

DYER & BLAIR INVESTMENT BANK

EARNINGS UPDATE

Founder Member of the Nairobi Securities Exchange

13TH NOVEMBER 2020



DYER & BLAIR
INVESTMENT BANK

WE KNOW. YOU KNOW.

KCB GROUP HOLDINGS: 3Q20 EARNINGS UPDATE

Dear All,

KCB GROUP released its 3Q20 results recording a 43.2% y-o-y drop in profit after tax (PAT) to KES 10.9 BN. Pre-provisions operating earnings rose 12.5% y-o-y to KES 37.2 BN but bad debt provisions surged 242.5% y-o-y to KES 20.0 BN to see the annualized cost of risk at 4.6%. Trailing EPS stands at KES 5.26. Annualized ROE declined 1,039 bps y-o-y to 10.7% whereas annualized ROA declined 185 bps y-o-y to 1.5%.

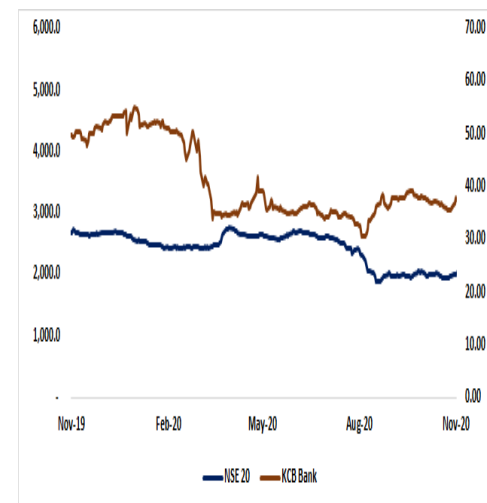
Below please find key highlights:

Net interest income rose 23.7% y-o-y to KES 47.9 BN on the back of a 23.0% y-o-y rise in interest income to KES 63.3 BN and a 20.8% y-o-y increase in interest expense to KES 15.4 BN on the back of consolidation of NBK. Annualized yield on interest earning assets declined 145 bps y-o-y to 10.4% whereas annualized cost of funds declined 52 bps y-o-y to 2.5%. Consequently, net interest margin declined 93 bps y-o-y to 7.9%.

Interest income from loans and advances rose 12.9% y-o-y to KES 45.8 BN placing the annualized yield on average loans at 11.5%, down 36 bps y-o-y. Interest income from government securities rose 65.7% y-o-y to KES 16.8 BN placing the annualized yield on average government securities at 12.3%. Interest expense from customer deposits rose 23.6% y-o-y to KES 14.0 BN placing the annualized cost of average customer deposits at 2.7%, up 17 bps y-o-y.

Non-funded income rose 1.5% y-o-y to KES 21.3 BN. This followed a 1.2% y-o-y rise in total fees and commissions to KES 14.3 BN and an 8.4% y-o-y rise in other operating income to KES 3.6 BN. Forex income declined 4.2% y-o-y to KES 3.3 BN. Fees and commissions on loans and advances declined 14.2% y-o-y to KES 6.8 BN whereas other fees and commissions rose 20.8% y-o-y to KES 7.5 BN. Funded income reliance ratio rose 230 bps y-o-y to 69.2%.

KCB GROUP: 52 WEEK PRICE PERFORMANCE



(Source: NSE, DBIB Research)

PRICE RETURN	ABSOLUTE RETURN	EXCESS RETURN
3 months (%)	24.1	21.0
6 months (%)	6.3	15.6
12 months (%)	(23.8)	9.8

KEY METRICS

Current Price (KES)	37.90
52 week Range (KES)	30.55-55.00
YTD Return (%)	(30.7)
Issued Shares (Mn)	3,213.5
Market Cap (USD Mn)	1,102.9

Recommendation	HOLD
Target Price	Under Review
Trailing EPS (KES)	5.26
NAV (KES)	42.30
Trailing P/E (x)	7.1
Trailing P/B (x)	0.9
Dividend Yield (%)	-

Research Analyst

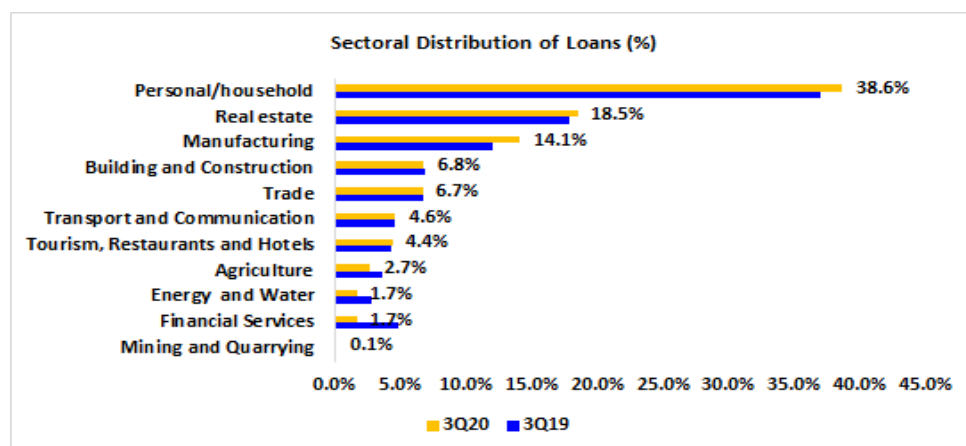
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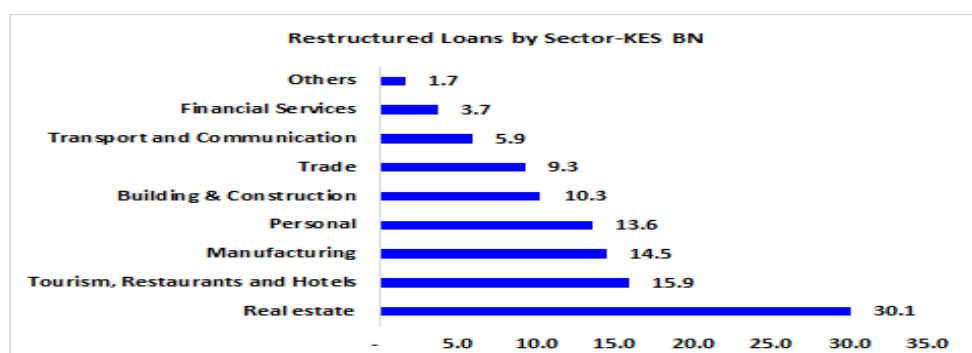
Operating expenses (less loan loss provisions) rose 20.1% y-o-y to KES 32.0 BN mainly on the back of a 12.8% y-o-y rise in staff costs to KES 15.2 BN and a 26.6% y-o-y rise in other operating expenses to KES 12.3 BN. Cost to income ratio declined 321 bps y-o-y to 46.3%.

Customer loans and advances grew 18.7% y-o-y to KES 577.5 BN (+3.1% q-o-q) whereas investment securities rose 83.9% y-o-y to KES 236.2 BN. On the funding side, customer deposits rose 31.7% y-o-y to KES 772.7 BN whereas borrowed funds declined 7.9% y-o-y to KES 20.4 BN. Loan to deposit ratio declined 788 bps y-o-y to 74.7% whereas loans to deposits and borrowed funds declined 667 bps y-o-y to 72.8%.



(Source: Company)

8,478 loan accounts with a total value of KES 105.0 BN were restructured as at 3Q20. The Sectoral distribution of restructured loans was as shown below,



(Source: Company)

Gross non-performing loans rose 127.8% y-o-y to KES 96.9 BN (+15.6% q-o-q). Interest in suspense rose 168.0% y-o-y to KES 12.9 BN (+10.9% q-o-q). As a result, total NPLs (Gross NPLs less interest in suspense) rose 122.6% y-o-y to KES 84.1 BN. NPL ratio rose 633 bps y-o-y to 14.4%. NPL coverage (Loan loss provision/ Total NPL) ratio rose 123 bps y-o-y to 52.2%. Central Bank of Kenya's coverage ratio rose from 58.9% in 3Q19 to 68.6% in 3Q20 whereas IFRS coverage ratio rose from 56.0% in 3Q19 to 63.5% in 3Q20.

KCB Kenya's core capital ratio (Core capital/TRWA) declined 50 bps y-o-y to 16.0% above the statutory minimum of 10.5% while Total capital/TRWA declined 50 bps y-o-y to 17.3% above the statutory minimum of 14.5%.

	KCB Kenya		Group	
	Reported	Adjusted ratios	Reported	Adjusted ratios
Core capital ratio (%)	16.0	16.3	17.8	18.0
Total capital ratio (%)	17.3	17.6	19.6	19.8

Source: Company

Adjusted ratios include the expected credit loss provisions added back to capital in line with the CBK guidance note issued in April 2018 on implementation of IFRS 9.

Channel Contribution: 98.0% of the group's transactions were performed outside the branch through mobile (77.0%), agency, internet and POS (17.0%) and ATMs (4.0%) continuing the group's transition to a variable cost driven model. Non branch revenue declined 13.0% y-o-y by KES 1.1 BN due to waiver of mobile banking fees. Mobile loans declined 26.0% driven by a 49.0% decline in KCB Mpesa disbursements to KES 49.7 BN. Fuliza disbursements rose from KES 47.8 BN in 3Q19 to KES 53.3 BN in 3Q20.

On a trailing basis: KCB is trading at a P/E ratio of 7.1x, above the industry median of 4.7x and a P/B of 0.9x above the industry median of 0.6x. ROE stands at 10.7% against a sector median of 12.0% whereas its ROA stands at 1.5% against a sector median of 1.7%. As the first bank to announce its 3Q20 earnings, we think that the multiples are skewed especially if other banks report similar performances. As the group has been re-added into the MSCI Frontier Index, we expect to see more portfolio inflows towards the stock in 2021. We issue a **HOLD** recommendation as we await management's direction on the 3Q20 earnings call (see side bar for the registration link).

[REGISTER FOR THE MANAGEMENT'S 3Q20 EARNINGS CALL](#)

PROFIT AND LOSS SUMMARY (KES MN)

Year End: December	3Q20	3Q19	y-y% ch	3q20	2q20	3q19	y-y% ch	q-q%ch
Interest income	63,287	51,448	23.0	29,684	21,175	19,228	54.4	40.2
Interest expense	15,424	12,768	20.8	7,222	5,160	4,694	53.9	40.0
Net interest income	47,863	38,680	23.7	22,461	16,016	14,534	54.5	40.2
Other operating income	3,649	3,365	8.4	1,440	1,119	1,485	(3.0)	28.6
Fees and commission income	14,303	14,137	1.2	5,401	3,995	7,362	(26.6)	35.2
Net income from forex dealings	3,327	3,472	(4.2)	1,267	952	649	95.3	33.0
Total non-interest income	21,280	20,975	1.5	8,108	6,067	9,495	(14.6)	33.6
Total income	69,143	59,654	15.9	30,569	22,082	24,029	27.2	38.4
Less operating expenses	31,987	26,638	20.1	14,378	10,050	8,936	60.9	43.1
Operating profit	37,155	33,016	12.5	16,191	12,032	15,093	7.3	34.6
Bad debt charge	(20,012)	(5,843)	242.5	(16,981)	(8,129)	(5,015)	238.6	108.9
Exceptional items	-	-	-	0	-	-	-	-
Profit before tax	17,143	27,173	(36.9)	(790)	3,903	10,078	(107.8)	(120.2)
Less tax	(6,252)	(8,010)	(22.0)	(1,042)	(2,587)	(3,026)	(65.6)	(59.7)
Profit after tax	10,891	19,163	(43.2)	(1,832)	1,316	7,052	(126.0)	(239.2)
Attributable Income	10,891	19,163	(43.2)	(1,832)	1,316	7,052	(126.0)	(239.2)
EPS (KES)	4.52	8.33	(45.7)	-3.78	(3)	0.43	(979.1)	23.1

(Source: Company, DBIB Research)

BALANCE SHEET SUMMARY (KES MN)

Year End: December	3Q20	1H20	3Q19	y-y % ch	q-q % ch
Total shareholder's equity	135,945	132,139	121,232	12.1	2.9
Minority interest	-	-	-	-	-
Total Equity	135,945	132,139	121,232	12.1	2.9
Deposits due to other banks	16,570	13,362	13,506	22.7	24.0
Customer deposits	772,663	758,241	586,715	31.7	1.9
Borrowed funds	20,389	21,377	22,131	(7.9)	(4.6)
Other liabilities	26,442	27,953	20,750	27.4	(5.4)
Total equity and liabilities	972,009	953,072	764,335	27.2	2.0
Central bank balances	48,624	60,786	54,335	(10.5)	(20.0)
Deposits due from banks	36,564	53,328	42,530	(14.0)	(31.4)
Investment securities	236,247	208,523	128,459	83.9	13.3
Held for dealing securities	-	-	-	-	-
Customer loans and advances	577,505	559,884	486,423	18.7	3.1
Other assets	46,476	42,999	35,719	30.1	8.1
Intangible assets	6,696	7,313	4,892	36.9	(8.4)
Fixed assets	19,897	20,239	11,977	66.1	(1.7)
Total assets	972,009	953,072	764,335	27.2	2.0

(Source: Company, DBIB Research)

INVESTMENT RETURN

	3Q20	1H20	3Q19	y-y bps ch	q-q bps ch
ROA (%)*	1.5	1.6	3.3	(185)	(10)
ROIC (%)*	1.6	1.7	3.5	(194)	(10)
ROE (%)*	10.7	11.5	21.1	(1039)	(79)

(Source: Company, DBIB Research)

*Annualized

CAPITAL ADEQUACY, LIQUIDITY & ASSET QUALITY (KCB KENYA)

	3Q20	1H20	3Q19	y-y bps ch	q-q bps ch
Core capital/TRWA (%)	16.0	16.1	16.5	(50)	(10)
Min. Statutory Ratio (%)	10.5	10.5	10.5	-	-
Total capital/TRWA (%)	17.3	17.4	17.8	(50)	(10)
Min. Statutory Ratio (%)	14.5	14.5	14.5	-	-
Liquidity Ratio (%)	33.3	34.7	32.7	60	(140)
Min. Statutory Ratio (%)	20.0	20.0	20.0	-	-
Leverage Ratio (%)	14.0	13.9	15.9	(188)	12
Equity-to-Loans Ratio (%)	23.5	23.6	24.9	(138)	(6)
NPL Ratio (%)**	14.4	13.0	8.0	633	135
NPL Coverage Ratio (%)**	52.2	50.0	51.0	123	221
Long Term Debt to Total Liabilities and Equity (%)	2.1	2.2	2.9	(80)	(15)
NTA/share (KES)	37.8	34.8	35.6	222	303
Book value/share (KES)	44.3	41.1	39.5	480	322

(Source: Company, DBIB Research)

**Total Loan Portfolio net of Interbank Lending

OPERATING PERFORMANCE

	3Q20	1H20	3Q19	y-y bps ch	q-q bps ch
Yield on interest earning assets (%)*	10.4	10.8	11.8	(145)	(40)
Cost of funds (%)*	2.5	2.6	3.0	(52)	(4)
Net Interest Margin (%)*	7.9	8.2	8.8	(93)	(36)
Loan-to-Deposits ratio (%)	74.7	73.8	82.6	(788)	90
Loan-to-Dep.& Borrowed Funds ratio (%)	72.8	71.8	79.5	(667)	101
Funded Income Generating Potential (%)	83.7	80.6	81.1	263	309
Funded Income Reliance (%)	69.2	69.0	66.9	230	23
Cost to income ratio (%)	46.3	47.0	49.5	(321)	(77)
Pre-tax margin (%)	24.8	28.5	47.2	(2241)	(368)
PAT margin (%)	15.8	16.8	33.3	(1751)	(107)

(Source: Company, DBIB Research)

* Annualized

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 5.0% and 15.0% upside over the next 12 months

Hold: Share price may fall within the range of <+5.0/ -10.0% 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

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