Securities (Pty) Ltd.
Member of the NSX

BANK WINDHOEK HOLDINGS
1H16 Results Review
APRIL 2016

Bank Windhoek Holdings

1H16 Results Review

Target Price (c)	1880
Current Price (c)	1696

Year End 30 June	2014A	2015A	F2016	F2017	F2018
Net interest income (N$m)	1,057	1,267	1,442	1,599	1,792
Non-interest income (N$m)	680	812	916	1,046	1,206
Profit (N$m)	654	753	894	989	1,182
HEPS (c)	127	150	179	198	236
P/E (x)#	13.4	11.3	9.5	8.6	7.2
DPS (c)	44.0	53.0	64.0	71.0	85.0
DY (%)*	2.6	3.1	3.8	4.2	5.0
P/B (x)*	2.7	2.3	2.0	1.7	1.5

Recommendation	BUY
NSX Code	BWH
Market Cap (N$m)	8570
Shares in Issue (m)	505.3
Free float (%)	26.5
52 week high (c)	1710
52 week low (c)	1520
Expected Total Return	12.8%

Source: BWH, IJG
#Based on HEPS and current share price
**Based on current share price*

BWH released its results for the first half of the financial year ending 30 June 2016. The firm recorded exceptional growth over the period. Profit expanded by 26.4% when compared to 1H15 levels. Earnings per share grew 26.8%, while dividends per share grew 25%. Strong income growth was driven by both net-interest and non-interest income, with the former expanding by 21.0%, and the latter by 21.7%. The results are very much in-line with our forecasts for the year, and given that the second half of the financial year often offers marginally better results than the first, we are well positioned to see a positive surprise in the full year results.

Interest income expanded by 23.7% year on year, while interest expenses increased by 26.7%, resulting in growth in the net interest income of 21.0%. As such, net interest income for 1H16 was N$727.9 million. The average cost of funding for the bank increased from 4.91% in 1H15, to 5.48% in 1H16. At the same time, the average interest rate on advances increased from 10.44% to 11.15%. As such, the net interest margin of the bank has improved by 14 basis points.

Non-interest income increased by 21.7% to N$481.4 million in 1H16, from N$395.7 million the previous year. The increase is mainly due to strong growth in income from trading activities, which included income earned from the Kwanza trading activities. Non-interest income now makes up 40.9% of total operating income, from 40.2% in the preceding year.

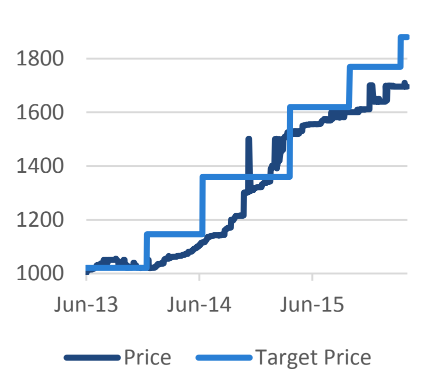
While strong growth was seen in income, operating expenses too grew, but at a much slower rate, of 13.8%, to N$578.7 million. This resulted in an improvement in the cost-to-income ratio of the bank, which improved from 51.7% to 49.1%. The increase in costs was largely driven by increased staff costs.

The group's total asset grew by 19.1%, driven by the growth in loans and advances of 15.8%, which according to the company is mainly due to growth in overdrafts and mortgage loans. Funding increased by 18.7%, driven by a 13.5% increase in debt securities in issue, a 12.5% increase in deposits and loans from the International Finance Corporation and Deutsche Investitions- und Entwicklungsgesellschaft of N$920m and N$250m respectively. Due to the strong funding increase, the loan-to-funding ratio of the bank improved to 96.1%, from 98.5%. However, the loan-to-deposit ratio weakened somewhat, and now stands at 110.6%, from 108.4%, illustrating a higher reliance on more costly, but often more desirable duration, debt-financing.

The group remains well capitalised with a total risk-based capital adequacy ratio of 14.5%, down from 15.7% in 1H15, but still well above the minimum regulatory requirement of 10%.

The company announced an interim dividend of 30 cents per share, up 25% from the interim dividend of 1H15. This implies a payout ratio of 32.9%, down from 33.4% in 1H15.

BWH Share Price



Dividends

An interim dividend of 30 cents per ordinary share was declared on 10 February 2016 for the period ended 31 December 2015.

Analyst

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Disclaimer

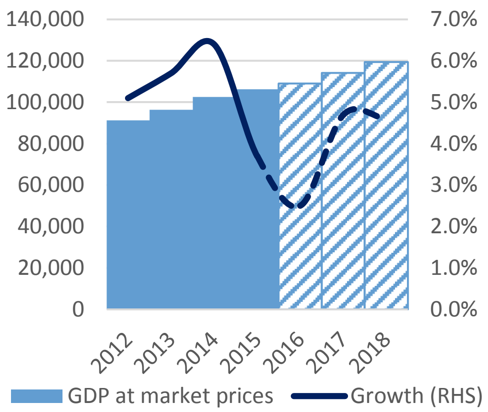
The report author holds a small long position in Bank Windhoek Holdings.

Noteworthy is the fact that the bank is in the process of undergoing a management change, with current MD of both Bank Windhoek Holdings and Bank Windhoek Limited set to complete his contract in June 2016. Mr. de Vries was appointed as Managing Director of Bank Windhoek Holdings and Bank Windhoek with effect from 6th June 2011 for a period of three years. In July 2014, his contract was extended until June 2016. The role filled by Mr. de Vries has now been split into two positions, with Mr. Thinus Prinsloo taking over as MD of Bank Windhoek Holdings from 1 January 2016, and Ms. Baronice Hans taking over as MD of Bank Windhoek Limited. Mr. Prinsloo has been a part of the CIH group and Bank Windhoek Holdings, in various roles, since 2011. Ms. Hans moved to Bank Windhoek from Standard Bank, where she was the Executive Director and Head Personal and Business Banking.

For the analyst's perspective, Mr. de Vries and his team did an excellent job of growing and developing the bank, more than doubling its operating profit between FY11 to FY15. While we have no reason to think that the new team will be any less effective at running and growing the bank, the change in top leadership and loss of an experienced and proven MD, and replacement with a less well known individual, warrants monitoring by shareholders.

For the purpose of valuing the company, we establish a **cost of equity, of 12.9%,** up from 11.6% in 1H15, largely on account of a major increase in the risk-free rate. Based on this cost of equity, a highly conservative **long-term growth rate for the company of 9.5%,** and a **dividend pay-out ratio of 36%**, we believe a **PE of 10.5x can be justified** on this share. Given **expected earnings growth of 18.7% in FY16**, taking **total earnings to c179/share**, we derive **a target price of N$c1880/share**. Coupled with an **expected final dividend of 34cps**, we expect a **total return of 12.8% in 2H16**. Based on the stellar performance of the bank in 1H16 and the expected growth in 2H16, coupled with expected changes to local capital regulations for pension funds, we **maintain** a strong **BUY recommendation on Bank Windhoek Holdings**.

Namibia Real GDP (N$ Million)



Source: NSA, IJG Securities

Macro backdrop

The Global and Namibian Economies

Growth environment:

The Namibian economy performed admirably over the five years from 2010 to 2014. Over this period, growth averaged over 5.6%, compared to average growth since independence of 4.3%. This abnormally strong growth was driven by three key factors. Firstly, Namibia has been through a prolonged period of historically low interest rates which drove unprecedented uptake of credit by the private sector; secondly, major fiscal expansion from 2011 until now, driving money into the pockets of the public, as well as major civil works programmes; finally, unprecedented levels of foreign direct investment into the country, driven by the consecutive construction of three FDI funded mines.

These factors resulted in a consumption and construction boom, which saw a major expansion in the local economy, with the economy rebasing from a N$83 billion dollar economy to a close to N$160 billion dollar economy in a period of six years.

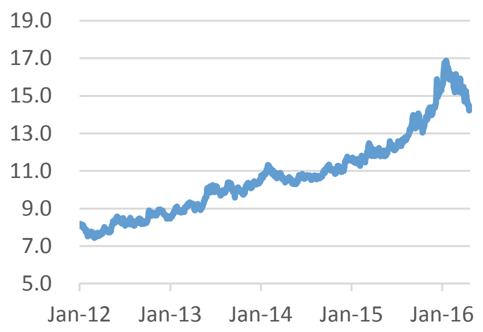
However, subsequently, the macroeconomic environment in Namibia has started to deteriorate, as a combination of factors have come together to dampen growth and drive imbalances within the local economy. The unwinding of historically low interest rates, lower levels of Government spending, less foreign direct investment into the country, fewer Angolan retail tourists, a reduction in diamond output, weak commodity prices, drought, potential water supply constraints and a high base, are a notable few. As such, growth for the current year is expected to stand well below the recent levels, however off the ever-higher base.

Inflation

Inflation expectations for the upcoming fiscal year are notably higher than was the case in 2015. There are a number of reasons for this. Firstly, major rand weakening through 2015 has driven up the cost of imports into the Common Monetary Area (CMA) in rand terms; secondly, oil prices, which fell dramatically through 2014 and 2015, now appear to be stabilising, and the pass-through of base effects is likely to see an upward rebasing in inflation; third, rand weakness and other factors have driven up costs for many services in the country, including many critical utilities such as electricity and water; fourth, drought and poor harvests in the region mean that food prices are likely to increase, particularly if basic grain imports are required; and fifth, increasing interest rates are likely to see some pass-through of increased borrowing costs to consumers, and reduce consumer disposable income.

As a result of the above, the real value spend of consumers is likely to be reduced, as disposable incomes come under pressure. This pressure is likely to drive increased demand for credit, as well as large wage settlement demands, both in the private and public sectors.

USDZAR



Source: Bloomberg

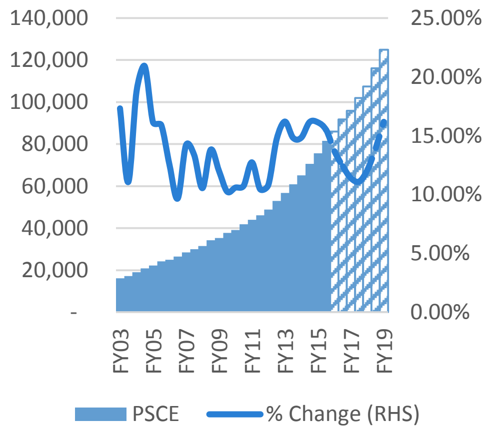
Exchange Rate

After major Rand weakness through 2015, some Rand recovery is expected in 2016 and beyond. This is largely due to the fact that the Rand has now depreciated far from fair value, as calculated using long term purchasing power parity. The Rand weakness has been largely driven by weak export numbers and thus a sizable current account deficit; increasing interest rates in the US and thus fund-flow reversals out of EM economies; and weak sentiment following a series of political gaffes. However, while the South African political and economic situation remains fragile on an absolute basis, on a relative basis, the country is faring little worse than much of the rest of the world, and continues to offer relatively attractive yields to international investors.

Funding costs

The cost of funding has increased across the board over the past 12 months, as demand for government securities has weakened following major increases in the supply of debt, and limited demand for such through the interest rate hiking cycle. As such, spreads have widened across Government yield curve. As most of the financial entities looking to raise debt securities are considered higher risk than Government, these entities have had to pay up for debt funding. On the deposits side, slow increases in interest rates in Namibia and South Africa have seen deposit rates increasing, albeit fairly marginal.

Private Sector Credit Extension



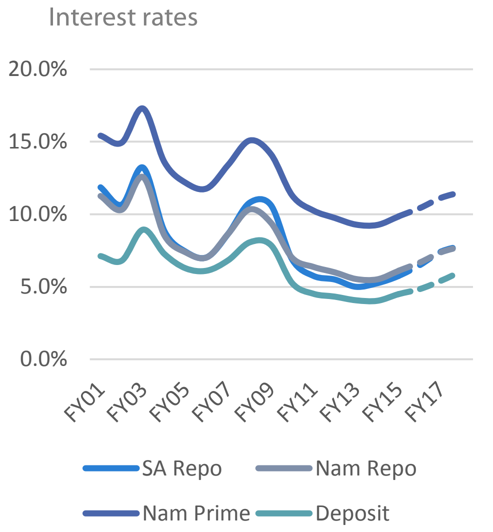
Source: Bank of Namibia, IJG Securities

Credit demand and supply

As we move through an interest rate hiking cycle, private sector credit extension, one of the key drivers of growth in the Namibian economy over recent years, is likely to come under ever increasing pressure. Strong growth in credit extension through the trough of the cycle has left many consumers highly indebted, and many corporates with heavily leveraged balance sheets.

In addition, after an extended period of extremely low interest rates, liquidity in the Namibian banking sector has fallen to relatively low levels as sustained long periods of low interest rates mean that borrowing has been incentivised, while saving has been disincentivized. This has put the loan to funding ratios of the commercial banks under a fair amount of pressure. In addition to this, Government, previously a key provider of liquidity in market came under severe financial pressure in the back end of 2015, and thus did not have the funds that they used to have to deposit with the commercial banks (often via local authorities or state owned enterprises) As well as this, government has become relatively slow when it comes to paying contractors, particularly for civil works, which meant fewer deposits from such individuals and entities into commercial banks. Private sector credit extension growth for 2015, however, remained fairly strong at 13.6%, driven by mortgage loans.

Going forward, both the demand and supply side of credit are expected to remain under pressure in 2016 and the first half of 2017, and PSCE growth is expected to slow considerably, particularly driven by the reluctance of commercial banks to lend to heavily indebted households in a low liquidity and rising interest rate environment.



Source: Bank of Namibia, IJG Securities

Interest Rates

Interest rates in South Africa and Namibia have been at or near historically low levels since the global financial crisis. Rates bottomed out in 2012 with the Namibia repo rate dropping to 5.5% during the year. Since then, the Bank of Namibia has administered six rate hikes of 25 basis points each, taking the current repo rate to 7.0%.

Our expectation is for the repo rate to remain at 7.0% to the end of the current financial year, thus averaging 6.7% for FY16. Thereafter, we expect to see a continued, but slow, rise in rates through the FY17 financial year, with the rate ending the year at 7.75%, and averaging 7.48% through the year. We expect to see rates start to top out through FY18.

The above scenarios assume that South Africa will be downgraded to a “junk” rating during 2016. Standard and Poor’s is likely to be the first ratings agency to issue a sub-investment grade rating. Standard and Poor’s and Fitch Ratings’ decisions to downgrade their respective outlooks and ratings in December effectively opened both agencies up to a ratings downgrade should the South African outlook change.

Outlook

The outlook for South Africa remains challenging, with commodity prices, social challenges and energy shortages hampering the development of the economy. Moreover, the current fiscal position of Government, given the general macroeconomic situation, remains somewhat precarious as policy makers seek to balance the mandates of prudent fiscal management with providing much needed services and investment into the economy, notably social and economic infrastructure.

For Namibia, however, the outlook remains somewhat more positive, despite some general challenges. A slowing of Government activity, coupled with infrastructure challenges and lower commodity prices are likely to put pressure on the local economy from a growth and sustainability perspective. Nevertheless, the bulk of these challenges are highly manageable, and as such the outlook for Namibia remains broadly positive, should policy makers make the correct decisions for long-term sustainability. Nevertheless, we expect 2016 and the first half of 2017 to be challenging for Namibia, but expect to ride this storm out relatively unscathed should the correct policy action be taken by the Ministry of Finance and Bank of Namibia.

Interest income and the asset base

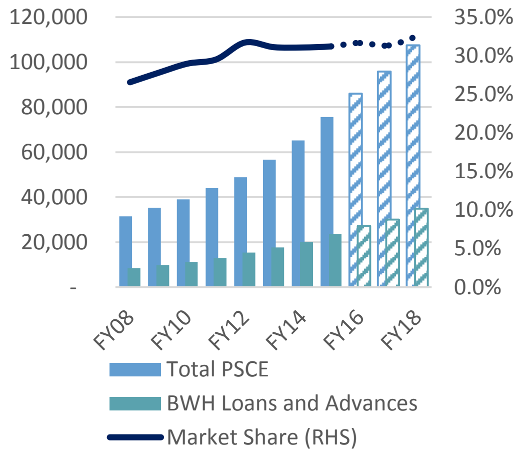
Asset growth

Between FY05 and FY12, BWH successfully grew its market share[1] within the Namibian banking sector, from 24.7% to 32.4%. Thereafter, the bank's market share has stabilised between 31% and 33%. As of the end of FY15, the bank had a market share of 32.2%, while at the end of the 1H16 this had declined marginally, to 31.3%. Going forward, we expect to see market share remain between 31.5 and 32.8%, however do not expect any market share growth beyond this point.

This is due to the fact that Bank Windhoek has grown its loan book aggressively over the past few years through the bottom of the interest rate cycle. Now that interest rates are increasing, the banking sector as a whole is likely to see a period of consolidation. Given liquidity challenges in the sector, we believe that the banks with "big brothers" outside of Namibia are likely to have a natural upper-hand over local banks, due to the availability of liquidity and funding via the parent company. This fact illustrates the unlevelled nature of the playing field in the country, between local and foreign owned banks. Secondly, we have seen a number of new entrants into the local banking space over the past two years. While still small in nature, these entities are likely to be competing for market share, both from a funding and advances perspective. We do not foresee any of the new entrants claiming major market share in the next three years, however they are likely to stem the growth in market share seen by the two largest commercial banks over recent years. Nevertheless, given the number of players in the market and the bank's current market share, the current and expected market shares remain highly attractive, and well above the bank's natural market share.

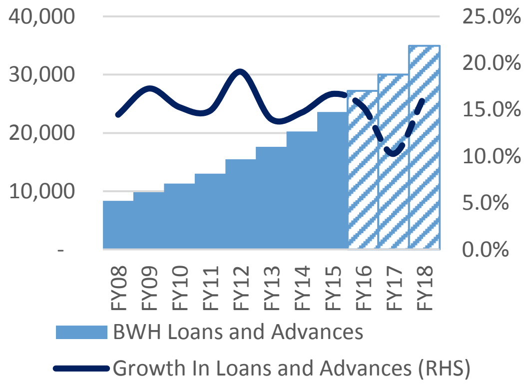
Bank Windhoek's loan book is expected to continue to grow over the next three years, however at a slowing rate, primarily due to the forecasted general slowdown in private sector credit extension growth, stemming from funding limitations and interest rate hikes. As interest rates rise, we expect to see a slight reduction in demand for credit, however the main constraint is expected from funding limitations as loan-to-funding ratios appear stretched, and new funding is both relatively hard to come by, and increasingly expensive.

Market Share (N$ Million)



Source: BWH, IJG Securities

Loans and Advances (N$ Million)



Source: BWH, IJG Securities

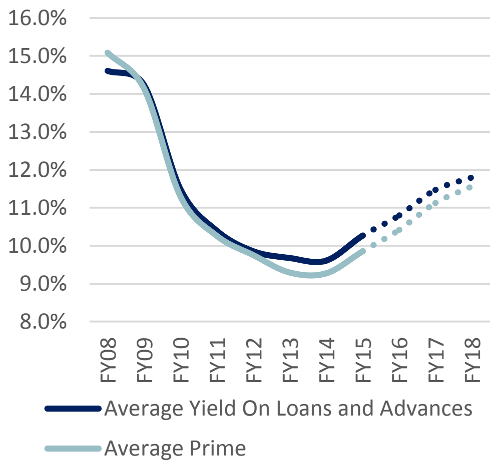
[1] Market share in this regard is measured as loans and advances to customers as a percent of total private sector credit extension.

Due to the tighter funding conditions within the banking sector, as well as an increasing reluctance of commercial banks to lend to highly indebted households in an ever less accommodative interest rate environment, we expect to see a notable slowdown in credit extension to households through 2016 and the first half of 2017. At the same time, however, we expect to see a sustained willingness to lend to corporates, which are likely to gain preference over households during this period.

From the bottom of the cycle, rates are up 150 basis points, however the manner in which these rates have increased has been generally positive for the banking sector. The slow and steady increases, with Namibian rates leading South African rates, has seen a widening in the net interest margin of banks, without any notable increase in non-performing loans. However, since the start of 2016, interest rate hikes in South Africa have lead Namibia, meaning that certain portions of the funding book reprice before the loan book.

Going forward, we expect to see a slowdown in credit extension growth and expect the largest impact of current and expected rate increases and liquidity challenges to take effect and markedly slow growth in FY16 and FY17, before recovering somewhat in FY18. For these three years, we expect to see PSCE growth normalising, bearing in mind the abnormally high levels of PSCE growth seen over recent years, and the high base created by this growth. We forecast year on year growth of 13.6%, 11.4% and 12.1% for FY16, 17 and 18, respectively.

Yield on Loans and Advances

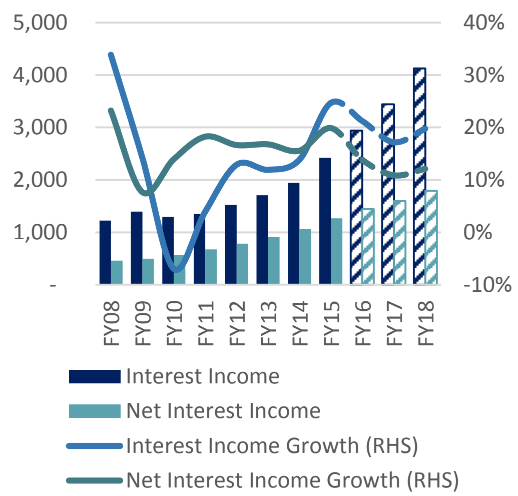


Source: BWH, IJG Securities

Yield on earning assets and interest income

The average yield on earning assets for Bank Windhoek has surged over recent years, and registered at 11.2% in 1H16 (normalised). This strong increase, from 9.6% in FY14, was primarily due to increases in the base lending rate, but also due to the bank reviewing its approach to classification of sub-prime and sub-mortgage rate clients. Going forward, we expect Bank Windhoek's average yield on loans to maintain a small spread over prime, due both to the weighting of mortgage loans on their book, which attract a higher interest rate than shorter duration loans, and the new focus on reclassification of sub-prime clients. For FY16 we expect a yield of 10.8%, while for FY17 and FY18 we expect 11.5% and 11.8%, respectively. This pickup will be driven by increasing administered interest rates.

Interest Income (N$ Million)



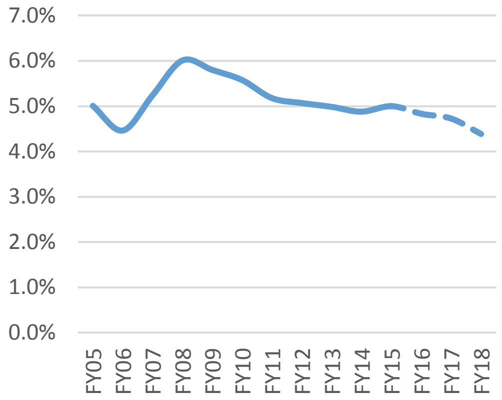
Source: BWH, IJG Securities

Following extremely strong interest income growth in FY15, largely on account of interest rate increases on a book that has grown much over recent years, we expect to see some consolidation in interest income in growth going forward. Following expansion of 24.7% in FY15, we expect to see some normalisation in growth, to 21.2%, 17.2% in FY16 and FY17, and then a recovery to 19.8% in FY18. This is largely due to the fact that we expect to see a slowdown in PSCE issuance as interest rates increase and liquidity declines, so while loan growth may slow, large interest rate increases will keep interest income growth relatively strong.

From a net-interest income perspective, the marginal cost of funding increased through FY15 and 1H16, with net interest income growth falling below interest income growth for the first time in five years. This was largely due to the funding position of the bank, and the low liquidity environment. This comes as little surprise after many years of expansive monetary policy, which is by nature designed to disincentivise saving and incentivise spending. As such, demand for borrowing has far exceeded growth in deposits at commercial banks, meaning that banks have not only increased competition for deposits (by raising deposit rates) but have also turned to other sources of funding such as debt instruments, which come at a relatively high cost when compared to customer deposits. Going forward, we expect to see liquidity remain tight for the next year to 18 months, which is likely to keep the cost of borrowing relatively high, and interest margins under pressure.

As such, we expect to see growth in net interest income slowing from the FY15 level of 19.9%, to 13.8% in FY16. This slowdown is both on account of increasing interest costs on the deposit book, but also the fact that Namibia has started to lag South Africa on interest rate increases. In addition to this, the Namibian central bank is putting increased pressure on the commercial banks to increase deposit rates in order to incentivise saving and compress the net interest margin. Finally, Bank Windhoek has been looking to extend its funding duration, particularly on the debt security side of its funding book, which naturally, comes at a price. Thus, while interest income will normalise over the next few years, the interest expense will also see similar or greater increases, resulting in a decline in net interest income relative to gross interest income. It is worth noting, that a high base has been created through the bottom of the interest rate cycle with regards to credit issuance and for the first few years of this cycle, the net interest margin. As such, we forecast net interest income of N$1.44 billion in FY16, N$1.64 billion in FY17 and N$1.79 billion in FY18, up from N$1.27 billion in FY15.

Net Interest Margin



Source: BWH, IJG Securities

Net interest margin

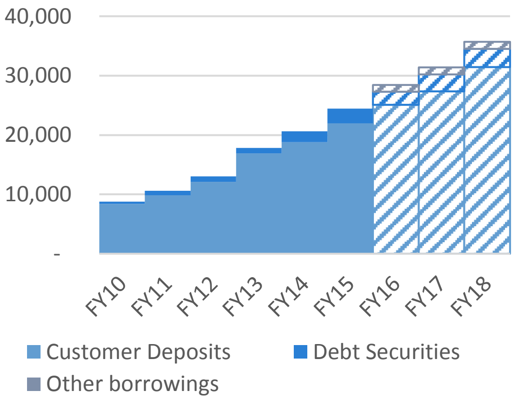
As of the end of FY15, Bank Windhoek had a net interest margin on lending of 5.0%, slightly above the FY14 level of 4.9%. Going forward, we expect to see this margin compressed through FY16, 17 and 18 declining to 4.8%, then 4.7%, then 4.4%. This is to be driven by the aforementioned factors, namely interest rate increases in South Africa leading Namibia, increased funding duration, competition for deposits and central bank pressure.

Funding the BWH asset base

Funding mix

In the 12 months from 1H15 to 1H16, Bank Windhoek's deposits due to customers increased by 13.5%, while debt securities in issue increased by 12.5%. In addition to this, another N$1.18 billion was borrowed by the bank, primarily from the International Finance Corporation (IFC). As such, total funding now stands at N$26.6 billion, with deposits making up N$23.1 billion of the total. At N$2.3 billion, debt securities still make up just 8.7% of total funding, while the new borrowings represent a further 4.4%. Going forwards, we expect to see a continuation of the trend of increases in debt securities (including "other borrowings", such as the IFC loan) at a faster rate than deposits. By FY17 and FY18, we expect to see debt securities and other borrowings making up approximately 12% of total funding. In FY15, growth in deposits was largely driven by current accounts, particularly when assessed on a weighted basis. This is a highly positive move given that the average cost of current accounts is around 50% of that of many of the other funding instruments, with the exception of saving deposits. As such, this has a positive impact on the net interest margin of the bank.

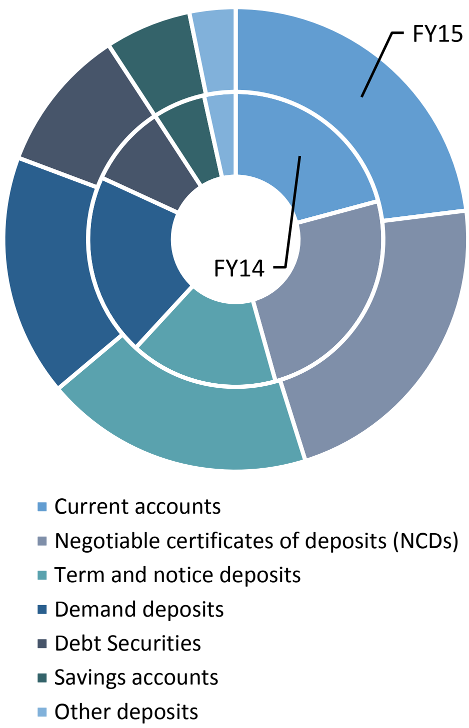
Funding Mix (N$ Million)



Source: BWH, IJG Securities

FY15	Average Interest Cost
Demand Deposits	5.5%
Term and notice deposits	5.5%
NCDs	6.7%
Cheque deposits (current)	2.9%
Debt securities	7.1%
Saving deposits	1.7%

Funding Breakdown



Source: BWH, IJG Securities

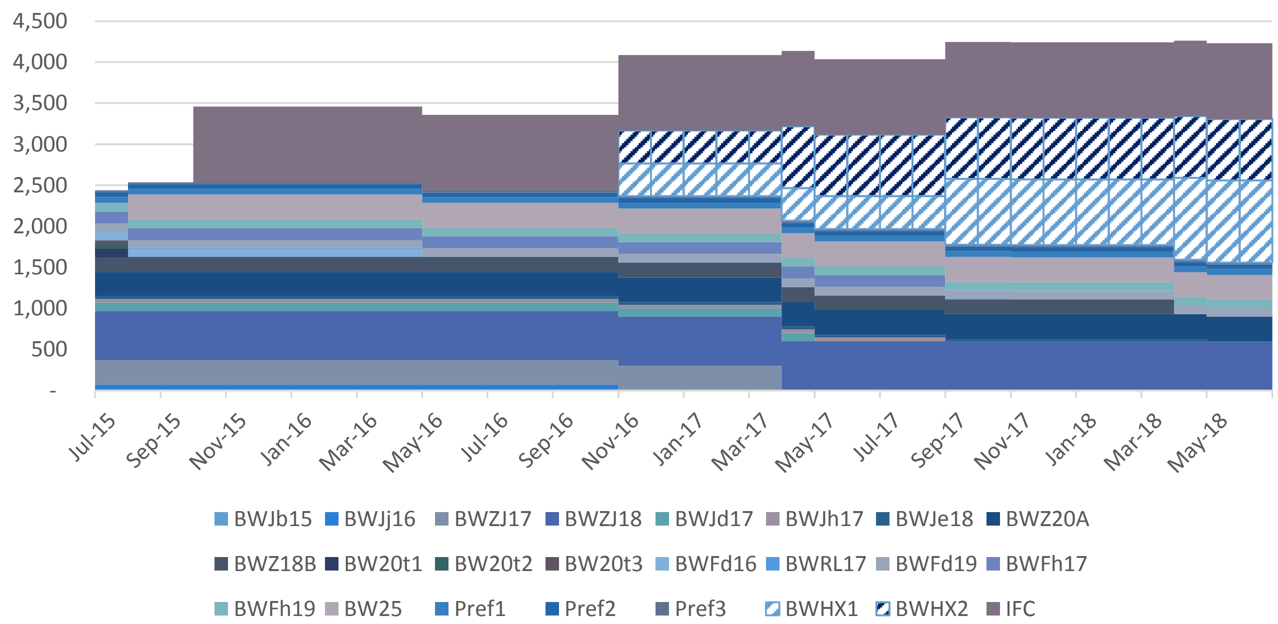
Historically, Bank Windhoek has had a higher cost of funding than many of its competitors, largely due to the lack of big-brother backing, and the higher percentage of funding sourced through negotiable certificates of deposit (NCD) and debt securities than the other major players. Going forward, we expect this to remain the case, as we expect the bank to remain partially reliant on debt securities to fund its loan growth into the future. In addition, with the upcoming (2018/19) introduction of Basel III in Namibia, we expect to see the bank looking to secure longer term funding, primarily from the debt markets. This is likely to be relatively expensive, due to the long-duration requirement. It should be noted, however that all of the commercial banks are likely to have to do the same, meaning that the playing field should be fairly level on this issue, and that one can expect some issuer competition with regards to long-duration debt issuance.

In FY15, the average cost of funding for Bank Windhoek was just under 5.0%. This is expected to increase to 6.0, 6.7 and 7.4%, respectively, for FY16, FY17 and FY18, largely on account of increasing interest rates, and partially due to the gradual change in funding mix for the bank.

Debt securities in issue

Shortly after the end of the FY15, the bank redeemed the BW20 notes, and issued a BW25 note. Otherwise, the BWJb15 floating rate note matured in FY15, and the BWZ18B, BWZ20A and BWJe18 were all issued through the second half of the FY15. In mid-April 2016, the BWFd16 matured.

Debt Securities in Issue (N$ Million)



Source: BWH, IJG Securities

In late October 2015, the Bank received a loan facility from the IFC, to the value of N$920 million. In addition to this, a further N$250 million was raised from the KfW DEG. These are, to our understanding, longer term funding, with duration of 7 years in the case of the IFC funds. The IFC funding is JIBAR linked, with an estimated spread, by our calculation, of between 260 and 300 points. Given the magnitude of the funds raised, the healthy cash balances and interbank position of Bank Windhoek, we do not expect to see a huge amount of further debt securities raised in FY16, as IFC funds are drawn down upon.

At the time of writing, the company's listed debt breaks down to 38.7% fixed rate, and 61.3% floating. All of the floating rate debt is JIBAR linked, meaning that it re-prices in the build up to interest rate moves, and more regularly than the company's loans to customers. Moreover, as interest rates increase, the cost of floating rate debt will increase, however we expect this to be partially offset by the bank being able to issue with a more attractive spread over JIBAR as it becomes more established and trusted within the listed debt space, both in Namibia and in South Africa. Going forward, longer duration debt issuance can be expected, which is likely to come at a premium over shorter duration paper.

Debt Securities in Issue

Series	Type	Issue date	Call date/ Expect maturity	Final Maturity	Coupon	Issue spread	Issue rate	Benchmark	Amount Issued
BW20	Subord/unsec	16-Aug-10	16-Aug-15	16-Aug-20	9.38%	174	9.380%	R157	100,000,000
BW20	Subord/unsec	29-Oct-10	16-Aug-15	16-Aug-15	9.38%	169	8.875%	R157	50,000,000
BW20	Subord/unsec	17-Jun-11	16-Aug-15	16-Aug-15	9.38%	167	9.150%	R157	50,000,000
BWRL17	Replica/unsec un	11-Feb-13	15-Oct-17	15-Oct-17	8%	68	7.210%	GC17	5,500,000
BWFd16	Senior/unsec	15-Apr-13	15-Apr-16	15-Apr-16	6.69%	140	6.690%	R157	100,000,000
BWFd19	Senior/unsec	25-Apr-14	25-Apr-19	25-Apr-19	9.425%	164	9.425%	R204	100,000,000
BWFh17	Senior/unsec	22-Aug-14	22-Aug-17	22-Aug-17	8.09%	107	8.090%	R203	145,000,000
BWFh19	Senior/unsec	22-Aug-14	22-Aug-19	22-Aug-19	8.86%	125	8.860%	R207	110,000,000
BWZ20A	Senior/unsec	27-Mar-15	27-Mar-20	27-Mar-20	9.75%	200	9.750%	R208	299,000,000
BW25	Subord/unsec	17-Aug-15	17-Aug-20	18-Aug-25	9.75%	200	9.750%	R208	181,000,000
Total Fixed Rate									**840,500,000**
BWZJ17	Senior/unsec	18-Mar-14	17-Mar-17	17-Mar-17	3m J +155	155	7.275%	3m Jibar	300,000,000
BWJj16	Senior/unsec	15-Apr-13	14-Oct-16	14-Oct-16	3m J +110	110	6.225%	3m Jibar	70,000,000
BWZJ18	Senior/unsec	14-Nov-13	19-Nov-18	19-Nov-18	3m J +180	180	6.992%	3m Jibar	600,000,000
BWJd17	Senior/unsec	25-Apr-14	25-Apr-17	25-Apr-17	3m J +94	94	6.715%	3m Jibar	100,000,000
BWJh17	Senior/unsec	22-Aug-14	22-Aug-17	22-Aug-17	3m J + 95	95		3m Jibar	45,000,000
BWZ18B	Senior/unsec	27-Mar-15	27-Mar-18	27-Mar-18	3m J +185	185	7.958%	3m Jibar	180,000,000
BWJe18	Senior/unsec	29-May-15	29-May-18	29-May-18	3m J +135	135	7.475%	3m Jibar	32,900,000
Total Floating Rate									**1,327,900,000**

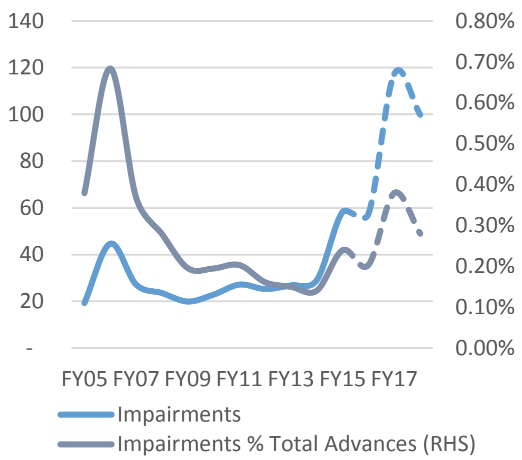
Source: BWH Treasury, BWH Annual Reports, IJG Research

Note: Grey – Matured/Called in FY16

Impairment Losses

As interest rates declined, impairments on the Bank Windhoek book fell to historically low levels when compared to loans and advances. As such, total impairments stood at 0.14% of loans and advances to customers, or N$29.1 million as of the FY14 year-end. However, with interest rates starting to pick up again, impairments have once again started to tick up, returning to 2009/2010 levels when compared to the loan book. As of the end of FY15, impairments stood at 0.24% of the total loan book, totally N$58.3 million. The first half of 2016 saw a continuation of this uptick, with impairments of N$31.5 million in the first half of the financial year.

Impairment Losses (N$ Million)

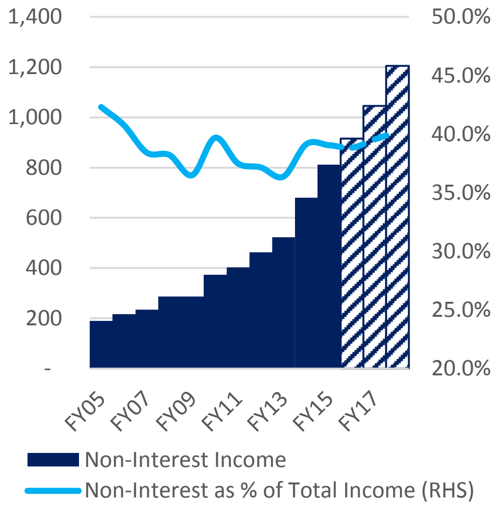


Source: BWH, IJG Securities

Going forward, we expect impairments to remain above the FY12, 13 and 14 levels, however do not foresee a major blowout in impairments over the three year forecast period. We do, however, remain cautious when it comes to the activities of Government, and should a major spending slowdown occur at the same time and interest rates pick up, the outlook for impairments could change with little warning. Nevertheless, we expect a slight recovery in impairments in FY16, as some of the impairment of FY15 is likely to remain recoverable, and new impairments are not expected to be sizable. Thereafter, we expect an impairment to pick up to 38bp of the book in FY17, before falling to 28bp in FY18. This low level of impairment loss speaks, to the prudential approach taken by Bank Windhoek when it comes to the extension of loans and advances to customers.

Nevertheless, in an increasing interest rate and slowing growth environment, it is unlikely that the bank will manage to maintain these losses at the extremely low level seen over the past five years. That said, however, at under 40bp of the total book, expected impairment losses remain negligible.

Non-Interest Income (N$ Million)



Source: BWH, IJG Securities

Non-interest income

Non-interest income has been a significant contributor to BWH overall revenue over recent years, and is likely to remain so as net-interest income growth slows due to margin compression. As of the end FY15, Bank Windhoek's non-interest income stood at N$812 million, representing 39.1% of total income. In 1H16, this income continued to grow, to N$481 million for the first six months of the financial year. Of this income, approximately 69.5% comprises fee and commission income, while the remainder is made up of foreign exchange gains and losses, brokerage fees, and asset management and administration fees, primarily.

Going forward, we are expecting to see continued growth in non-interest income, as the bank tries to diversify its revenue sources further. In this regard, the company has been investing heavily in IT systems, allowing for improved digital service provision. Nevertheless, we are cognisant of the fact that the regulator is in the process of attempting to reduce fee and commission income earned by commercial banks, particularly through regulating cash deposit fees. That said, we continue to believe that commercial banks will be able to innovate and generate new products and charges to make up for lost revenue. However, in FY15, Bank Windhoek saw huge growth in trading income (103% growth), both on account of Kwanza trading in the last two weeks of the financial year, and favourable markets for currency trading more generally. Given the magnitude of the step up, we do not see it as likely that this trading income will remain at such elevated levels going forward. As such, we are looking at a decline in trading income of 22% in FY16, before stabilising at this level in FY16 and FY17. This will have a temporary dampener effect on non-interest income growth in FY16.

Nevertheless, as net interest income growth slows, and in order to compensate for such, we expect to see the bank explore and develop avenues to increase non-interest revenue. Given the comparative ratio of interest to non-interest income in competitors, we believe there to be ample scope for this for Bank Windhoek.

Operating expenses

While strong growth was seen in income in the first half of FY16, operating expenses too grew, but at a much slower rate. Year on year, operating income grew 13.8%, to N$578.7 million for 1H16. This resulted in an improvement in the cost-to-income ratio of the bank, which improved from 51.7% to 49.1%. The increase in costs was largely driven by increased staff costs. Staff costs make up the largest cost item for the bank, representing more than 50% of total costs.

Going forward, we expect to see a concerted effort in cost containment as revenue and profits come under pressure due to the weakening economic climate and increasing interest rates. This strategy, when coupled with efforts to improve non-interest revenue, is likely to assist the bank in maintaining sound growth for the coming 18 months.

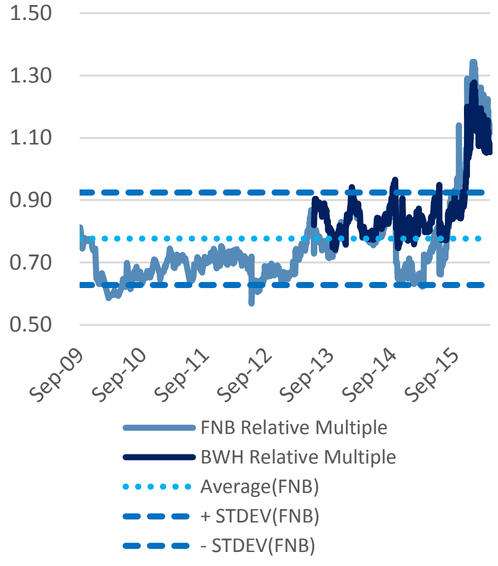
Financial Statement Summary

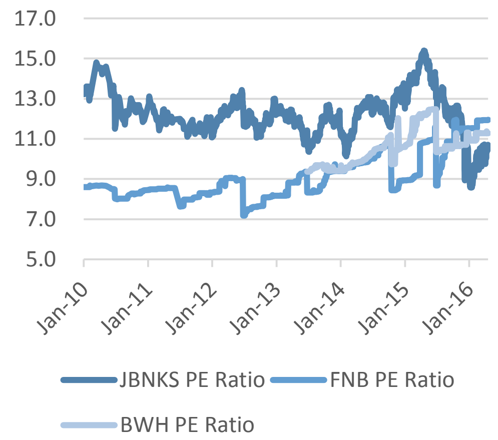
Income Statement

	Actual		Forecast		
in N$ 000s	**2014**	**2015**	**2016**	**2017**	**2018**
Interest and similar income	1,944,847	2,425,239	2,939,860	3,444,414	4,124,850
Interest and similar expense	(887,949)	(1,158,278)	(1,497,620)	(1,845,372)	(2,332,422)
Net interest income	**1,056,898**	**1,266,961**	**1,442,240**	**1,599,041**	**1,792,429**
Impairment losses	(29,115)	(58,305)	(57,281)	(117,367)	(99,888)
Non-Interest Income	**679,732**	**811,891**	**916,179**	**1,046,096**	**1,205,507**
Operating expenses	(914,641)	(1,042,231)	(1,156,277)	(1,266,124)	(1,384,170)
Operating profit	**821,989**	**978,316**	**1,144,861**	**1,261,646**	**1,513,878**
Share of profit from joint ventures	1,151	1,667	1,967	2,262	2,601
Share of profit from associates	84,264	87,159	95,166	109,441	125,857
Profit before tax	**907,404**	**1,067,142**	**1,241,994**	**1,373,349**	**1,642,336**
Income tax expense	(253,374)	(314,140)	(347,758)	(384,538)	(459,854)
Profit for the year	**654,030**	**753,002**	**894,236**	**988,811**	**1,182,482**
Other Comprehensive Income	14,244	28,486	28,486	28,486	28,486
Total comprehensive income	**668,274**	**781,488**	**922,722**	**1,017,297**	**1,210,968**
Headline Earnings	635,336	753,218	894,236	988,811	1,182,482
EPS (c)	**130.5**	**150.4**	**178.7**	**197.6**	**236.2**
HEPS (c)	**126.8**	**150.5**	**178.7**	**197.6**	**236.2**
Dividends declared per share (c)	**44.0**	**54.0**	**64.0**	**71.0**	**85.0**

Balance Sheet

in N$ 000s	*Actual*			*Forecast*	
	2014	**2015**	**2016**	**2017**	**2018**
ASSETS					
Cash and balances with central bank	709,431	619,907	1,109,091	1,720,745	1,786,268
Financial assets designated at fair value	2,104,938	2,587,461	2,730,930	2,730,930	2,730,930
Investment securities	72,047	100,533	120,000	198,900	307,798
Derivative financial instruments	2,190	977	8,281	9,287	10,416
Due from other banks	472,972	740,321	987,793	928,831	713,488
Loans and advances to customers	20,245,395	23,621,871	27,234,866	30,032,190	34,960,893
Investment in associates	209,364	233,157	280,740	335,460	398,389
Other assets	501,931	704,615	806,788	921,843	1,053,058
Total assets	**24,318,268**	**28,608,842**	**33,278,490**	**36,878,186**	**41,961,239**
LIABILITIES					
Derivative financial instruments	138	1,731	2,451	2,562	2,935
Due to other banks	282,664	130,151	143,977	159,272	176,191
Other borrowings			1,180,719	1,180,719	1,180,719
Debt securities in issue	1,841,287	2,461,212	2,176,558	2,856,558	3,048,158
Deposits	18,782,411	21,993,998	25,110,909	27,370,891	31,476,525
Other liabilities	317,610	378,377	398,460	391,699	385,204
Total liabilities	**21,224,110**	**24,965,469**	**29,013,074**	**31,961,700**	**36,269,732**
EQUITY					
Share capital and premium	532,435	530,050	532,435	532,435	532,436
Non-distributable reserve	170,354	196,486	232,949	258,147	293,729
Distributable reserve	2,391,369	2,916,837	3,500,031	4,125,903	4,865,342
Total shareholders' equity	**3,123,273**	**3,672,488**	**4,265,415**	**4,916,486**	**5,691,507**





Valuation and recommendation

Both of the domestically listed banks have seen large moves in share prices over the past year, and despite strong earnings growth, have repriced on a multiple basis. As such, the multiples on both FNB Namibia and Bank Windhoek Holdings have increase well beyond one standard deviation of the norm, when compared to the South African JBanks Index. Nevertheless, it can be argued that the Namibian banks were undervalued historically from a multiple perspective, usually trading on PEs of approximately 75% of those of the JBanks Index. Given the relatively strong earnings growth of the two domestically listed banks, this relatively low PE multiple makes little sense. However, as of mid-April 2016, however, both FNB Namibia and Bank Windhoek Holdings were trading at significant premiums, from a multiple perspective, to their South African counterparts. This was largely on account of the fact that a sizable de-rating in multiple has been seen in South Africa, notably on account of the finance minister debacle of late 2015. While the local banks multiples have crept upwards, the JBanks multiple has fallen from over 15x in mid-2015, to a low of 8.5x in early 2016. We believe that this decline in multiple reflects the poor sentiment in and on South Africa, resulting from the recent political gaffes there seen, as well as the weak exchange rate and increasing interest rates. However, we do not believe that the same sentiment is witnessed in Namibia. Moreover, regulated capital in Namibia is only likely to increase going forward, and as such we are comfortable with the current multiples seen on the local banks. At the time of writing, Bank Windhoek Holdings was trading on a historic PE of 11.3x, while FNB Namibia was trading on a historic PE of 11.9x and the South African JBank Index at 10.4x.

For the purpose of valuing the company, we establish a **cost of equity, of 12.9%,** up from 11.6% in 1H15, largely on account of a major increase in the risk-free rate. Based on this cost of equity, a highly conservative **long-term growth rate for the company of 9.5%,** and a **dividend pay-out ratio of 36%**, we believe a **PE of 10.5x can be justified** on this share. Given **expected earnings growth of 18.7% in FY16**, taking **total earnings to c179/share**, we derive **a target price of N$c1880/share**. Coupled with an **expected final dividend of 34cps**, we expect a **total return of 12.8% in 2H16**. Based on the stellar performance of the bank in 1H16 and the expected growth in 2H16, coupled with expected changes to local capital regulations for pension funds, we **maintain** a strong **BUY recommendation on Bank Windhoek Holdings**.

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