshego Namibia continues to benefit from the additional funding received from group level, with the loan book surging 144.3% y/y (59.9% h/h) to BWP 259m while PBT grew 216.7% y/y (14.6% h/h). Letshego Namibia's loans have grown more than six-fold since the acquisition of Eduloan in December

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|                                   |      |         |
|-----------------------------------|------|---------|
| Current price                     | BWp  | 2.0     |
| Market cap                        | BWpm | 3,682.8 |
|                                   | USDm | 565.32  |
| Daily value traded (last 12 mths) | BWpm | 1.33    |
|                                   | USDm | 0.2     |

### PRICE PERFORMANCE



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2008, and we believe this momentum will continue into FY12. Loan growth will be in excess of a 100% in FY11 while PBT growth will likely double. A significant reduction in impairments was recorded in 1H11 as impairments reduced to 2.9% of average loans against 6.5% in 1H09. We believe 1H09 impairments were inflated by a clean-up of the loan book post the acquisition transaction.

- **Other operations affected by operational deficiencies.** Tanzania was affected by administrative requirements imposed by the Central government and District authorities. Zambia continues to see high impairments (27.6% of loans), with no new loans since May 2010. Swaziland has not recovered from the interruption from the establishment of a central registry, but lending has resumed in September 2010. Uganda has made a u-turn, reporting a 22.2% h/h rise in loans and growing PBT to 7.6m from a loss of BWP 2.1m in 1H09.
- **Outlook.** The outlook for Letshego remains positive in the key markets, while marginal operations will likely not increase their contribution to group PBT significantly in 2H10. We forecast 2H11 EPS of BWP 0.14 (FY11: BWP 0.26). The ability to gear the balance sheet (current debt-to-equity ratio of 22.7%) provides the potential for real earnings growth over the medium term even if the core Botswana market experiences lower loan growth and margin pressure. At 1H11 the group had only drawn down BWP 106m (USD 16m) from the BWP 240m (USD 36m) convertible note facility.
- **Valuation.** Letshego is currently trading on a trailing PE and PB of 8.6x and 1.8x respectively. Recent price action on the counter has seen its price increase to BWP 2.00 (our fair value) and 8.5% below our 12mth target price of BWP 2.17.

## SUMMARY TABLES

### INCOME STATEMENT

| 6m to July (BWPm)                          | 1H10         | 1H11         | %ch   |
|--|--------------|--------------|-------|
| Interest income                            | 277.4        | 343.4        | 23.8  |
| Interest expense                           | -25.3        | -18.0        | -28.9 |
| <b>Net interest income</b>                 | <b>252.1</b> | <b>325.4</b> | 29.1  |
| Other income                               | 59.6         | 64.1         | 7.4   |
| <b>Total income</b>                        | <b>311.7</b> | <b>389.5</b> | 24.9  |
| Operating expenses                         | -80.6        | -77.4        | -3.9  |
| <b>Operating income before impairments</b> | <b>231.1</b> | <b>312.0</b> | 35.0  |
| Impairment of advances                     | -18.8        | -15.3        | -18.5 |
| <b>Profit before tax</b>                   | <b>212.3</b> | <b>296.7</b> | 39.8  |
| Income tax                                 | -52.5        | -75.4        | 43.6  |
| <b>Profit after tax</b>                    | <b>159.8</b> | <b>221.4</b> | 38.5  |
| Weighted shares in issue(m)                | 1,761.9      | 1,833.3      |       |
| Year end shares in issue(m)                | 1,824.7      | 1,841.4      |       |
| Basic EPS (BWP)                            | 0.09         | 0.12         | 33.0  |
| Diluted EPS (BWP)                          | 0.08         | 0.12         | 47.5  |

Source: Company data, African Alliance

### BALANCE SHEET

| 6m to July (BWPm)                   | 1H10           | 1H11           | %ch         |
|-------------------------------------|----------------|----------------|-------------|
| Cash and cash equivalents           | 105.4          | 112.6          | 6.9         |
| Loans and advances                  | 1,532.0        | 1,862.9        | 21.6        |
| Fixed assets                        | 7.3            | 5.8            | -20.8       |
| Other assets                        | 54.8           | 86.5           | 57.9        |
| <b>Total assets</b>                 | <b>1,698.0</b> | <b>2,069.3</b> | <b>21.9</b> |
| Trade creditors                     | 91.0           | 153.9          | 69.0        |
| Income tax                          | 20.9           | 28.8           | 37.7        |
| Borrowings                          | 456.8          | 348.8          | -23.6       |
| Shareholders' equity                | 1,129.3        | 1,537.9        | 36.2        |
| <b>Total equity and liabilities</b> | <b>1,698.0</b> | <b>2,069.3</b> | <b>21.9</b> |

Source: Company data, African Alliance

### KEY RATIOS

| Key ratios (%)       | 1H10 | 1H11 | FY10 |
|----------------------|------|------|------|
| Annualised ROaA      | 25.0 | 31.5 | 27.9 |
| Annualised ROaE      | 28.3 | 33.2 | 36.7 |
| Debt to equity ratio | 40.4 | 22.7 | 28.0 |
| NIM                  | 30.8 | 36.0 | 33.7 |
| NIR/Total income     | 19.1 | 16.4 | 18.6 |
| Cost-to-income ratio | 25.9 | 19.9 | 20.8 |

Source: African Alliance

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