



NCBA GROUP: 1Q20 EARNINGS UPDATE

Dear All,

As NCBA results are reported on a prospective basis (continuation of CBA), for our y-o-y variance analysis and purely for the sake of discussion we have tried to achieve an apples to apples comparison by combining NIC's 1Q19 and CBA's 1Q19 numbers to get NCBA 1Q19**.

NCBA Group announced its 1Q20 results reporting a 26.8% y-o-y decline in profit after tax (PAT) to KES 1.6 BN. Earnings per share (EPS) for the period closed at KES 1.09.

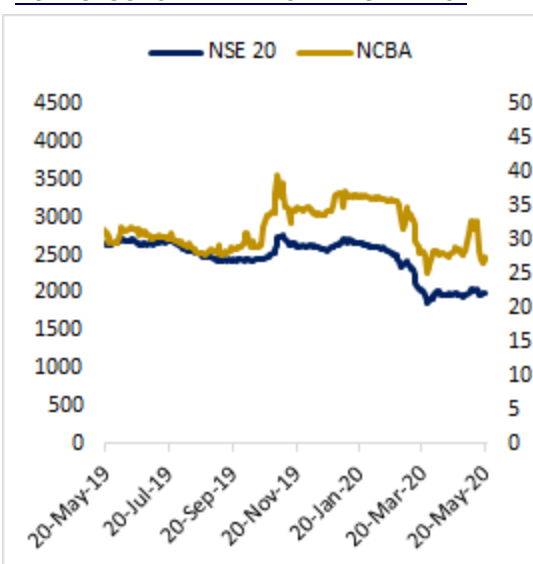
Key highlights:

Net interest income rose 5.5% y-o-y to KES 5.5 BN (-1.7% q-o-q) attributable to a 6.8% y-o-y increase in interest income to KES 10.2 BN (-2.9% q-o-q). Interest expense rose 8.3% y-o-y to KES 4.7 BN (-4.3% q-o-q) owing to continued pressure on customer deposits. Annualized yield on interest earning assets dropped 9 bps y-o-y to 9.5% whereas the annualized cost of funds dropped 2 bps y-o-y to 4.4%. As a result, the bank's annualized net interest margin (NIM) edged down 7 bps y-o-y to 5.0%.

Interest income from loans and advances rose 3.9% y-o-y to KES 6.2 BN (-7.2% q-o-q). This placed the annualized yield on loans for the period at 10.2%, 2 bps down y-o-y. Margin compression remains a key theme for FY20 in the sector given the depressed environment. However, management relayed that the local currency denominated loan book (c. 65.0%) is now referenced under the NCBA base rate, which somewhat hands over control of the future cost of credit to the bank.

Interest income from government securities rose 11.8% y-o-y to KES 3.8 BN (+3.1% q-o-q) placing the annualized yield on government securities at 10.7%, 15 bps up y-o-y. Interest expense from customer deposits rose 14.4% y-o-y to KES 4.2 BN (+3.9% q-o-q) placing the annualized cost of deposits at 4.5%, 15 bps up y-o-y. Given management's low risk appetite for lending, we expect the bank to be an even more pronounced player in the fixed income and interbank market.

NCBA GROUP 52 WEEK PRICE PERFORMANCE



(Source: NSE, DBIB Research)

PRICE RETURN	ABSOLUTE RETURN	EXCESS RETURN
3 months (%)	(31.1)	2.0
6 months (%)	(15.9)	23.2
12 months (%)	(11.6)	12.5

KEY METRICS

Current Price (KES)	27.55
52 week Low (KES)	25.10
52 week High (KES)	39.45
YTD Return (%)	(25.2)
Issued Shares (MN)	1,497.7
Market Cap (USD MN)	386.4

Recommendation	HOLD
Target Price (KES)	Under review
Trailing EPS (KES)	5.46
NAV (KES)	45.95
P/E (x)	5.0
P/B (x)	0.6
Div Yld (%)	0.9

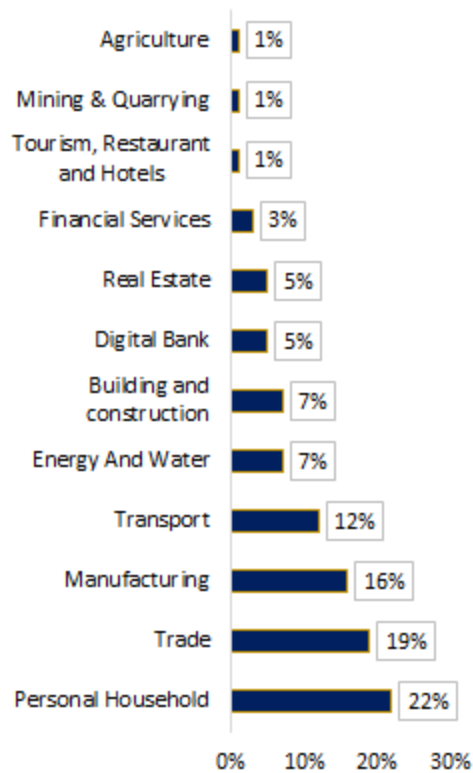
Research Analyst

Mary Mukuria

mmukuria@dyerandblair.com

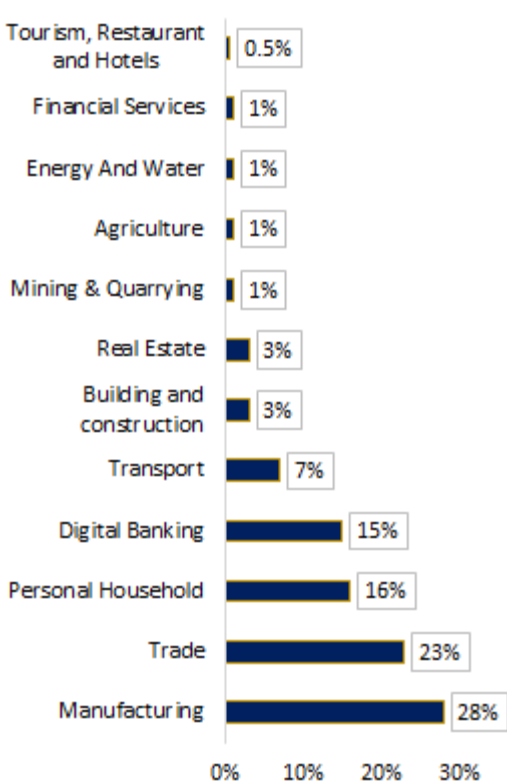
+254 709 930 128

LOAN BOOK: SECTORAL EXPOSURE (%)



Source: (Company Filings, DBIB Research)

NPLs: SECTORAL EXPOSURE (%)



Source: (Company Filings, DBIB Research)

Non-funded income (NFI) rose 31.2% y-o-y to KES 5.4 BN (-46.7% q-o-q). This is ascribable to a 37.0% y-o-y increase in fees and commission income to KES 4.0 BN (-4.5% q-o-q) and a 17.0% y-o-y increase in forex income to KES 1.0 BN (+2.4% q-o-q). Fees and commissions on loans rose 65.5% y-o-y to KES 3.2 BN (-26.7% q-o-q) whilst other fees and commissions declined 17.6% y-o-y to KES 818.8 MN. As a result, funded income reliance declined 542 bps y-o-y to 50.3%.

Operating expenses (less loan provisions) declined 5.5% y-o-y to KES 4.5 BN courtesy of an 18.4% y-o-y decline in staff costs to KES 1.7 BN (-24.8% q-o-q). The bank's cost to income ratio declined 981 bps y-o-y to 41.5% owing to various merger-related synergies. Pre-provision operating profit rose 40.4% y-o-y to KES 6.4 BN (-38.9% q-o-q).

The loan loss provision expense saw an upswing of 200.1% y-o-y to KES 3.8 BN placing the annualized cost of risk at 6.1%, 405 bps up y-o-y. This was as a result of factoring in key legacy NPL names as well as foreseen delinquencies owing to a COVID-inflicted economy, the looming locust swarms that pose a threat to the food basket and the unprecedented flash floods. Whilst the bank does not have a significant direct exposure to key affected sectors i.e. Tourism, we believe secondary exposure will still weigh down key accounts in both strongholds of the bank; asset financing and corporate banking.

Total assets rose 9.2% y-o-y to KES 509.6 BN (+3.0 q-o-q). Customer loans and advances saw a 2.2% y-o-y increase to KES 245.9 BN (-1.4% q-o-q). Investment securities rose 18.9% y-o-y to KES 154.7 BN (+5.9% q-o-q). We foresee subdued growth of the loan book in the upcoming quarters. Inversely, we foresee a surge in activity in the bank's investments in investment securities. **On the other hand, customer deposits** advanced 9.9% y-o-y to KES 390.5 BN (+3.2% q-o-q). Deposits due to other banks declined 3.8% y-o-y to KES 8.9 BN (-18.6% q-o-q). In parallel, loans to deposits and borrowed funds ratio declined 401 bps y-o-y to 59.6%.

Gross non-performing loans (NPLs) rose 31.8% y-o-y to KES 38.8 BN whereas interest in expense rose 44.0% y-o-y to KES 7.4 BN. As such, total NPLs rose 29.2% y-o-y to KES 31.4 BN. On a year-on-year basis, the NPL ratio worsened to 13.6%, 273 bps up y-o-y. Loan loss provisions rose 15.9% y-o-y to KES 13.8 BN. The NPL coverage ratio declined 486 bps y-o-y to 35.4%.

NCBA Kenya's core capital ratio (Core capital/TRWA) edged up 89 bps y-o-y to 18.9% whereas Total capital ratio (Total capital/TRWA) rose 35 bps y-o-y to 19.5%. Both ratios remain above the statutory minimum of 10.5% and 14.5% respectively. Liquidity ratio rose 136 bps y-o-y to 54.6%, above the statutory minimum of 20.0%. The BOD's decision to forgo the initially declared cash dividend and propose a bonus share of 1:10 was in a bid to further conserve capital and comfortably ride the unprecedented wave that is 2020.

On a trailing basis, the bank is trading at a P/E multiple of 5.0x and a P/B multiple of 0.6x, relative to the sector medians of 4.9x and 0.8x respectively. Its ROE stands at 11.9% relative to sector median of 16.7% whereas its ROA stands at 1.6% relative to sector median of 2.4%. Currently, NCBA Group has a dividend yield of 0.9%. On the basis of a highly discounted price that does not reflect the value of the now merged entity, we maintain our **HOLD** recommendation.

PROFIT AND LOSS SUMMARY (KES MN)

Year End: December	1Q20	1Q19**	1Q19	4Q19	y-y% ch**	y-y% ch	q-q%ch
Interest income	10,176	9,531	4,805	10,483	6.8	111.8	(2.9)
Interest expense	4,677	4,320	2,311	4,888	8.3	102.4	(4.3)
Net interest income	5,499	5,212	2,494	5,595	5.5	120.5	(1.7)
Other operating income	441	371	161	5,025	18.8	173.3	(91.2)
Fees and commission income	3,972	2,899	2,300	4,160	37.0	72.7	(4.5)
Net income from forex dealings	1,011	863	555	987	17.0	82.1	2.4
Total non-interest income	5,423	4,133	3,016	10,171	31.2	79.8	(46.7)
Total income	10,922	9,345	5,510	15,767	16.9	98.2	(30.7)
Less operating expenses	4,535	4,797	2,971	5,320	(5.5)	52.7	(14.7)
Operating profit	6,387	4,548	2,539	10,447	40.4	151.6	(38.9)
Bad debt charge	3,775	1,258	585	8,240	200.1	545.4	(54.2)
Exceptional items	196	-	-	2,319	N/A	N/A	(91.6)
Profit before tax	2,416	3,290	1,954	4,527	(26.5)	23.7	(46.6)
Less tax	785	1,062	657	5,652	(26.1)	19.4	(86.1)
Profit after tax	1,631	2,228	1,296	3,236	(26.8)	25.8	(49.6)
Attributable Income	1,557	2,447	1,516	2,891	(36.4)	2.7	(46.1)

(Source: Company, DBIB Research)

BALANCE SHEET SUMMARY (KES MN)

Year End: December	1Q20	FY19	1Q19**	1Q19	y-y% ch**	y-y% ch	q-q%ch
Total shareholder's equity	68,565	66,993	67,286	30,298	1.9	126.3	2.3
Minority interest	251	267	318	-	(21.1)	N/A	(6.1)
Total Equity	68,816	67,260	67,604	30,298	1.8	127.1	2.3
Balances due to Central Bank	-	-	-	-	N/A	N/A	N/A
Deposits due to other banks	8,868	10,893	9,215	3,042	(3.8)	191.5	(18.6)
Customer deposits	390,529	378,237	355,308	204,228	9.9	91.2	3.2
Borrowed funds	22,317	22,081	23,304	8,385	(4.2)	166.2	1.1
Other liabilities	19,064	16,372	11,317	7,165	68.5	166.1	16.4
Total equity and liabilities	509,595	494,843	466,748	253,118	9.2	101.3	3.0
Central bank balances	30,318	26,358	30,682	14,080	(1.2)	115.3	15.0
Deposits due from banks	29,625	36,421	28,501	22,953	3.9	29.1	(18.7)
Investment Securities	154,670	146,119	130,074	69,678	18.9	122.0	5.9
Held for dealing securities	-	-	-	-	N/A	N/A	N/A
Customer loans and advances	245,858	249,355	240,650	122,326	2.2	101.0	(1.4)
Other assets	37,471	25,737	28,012	18,446	33.8	103.1	45.6
Intangible assets	6,689	7,009	5,051	3,214	32.4	108.2	(4.6)
Fixed assets	4,963	3,844	3,778	2,421	31.4	105.0	29.1
Total assets	509,595	494,843	466,748	253,118	9.2	101.3	3.0

(Source: Company, DBIB Research)

INVESTMENT RETURN

	1Q20*	1Q19**	1Q19*	FY19	y-y bps ch**	y-y bps ch	q-q bps ch
ROA (%)	1.3	1.9	2.0	1.6	(63)	(77)	(30)
ROIC (%)	1.3	2.0	2.1	1.6	(63)	(78)	(31)
ROE (%)	9.5	13.2	17.1	11.7	(370)	(763)	(218)

(Source: Company, DBIB Research)

*Annualized

CAPITAL ADEQUACY, LIQUIDITY & ASSET QUALITY

	1Q20	1Q19**	1Q19	FY19	y-y bps ch**	y-y bps ch	q-q bps ch
Core capital/TRWA (%)	18.9	18.0	15.8	16.6	89	309	227
Min. Statutory Ratio (%)	10.5	10.5	10.5	10.5	-	-	-
Total capital/TRWA (%)	19.5	19.1	17.0	17.3	35	244	214
Min. Statutory Ratio (%)	14.5	14.5	14.5	14.5	-	-	-
Liquidity Ratio (%)	54.6	53.2	50.5	51.8	136	406	272
Min. Statutory Ratio (%)	20.0	20.0	20.0	20.0	-	-	-
Leverage Ratio (%)	32.4	34.5	27.7	13.5	(204)	476	1,889
Equity-to-Loans Ratio (%)	28.0	28.1	24.8	27.0	(10)	322	102
NPL Ratio (%)***	13.6	10.9	9.0	11.9	273	468	175
NPL Coverage Ratio (%)***	35.4	40.3	61.3	44.9	(486)	(2,592)	(954)
IFRS 9 NPL Coverage Ratio (%)	54.5	57.8	82.3	2.5	(324)	(2,778)	5,201
LT Debt to Total Liab. and Equity (%)	3.7	2.4	2.8	32.8	132	91	(2,909)
NTA/share (KES)	41.5	41.8	18.1	40.2	(28)	2,340	125
Book value/share (KES)	45.9	45.1	20.2	44.9	81	2,572	104

(Source: Company, DBIB Research)

***Total Loan Portfolio net of Interbank Lending

OPERATING PERFORMANCE

	1Q20	1Q19**	1Q19	FY19	y-y bps ch**	y-y bps ch	q-q bps ch
Yield on interest earning assets (%)*	9.5	9.5	8.9	5.9	(9)	52	356
Cost of funds (%)*	4.4	4.5	4.3	3.0	(2)	15	148
Net Interest Margin (%)*	5.0	5.1	4.7	2.9	(7)	37	208
Loan-to-Deposits ratio (%)	63.0	67.7	59.9	64.1	(477)	306	(113)
Loan-to-Dep. & Borrowed Funds (%)	59.6	63.6	57.5	60.6	(401)	202	(109)
Funded Income Gen. Potential (%)	84.4	85.5	84.9	87.3	(112)	(51)	(287)
Funded Income Reliance (%)	50.3	55.8	45.3	39.6	(542)	508	1,072
Cost to income ratio (%)	41.5	51.3	53.9	41.9	(981)	(1,240)	(39)
Cost of risk (%)	6.1	2.1	1.9	33.6	405	423	(2,747)
Pre-tax margin (%)	22.1	35.2	35.5	23.3	(1308)	(1,334)	(118)
PAT margin (%)	14.9	23.8	23.5	-	(890)	(859)	1,493

(Source: Company, DBIB Research)

* Annualized

NOTE:

1Q19** represents the position of both NIC and CBA as at 1Q19

y-y bps ch** represents the year on year change between 1Q20 and 1Q19**

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 10.0% and 15.0% upside over the next 12 months

Hold: Share price may fall within the range of +/- 10% 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

DISCLAIMER

While every care has been taken in preparing this report and it has been prepared from sources believed to be reliable, no representation, warranty, or undertaking (express or implied) is given and no responsibility is accepted by Dyer and Blair Investment Bank Limited, its related companies, subsidiaries, affiliates, its employees and agents, as to the accuracy and completeness of the information contained herein or in respect of any reliance on or use thereof. This report is solely intended for distribution to clients of Dyer and Blair Investment Bank Limited. Any information may be changed after distribution at any time without any notice.