KENYAN BANKING SECTOR REPORT 2022

Update – February 2023

EXECUTIVE SUMMARY

In this report, we update our Kenyan banking sector 2022 report with coverage of DTB, I&M and Stanbic Banks.

The report retains the initial format as follows;

a) Introduction to the Kenyan banking sector,
b) Key themes that shaped the sector in 2022 and our 2023 outlook,
c) Performance of the listed banks as of Q3'2022, and,
d) Detailed coverage – Equity, KCB, Co-operative, Standard Chartered, Absa, DTB, I&M and Stanbic Banks.

Expectations for the Banking Sector in 2023

a) Risk-Based Lending

Implementation of risk-based lending will have significant dual-effects on bank's funded income. These are

i. Higher interest revenue due to the expected increase of lending rates, and,
ii. Increased quantum of loans disbursed given that high risk borrowers will now be accommodated at proportionate risk-based prices.

We expect an increased deployment of funding towards lending which will result in higher loan to deposit ratios and loan loss provisions. The deployment may be gradual in light of the current unfavorable macroeconomic variables.

b) Non-funded income growth

We expect Non-funded income to record muted growth in 2023 on account of the reintroduction of mobile to bank transaction charges being offset by reduced FX income.

c) Asset Quality

We expect a gradual improvement in the sector's asset quality on the back of economic recovery following the twin disruptions of COVID-19 and general elections held in August 2022.

Kenya's Economy is projected to grow by 5.1% in 2023, according to the IMF.

Downside risks include increased credit risk crystalizing in the medium term once the risk-based pricing takes full effect, and, should the unfavorable global macroeconomic situation persist.

d) Dividends

As a result of improved performance in 2022, we expect that Equity, KCB, Co-operative, Standard Chartered, Absa, DTB, I&M and Stanbic will issue full year dividends.

2022 performance was boosted by FX income underscoring the sector's resilience in a year when inflation spiraled to hit a 5-year high and deteriorating macroeconomic conditions around the globe.

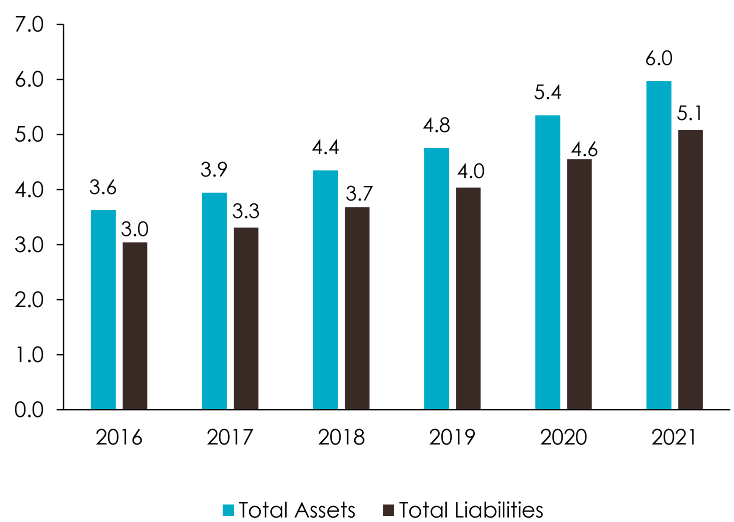
Introduction to Kenya's Banking Sector

"Banks are to the economy what the heart is to the human body. They cycle necessary capital through the whole, and they are barely noticed until pressure, necessity, or crises." - Hendrith Vanlon Smith Jr., Banker and Author.

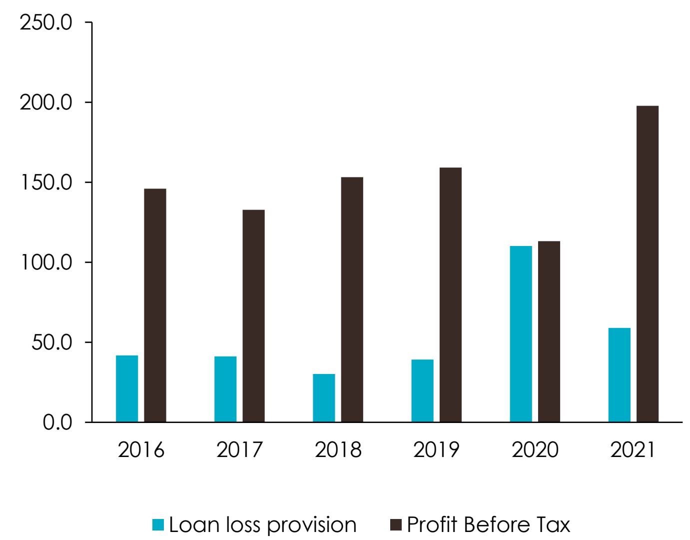
Banks act as the main financial intermediary in the economy by creating the link and facilitating the movement of un-invested capital deposited by savers to parties that need the funds through lending. Additionally, alternative savings platforms such as SACCOs and Pension Funds ultimately rely on a banking institutions to function. As such, the inextricable intertwining of banks and financial activities helps analysts assess the health of an economy by looking through a banking sector-tinted lens.

The Kenyan banking sector is highly competitive with 38 banking institutions, 14 microfinance banks and 97 non-bank financial institutions. Ten of these are listed and account for more than 75% of market share based on assets. Equity & KCB lead the pack with a market share of 41%. Owing to increasing financial inclusion levels and a growing economy, Kenyan banks have seen their asset base grow at a CAGR of 10.5% over the period 2016-2021 to KES 6.0Tn.

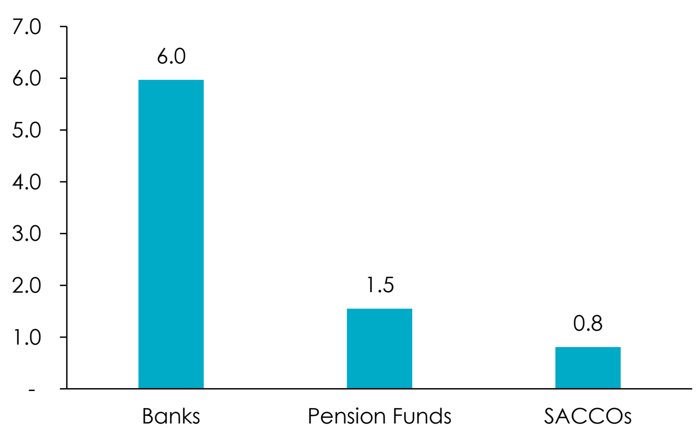
Kenyan Banking Sector Balance Sheet (KES Tn)



Banking Sector Profits and Loan Provisions (KES Bn)



Total Assets as of December 2021 (KES Tn)



Source: CBK, SASRA, RBA Sector Reports, NCBA IB Research

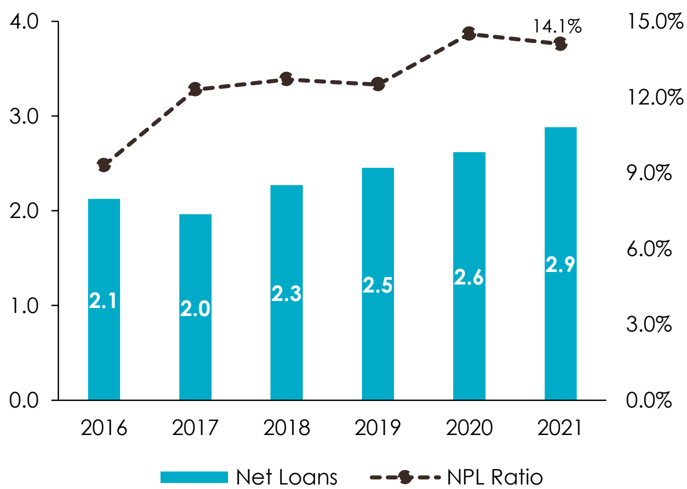
Key Thematic Areas

A. Risk Based Lending

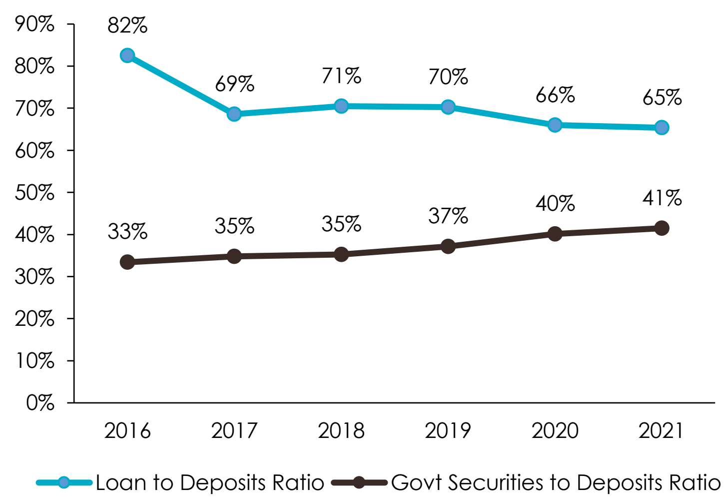
Risk-based lending is a pricing framework which allows banks to set interest rates that are commensurate with the risk profile of the borrower. It assesses inter alia the customer's credit score, financial profile, historical borrowing trends and loan repayment discipline.

The risk-based pricing regime replaces the previous rate cap law which was in place for three years, i.e., September 2016 to November 2019. The regulator had instituted a lengthy approval process for the risk-based model, which led to a delay in adoption of the same. The rate cap, which was intended to reduce the cost of credit, had the unfortunate effect of shrinking access to credit by small businesses and individual borrowers. Consequently, net loans decreased by 8% in 2017 against historical trends and led to increased investments in government securities, as exhibited in the graphs below.

Net Loans - Kenyan Banking Sector (KES Tn)



Deployment of Funds - Kenyan Banking Sector



Source: CBK Banking Sector Reports, NCBA IB Research

As of September 2022, 22 out of the 38 banking institutions had received regulatory approval for their risk-based lending models. A majority of the lenders have however, opted to delay full implementation with the exception of Equity Bank. It recently commenced implementation with a minimum lending rate of 12.52% and a maximum of ~18.5%.

The implementation of risk-based lending will have significant dual-effects on bank's funded income. These are;

i. Higher interest revenue due to the expected increase of lending rates.
ii. Increased quantum of loans advanced. Higher risk borrowers will now be accommodated at proportionate risk-based loan prices.

We expect increased deployment of new funding to loans leading to higher loan to deposit ratios and loan provisions. The increased deployment may be gradual in light of the current macroeconomic variables.

B. Digital Credit Providers (DCPs) Regulations

The Digital Credit Providers Regulations are a new set of regulations published in March 2022, which bring all digital credit providers in Kenya under the ambit of the Central Bank of Kenya (CBK). The main reasons that led to publishing of the regulations were:

i) To cure unscrupulous trading activities such as data mishandling and predatory lending.
ii) To promote soundness of the digital credit financial space whose popularity has drastically increased.

The new regulations require DCPs to have their products and variations-to-product features approved by the CBK, observe sound corporate governance principles and be subject to confidentiality requirements and compliance with the Data Protection Act Number 24, 2019.

As of January 2023, 22 out of 381 applicants had been licensed as digital credit providers, although applicants continue to operate as their licensing is being considered.

Banking institutions and their digital credit products have been operating under the CBK's purview which implies that the impact of the new regulations will be insignificant. The regulations, however, may lead to a microscale windfall to the existing bank digital credit platforms should other digital credit providers struggle to comply with the new regulations. This will lead to a boost in revenue for banking institutions.

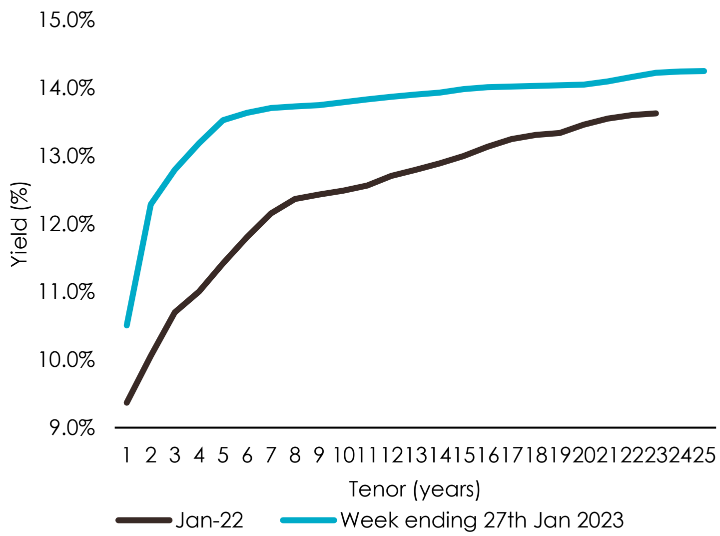
C. Interest Rate Environment

Banking institutions, with a view to de-risk their portfolios, hold a considerable amount of government debt. As of 27th January 2023, banks held KES 2.1Tn (46.8%) of domestic government debt. The balance i.e., 53.2% is held by pension schemes (33.3%), insurance companies (7.4%), parastatals (6.0%) and other investors.

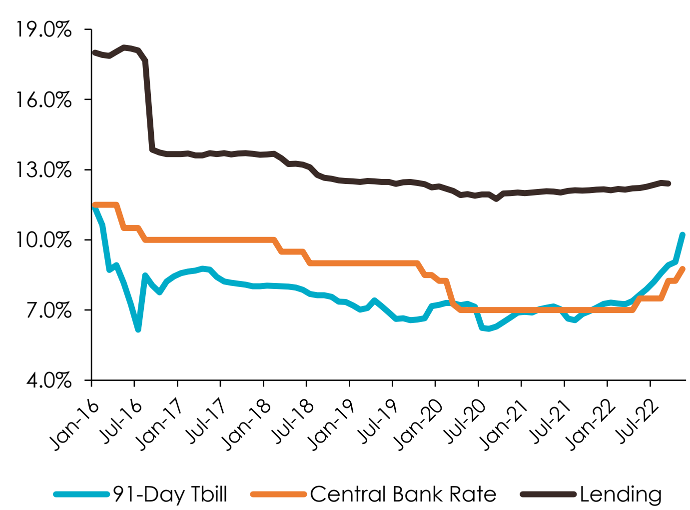
Government bond yields increased significantly in 2022 owing to increased inflation and upward reviews of the Central Bank Rate, 175 bps cumulatively. Rising yields have a negative effect on bond prices. This has led to high unrealized fair value losses recorded by banks in the first three quarters of 2022. We expect the unrealized losses to have little negative effect on the listed Tier I banks, who are well capitalized and have significant customer deposits that reduces the need to sell their bond holdings.

On the other hand, maturities within the year have allowed banks to take advantage of the higher yields.

Government Securities Yield Curve



Lending Rates have not adjusted fully to the Rise in Central Bank Rate



Source: NSE, CBK, NCBA IB Research

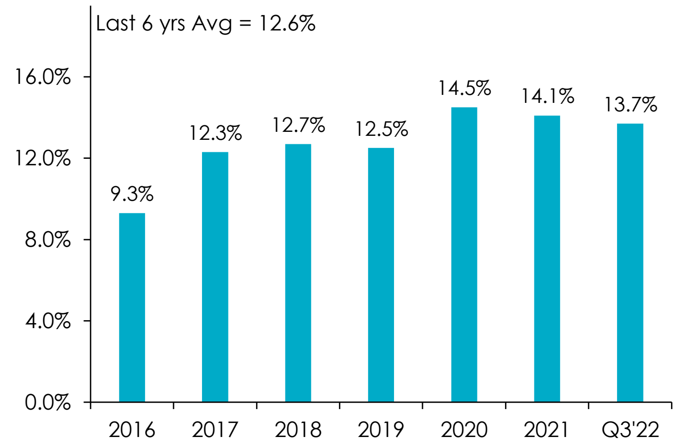
CBK's rate hikes intentions have been to taper inflation which currently stands at 9.0% and to decelerate the Kenyan Shilling depreciation against major currencies. The transmission of the hikes to lending rates has however been slow with banks only announcing changes in November 2022 despite a 175 bps increase in the Central bank rate. Barring any further rate hikes, we expect lending rates and loan interest revenues to edge upwards in Q1'2023 onwards and remain sticky for the rest of the year.

D. Asset Quality

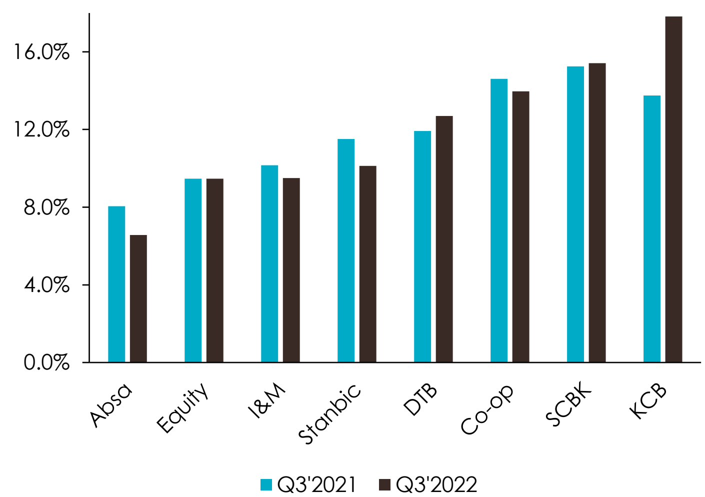
Asset quality is a key concern in the banking sector with non-performing loans ratio deteriorating from below 10% in 2016 to a 7-year peak of 14.5% when the pandemic struck in 2020. The latter adversely affected loan repayment capability of key sectors such as Tourism, Manufacturing, Real Estate and Transport. 57.0% or KES 1.7Tn of the banking sectors loan book was restructured during the 1-year window that commenced in March 2020. This flexibility allowed for management of the NPL ratio within acceptable limits. In the course of 2022, majority of listed banks announced that a vast majority of the previously restructured loans were performing. This should lead to better NPL ratios going forward.

As of Q3'2022, the average banking sector gross NPL ratio stood at 13.7% marginally down from 14.1% in FY'2021, while the listed banking sector NPL ratio improved to 12.0% from 12.4% y-o-y.

Non-Performing Loans (NPL) Ratio



NPL Ratio - Q3'2021 vs Q3'2022



Source: CBK Banking Sector Reports, Respective Banks' Financial Reports, NCBA IB Research

Going forward, we expect a gradual improvement in the banking sector's asset quality with the Kenyan economy on a recovery path. This is however within the context of tougher macroeconomic variables, both globally and locally that are expected to ease in the near term. These include high inflation, weakening currency, elevated oil prices, rising input and production costs, unreliable weather patterns and reduced demand for some of Kenya's major agricultural export (such as cut flowers) – all of which affect various consumer segments.

The administration is keen on improving access to credit for small enterprises. The focus has led to key directives being issued. These include;

a) Credit Repair framework which waived off 50.0% of non-performing mobile phone digital loans by commercial banks, microfinance banks and mortgage finance companies outstanding at the end of October 2022 for six months, up to end of May 2023, and,
b) Credit Reference Bureau framework to retreat from blacklisting using consumers' credit scores. CBK updated the Credit Information Sharing Framework, which mandated the CRBs to include additional metrics in credit scoring.

Possible headwinds include credit risk crystalizing in the medium term once the risk-based pricing lending has taking full effect, and, should the unfavorable global macroeconomic situation persist.

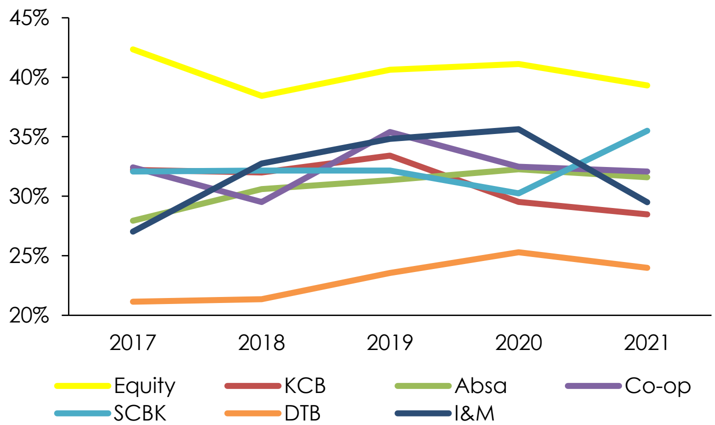
E. Non-funded Income (NFI) – Focus on FX Income

Non-Funded Income refers to revenue generated from non-core activities by the banking institutions such as loan processing fees, late payment charges, service charge and foreign exchange income. Revenue diversification is vital for banks for two key reasons; a) Reduces reliance on interest revenue, and, b) Bolsters the bottom-line because non-interest revenue fluctuates less than interest rates.

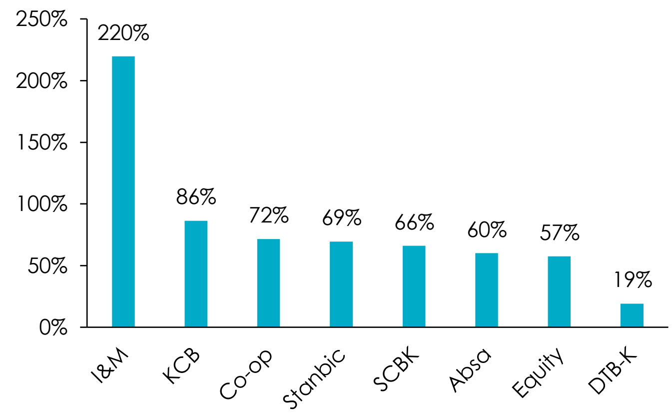
Increased focus on reducing the cost of credit coupled with investment in fintech and consumers' clamor for a one-stop shop services have played a key role in changing the composition of non-funded income. Business lines such as bancassurance, wealth management, digital credit and investment banking services are increasingly contributing to the NFI.

Conscious efforts towards revenue diversification by banks, has trended with NFI at an average of 35% of total operating income in the last six years, as highlighted in the graph. The depreciating KES coupled with increased demand for USD led to wide foreign currency exchange spreads in 2022. Demand pressures have been brought about by an increase in commodity prices such as oil, with Kenya been a net importer. Consequently, foreign exchange income has improved significantly and helped to boost banks' profit levels. As this moderates in 2023, we expect performance to be supported more by funded income.

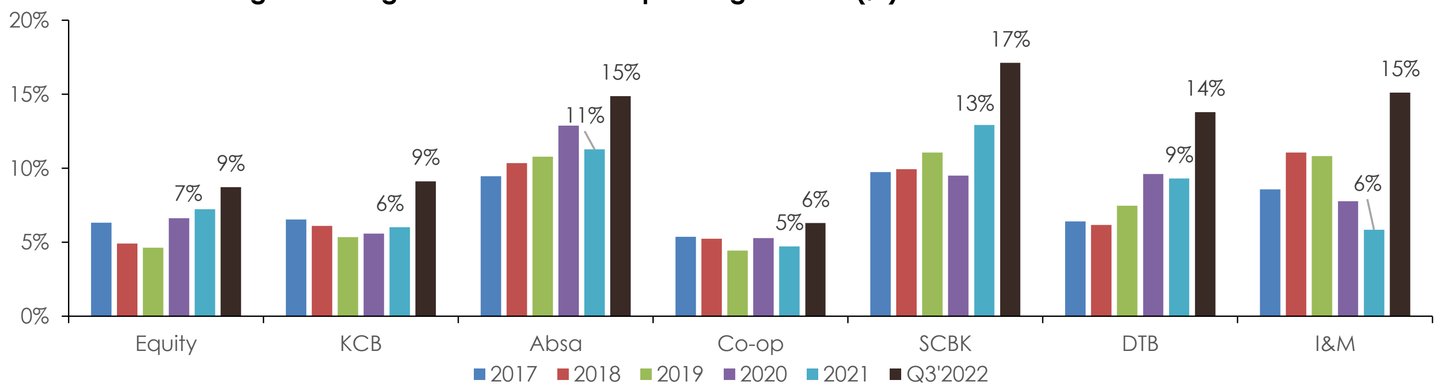
Non-Funded Income contribution to Total Operating Income



FX Income y/y Growth (Q3'22)



Contribution of Foreign Exchange Income to Total Operating Income (%)



Source: Respective Banks' Financial Reports, NCBA IB Research

We expect larger banks such as KCB that have a larger market share of digital credit boosted by Fuliza and KCB M-Pesa, and, Standard Chartered which has a substantial wealth management and advisory business to exhibit superior revenue diversification in comparison to the rest of the market.

Equity Group recently ventured into the insurance business with the launch of Equity Life Insurance in January 2022 while Absa is banking on its asset management business to boost NFI revenues.

Non-funded income is expected to be spurred further by the reintroduction of charges for mobile money wallets and bank transactions effective 1st January 2023.

The reintroduced charges will however be lower. The maximum charge for bank to mobile transactions has been reduced by an average of 61%, mobile to bank reduced by an average of 47% and business pay-bill tariffs by an average of 50%.

F. Regional Diversification

The larger Kenyan banks, are venturing into other markets through mergers and acquisition in a bid to take advantage of growth opportunities in the region and reduce the sovereign risk exposure to Kenya. Democratic Republic of Congo (DRC) market offers an advantage of increased access to foreign currency because US Dollar is widely used in the economy.

Entry into new markets often present a challenge of proving to investors that the capital outlay was worthwhile. Looking at KCB and Equity Group, regional subsidiaries still lag behind in terms of profit and assets contribution. Optimization efforts are still required to improve the businesses with a key focus on Return on Equity and improving asset quality. Equity's Tanzania subsidiary recorded a high NPL ratio of 23.3% in 2021 while KCB's South Sudanese subsidiary had an NPL ratio of 29.6% in the same year.

In December 2022, KCB completed the acquisition of 85% of DRC-based Trust Merchant Bank (TMB). A cash consideration for this acquisition at a price to book multiple of 1.49x (~ KES 16Bn) was to be paid.

This followed the successful entry of Equity Group into the DRC market through acquisition of BCDC in November 2019. In FY'2021, Equity BCDC was the second most profitable subsidiary contributing to the Group 9.4% of PBT and 19.0% of total assets. These figures increased in Q3'2022 to 14.0% of Group PBT and 30.0% of total assets, underpinning the potential that the DRC market offers.

According to the World Bank Global Findex Reports, Kenya has a higher percentage of adults holding bank accounts compared to other countries in the region. Kenya has 79% followed by Uganda, Tanzania and Rwanda at 66%, 52% and 50% respectively. DRC has only 26% hence proving to be an attractive market due to its population size and ability to scale revenue upwards organically.

NPL Ratio	KCB		Equity	
	2020	2021	2020	2021
Tanzania	6.1%	2.7%	35.4%	23.3%
Rwanda	5.1%	1.8%	2.9%	8.7%
Kenya	12.4%	15.9%	11.5%	8.2%
National Bank Kenya	38.1%	31.6%	-	-
DRC	-	-	9.0%	6.7%
Uganda	6.8%	5.4%	4.9%	4.9%
South Sudan	68.7%	29.6%	1.2%	0.7%
Rwanda	5.1%	1.8%	-	-
BPR	-	7.5%	-	-
Burundi	4.1%	1.8%	-	-

Equity Group Regional Subsidiaries' Perfomance	2020	2021	Target
Profit Before Tax (% of Group)	34%	22%	25% - 30%
Asset Size (% of Group)	39%	41%	40% - 45%

KCB Group Regional Subsidiaries' Perfomance	2020	2021	Target
Profit Before Tax (% of Group)	12%	11%	20%
Asset Size (% of Group)	10%	15%	-

Source: Respective Banks' Financial Reports, NCBA IB Research

Performance of the Listed Banks as of Q3'2022

Sustained Earnings Growth as two more counters declare Interim Dividends for Investors

All banks recorded double digit growths in core Earnings per Share (EPS).

Standard Chartered Bank and KCB Group announced interim DPS of KES 6.0 and KES 1.0 respectively in Q3'2022 while Absa announced a DPS of KES 0.2 in H1'2022.

Despite the improved performance, the share prices of the listed banks had muted movements due to the prevailing tough macroeconomic conditions, the un-abating foreign investor sell-offs as international investors attach higher risk premium to emerging & frontier markets and higher interest rate hikes in the advanced markets which have increased the attractiveness of their bond markets and banking sector stocks.

TABLE I: Earnings and Price Performance

Institution	EPS	EPS Change	Interim Dividend	Implied Dividend Yield	Current Price*	Target Price	Upside	Recomm-endation	YTD 2023 Change	52-Wk High	52-Wk Low
Co-op Bank	2.9	47%	-	0.0%	**12.40**	15.10	22%	**BUY**	1.2%	14.00	10.00
Standard Chartered	22.6	37%	**6.00**	4.2%	**157.00**	156.93	0%	**HOLD**	10.2%	155.25	115.00
Stanbic	41.0	37%	-	0.0%	**110.75**	113.03	2%	**HOLD**	7.8%	112.00	82.00
ABSA Bank	2.0	30%	**0.20**	1.7%	**12.45**	14.52	17%	**ACCUMULATE**	0.8%	13.40	9.00
Equity Group	8.8	27%	-	0.0%	**45.05**	59.32	32%	**BUY**	(1.1%)	56.00	38.75
I&M Group	4.1	25%	-	0.0%	**17.00**	23.40	38%	**BUY**	0.0%	23.00	16.00
KCB	12.6	21%	**1.00**	2.6%	**38.10**	53.80	41%	**BUY**	0.0%	48.00	32.50
DTB Kenya	20.6	19%	-	0.0%	**50.00**	62.53	25%	**BUY**	0.0%	65.50	44.50

Source: Respective Banks' Financial Reports, NCBA IB Research
****Current Prices – as of 31st January 2023***

Foreign Income Exchange Gains Boost Non-Funded Income

- All Tier 1 banks benefited from the KES depreciation against the USD. As the USD appreciated and preference for hard currencies increased, the demand for the greenback led to wider spreads in the exchange rate. This led to a 60.5% y/y growth in aggregate FX income as of Q3'2022.
- The significant uptick in Kenya's yield curve led to fair value losses from government securities across the sector. The fair value losses are not expected to hamper the banks' income as the focus will slowly shift towards leveraging the risk-based pricing model's higher rates and NFI until the interest rates environment stabilizes.
- In terms of efficiency, the NFI-boosted faster growth in operating income. Conscious efforts by lenders in reigning in on their recurrent expenses, saw broad declines in Cost to Income ratio (CIR) without Loan Provisions.

Table II: Income Statement (Amounts in KES Bn)

Institution	PAT	PAT Change	RoA	RoE	TOPI Change	OpEx Change	CIR with Loan loss provision	CIR w/o Loan loss provision	NFI/ TOPI	FX income change	FVOCI Loss
Equity	**33.4**	27%	2.4%	**21.6%**	27%	32%	57%	**47%**	41%	**57%**	(45.0)
ABSA Bank	**10.7**	30%	2.2%	**17.8%**	22%	19%	55%	**40%**	30%	**60%**	(2.1)
Co-op Bank	**17.1**	47%	2.7%	**16.9%**	18%	6%	57%	**46%**	39%	**72%**	(10.1)
KCB	**30.6**	21%	2.4%	**16.1%**	15%	7%	51%	**43%**	33%	**86%**	(7.2)
Standard Chartered	**8.7**	37%	2.4%	**15.7%**	10%	(8%)	50%	**47%**	36%	**66%**	(1.5)
Stanbic	**7.0**	37%	1.9%	**13.9%**	31%	(21%)	58%	**45%**	45%	**69%**	(0.0)
I&M Group	**6.8**	25%	1.6%	**9.3%**	24%	(88%)	60%	**45%**	35%	**220%**	(5.9)
DTB Kenya	**5.8**	20%	1.1%	**7.4%**	21%	21%	62%	**45%**	29%	**81%**	(3.4)

Source: Respective Banks' Financial Reports, NCBA IB Research

Asset Quality remains a Key Concern

- Total assets increased by 13% y/y to KES 6.0Tn, driven mainly by net loans and advances which grew by 17% as the economy improved compared to 2021 when it was still reeling from COVID-19 effects.
- Equity and KCB Groups accounted for 44% of the total assets - KCB's acquisition of DRC-Based Trust Merchant Bank (TMB) is envisaged to further increase this figure.
- Standard Chartered continued with its loan book optimization which saw its balance sheet expanding by only 3% while the NPL ratio remained unchanged at 15, which is 4% above industry average.
- Asset quality remains a key concern and with the current macroeconomic conditions, it goes without saying that debt servicing will be a challenge to borrowers.
- As of Q3'2022, the NPL ratio for listed banks was 12.0%, significantly above the 10-year sector average of 8.7% but slightly below the 14.1% level recorded at the end of 2021.
- On a positive note, listed banks have increased their NPL Coverage ratio to 66.3% from 64.7% while total provisions increased by 13% on a y/y basis.

Table III: Balance Sheet (Amounts in KES Bn)

Institution	Assets	Loans	Loans Growth	NPL Ratio	NPL Coverage	Deposits	Deposits Growth	LDR (%)
Equity Group	1,363.7	673.9	21%	9.8%	60.6%	1007.3	15%	67%
KCB	1,276.3	758.8	16%	17.8%	52.8%	922.3	7%	82%
Co-op Bank	622.1	335.2	9%	14.0%	69.3%	432.0	3%	78%
DTB Kenya	507.5	243.7	19%	12.7%	45.2%	359.7	11%	68%
ABSA Bank	481.3	289.4	26%	6.6%	80.0%	281.1	5%	103%
I&M Group	428.7	231.2	11%	9.5%	75.4%	308.0	7%	75%
Stanbic	371.4	236.9	34%	10.1%	63.4%	267.3	26%	89%
Standard Chartered	366.1	136.1	3%	15.4%	82.4%	286.1	11%	48%
Average				**12.1%**	**66.1%**			**74%**

Source: Respective Banks' Financial Reports, NCBA IB Research

Valuation Ratios

Listed banks are currently trading at a market cap-weighted price to tangible book value (P/B) of 0.9x – indicating that the banking counters are almost priced at par with their book values. There exist outliers such as DTB Kenya which has the lowest P/B and P/E of 0.2x and 1.8x, respectively, while Equity, Standard Chartered and Absa Bank are trading at a marginal premium to their tangible book values.

The market cap-weighted average P/E is at 3.8x, below NASI's P/E of 6.6x. This is indicative of the bear run at the bourse with banking stocks suffering more due to their high liquidity. Notably, the P/E for listed banks stood at 4.9x and 7.4x in FY'2021 and FY'2020, respectively.

Institution	Current Price (KES) – 31/01/23	Tangible Book Value (KES Bn)	Annualized Earnings (KES Bn)	P/B	P/E
Equity Group	45.05	141.4	44.5	**1.2x**	**3.8x**
Standard Chartered	157.00	51.2	11.6	**1.2x**	**5.1x**
ABSA Bank	12.45	59.8	14.3	**1.1x**	**4.7x**
Stanbic	110.75	49.5	9.3	**0.9x**	**4.7x**
Co-operative Bank	12.40	94.0	22.8	**0.8x**	**3.2x**
KCB	35.00	184.1	40.8	**0.7x**	**3.0x**
I&M Group	38.10	66.7	9.1	**0.4x**	**3.1x**
DTB Kenya	17.00	77.0	7.7	**0.2x**	**1.8x**
Market capitalization -weighted Average				**0.9x**	**3.8x**

Source: Respective Banks' Financial Reports, NCBA IB Research

DETAILED COVERAGE OF INDIVIDUAL BANKS

EQUITY GROUP HOLDINGS PLC

We maintain our **BUY** recommendation based on a target price of KES 59.32 implying a 31.7% upside, from the current price of KES 45.05 as of 31st January 2023, exclusive of dividend yield.

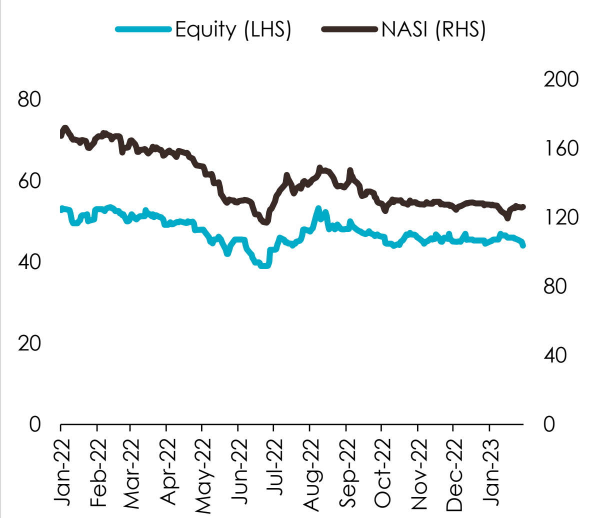
The recommendation is based on the bank's organic balance sheet growth, renewed focus on increasing its topline through increased allocation to higher-yielding loans, strong performance of subsidiaries especially DRC and healthy efficiency ratios.

At the current market price, the stock is trading below its fair value and presents a value pick for long-term investors.

Share Data	Equity Group
Ticker	EQBNK KN
RECOMMENDATION	**BUY**
Current Price (KES)	45.05
Target Price (KES)	59.32
Upside(Excl. Div. Yield)	31.7%
52WK High (KES)	56.00
52WK Low (KES)	38.75
Market Cap (KES Bn)	170.00
Free Float	78.3%
P/B	1.2x
P/E (Annualized)	3.8x
Current Price = as of 31st Jan 2023	

Source: Bloomberg, NSE, NCBA IB Research

Equity vs NASI Performance (LTM)



Source: NSE, NCBA IB Research

Q3'2022 Performance (% = y/y performance)

- **Earnings:** PAT grew by 26.6% y/y attributed to strong growth in both Net Interest Income and Non-Funded Income. As a result, EPS improved to KES 8.8 from KES 7.0 in Q3'2021.

- **Non-Funded Income** grew faster than Net Interest Income, mainly driven by a 57.5% y/y in FX Income as banks continue to experience a windfall following weakening of KES against USD amid high demand for the hard currency. Fees and Commissions also rose by 13.3% on account of increased loans and advances to customers.

- **Balance Sheet**: Net Loans grew increased by 20.6% to KES 673.9Bn, an accelerated pace compared to Govt. Securities which saw a 0.1% decline to KES 233.0 and underlining the Group's shift to focusing on loan book expansion.

- **Customer Deposits**: Deposits grew by 15% to hit the KES 1.0Tn mark underlining the lenders' strong resilience in a tough operating environment. Notable though, the growth comes on the back of management's guidance of 25%-30% growth in FY'2022. The loan to deposit ratio increased to 67% from 64% in Q3'2021.

- **Asset Quality:** The lender's NPL ratio remained largely unchanged from Q3'2021 at 9.5%, as the group boosted its loan provisions by KES 9.7Bn to cater for additional credit risk occasioned by the unfavorable macroeconomic environment.

Outlook

We expect Equity Group to maintain its strong profits and asset growth performance due to:

1. **Focus on higher disbursement of loans:** Loans often yield more than government securities and as a result of this focus, we anticipate Equity to register higher Net Interest Income in the near term. The shift from government securities is timely following the lender's recent adoption of the risk-based lending.

2. **Strong performance of regional subsidiaries:** The subsidiaries contributed 41% of total assets as of Q3'2022 which was within management's target and 22% of profitability. The Group's performance is expected to be bolstered by this continued strong performance especially Equity BCDC in DRC which contributed 10% of total profitability in FY'2021 and has further growth potential owing to the countries low banking penetration.

- **Dividend Outlook:** We expect Equity Group to issue a full year dividend following its strong performance. Our outlook is for a 26% dividend payout ratio.

Valuation and Investments Recommendation – Equity Group

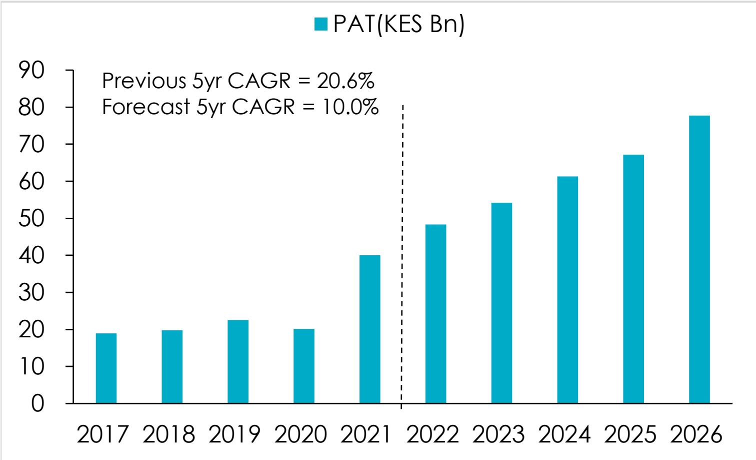
Assumptions

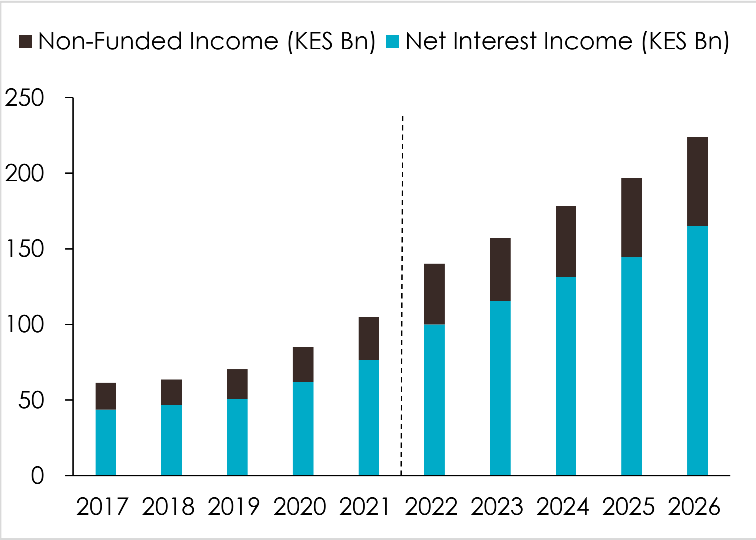
- Risk free rate of 12.45% based on the 10-year Treasury bond historical yields.
- Tax rate of 30%
- Equity risk premium of 5.4%
- Adjusted Beta of 1.3 on stock's relative volatility on the index.
- Long term growth rate of 5.0% based on average GDP forecast.

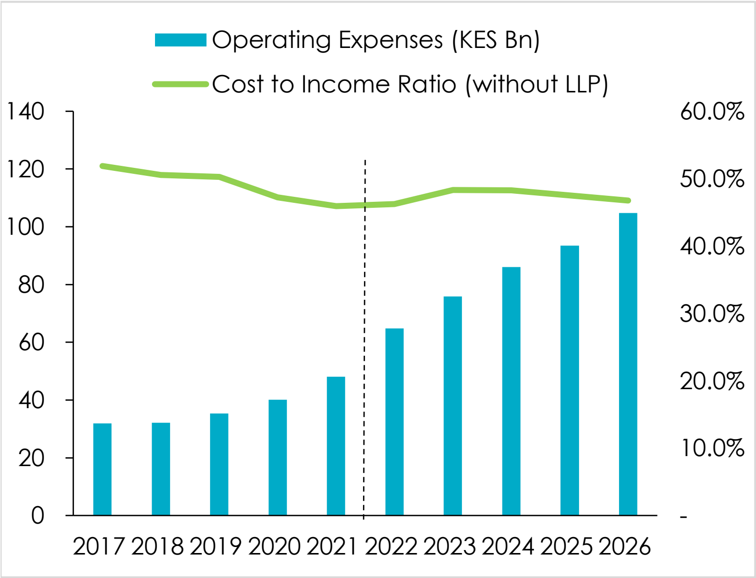
Valuation Methodology	Implied Price	Weighting	Weighted Value
Residual Income	73.99	40%	29.60
DDM	70.50	15%	10.58
P/BV	41.35	40%	16.54
P/E	52.09	5%	2.60
Fair Value		**100%**	**59.32**
Current Price			**45.05**
Upside/(Downside)			31.7%

Source: NCBA IB Research Estimates

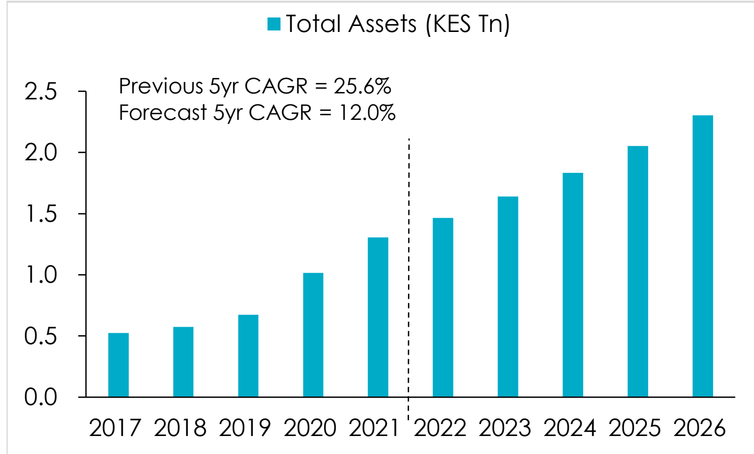
Income Statement Projections – Equity Group

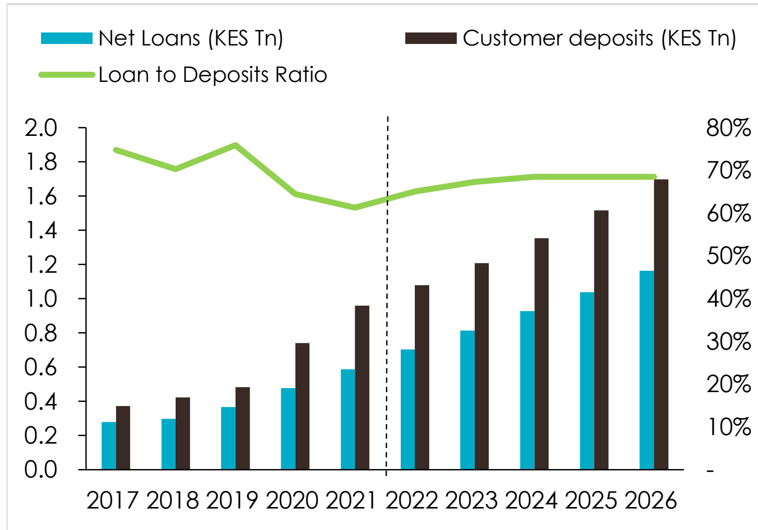


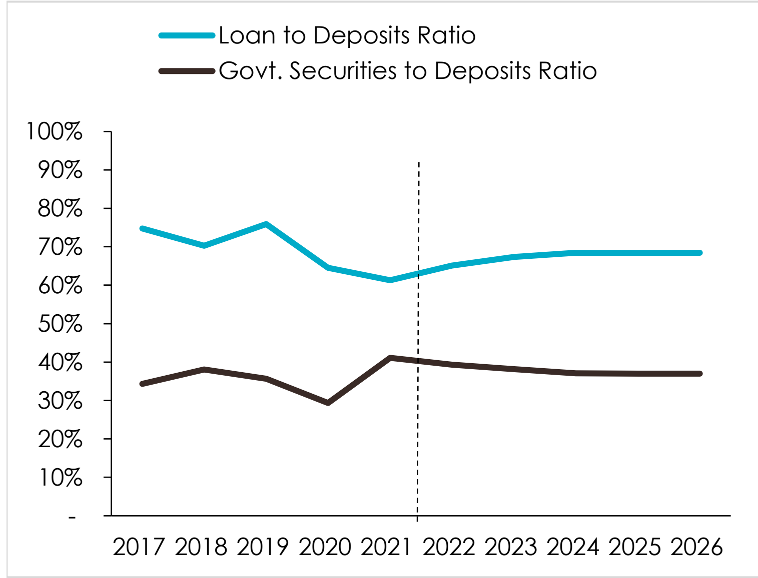




Balance Sheet Projections – Equity Group







ABSA BANK KENYA PLC

We have updated our recommendation to **ACCUMULATE** based on a target price of KES 14.52 implying a 16.6% upside, from the current price of KES 12.45 as of 31st January 2022, exclusive of dividend yield.

We expect the bank to continue generating long-term profitability based on its focus on channel diversification, impressive asset quality, and, entrance into new business lines namely custody and asset management.

At the current market price, the stock is trading within its fair value but presents a value pick for long-term investors owing to its reliable dividend payouts.

Share Data	Absa Bank
Ticker	ABSA KN
RECOMMENDATION	**ACCUMULATE**
Current Price (KES)	12.45
Target Price (KES)	14.52
Upside(Excl. Div. Yield)	16.6%
52WK High (KES)	13.40
52WK Low (KES)	9.00
Market Cap (KES Bn)	67.62
Free Float	30.5%
P/B	1.1x
P/E (Annualized)	4.7x
Current Price = as of 31st Jan 2023	

Source: Bloomberg, NSE, NCBA IB Research

Q3'2022 Performance (% = y/y performance)

- **Earnings:** PAT grew by 30.1% y/y attributed to strong growth in both Net Interest Income and Non-Funded Income. As a result, EPS improved to KES 2.0 from KES 1.5 in Q3'2021.

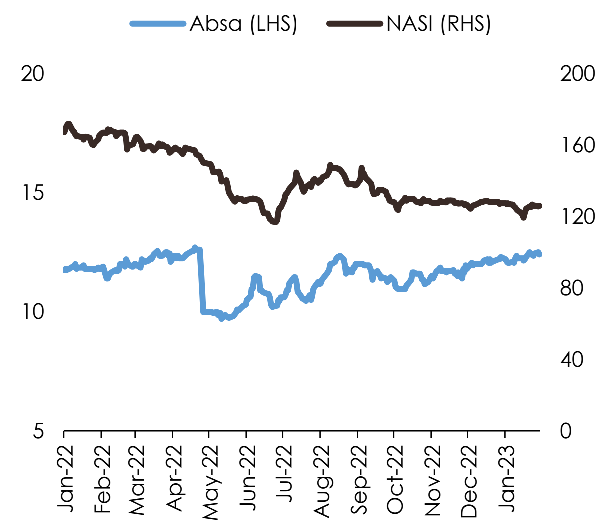
- The lender's performance was driven by topline growth as **Net Interest Income** grew faster than Non-Funded Income. The former was driven by 26.4% growth in Net loans to KES 289.4B. **Non-Funded Income** grew by 16.4% boosted by Foreign Exchange income. FX income increased by 60% to KES 5.0Bn.

- **Balance Sheet**: The high growth in loans was attributed to growth in foreign currency loans which was funded primarily by borrowing from the Group.

- **Customer Deposits**: Deposits grew by 4.6% y/y to KES 281.1Bn but declined marginally from H1'2022. The stagnation is concerning especially looking at the peer banks' performance. The Loan to Deposits ratio subsequently surged to 103% from 85% in Q3'21 while borrowings increased by 69% to KES 101.8Bn. Management noted that it is committed to grow customer deposits but at a low cost.

- **Asset Quality:** The lender's NPL ratio improved to an impressive 6.6% from 8.1% in Q3'2021, and below the industry average of 13.7%. Loan provisions increased by 48% to KES 5.0Bn as a result of the deteriorating macroeconomic conditions and boosting the lender's NPL Coverage to 80% from 74.5%.

Absa vs NASI Performance (LTM)



Source: NSE, NCBA IB Research

Outlook

We expect Absa Bank to sustain its current growth momentum and profitability due to:

1. **Improved efficiency level:** The bank's cost to income ratio without loan loss provisions decreased to 40% in Q3'2021, as a result of investments in its digital banking solutions. Absa has sufficient capacity to embark on cost rationalization measures that will increase its profitability.

2. **Revenue diversification:** The bank's focus on Asset Management in addition to Bancassurance and Timiza offering are expected to sustain the NFI revenue Line. NFI contributed 30% to total operating income in Q3'2022.

3. **Expected Topline growth:** With the implementation of risk-based pricing model and CBR rate hikes yet to be effected in Absa's lending rates, the growth potential for interest income is high.

- **Dividend Outlook:** As per our expectation, management confirmed that the bank will pay out a final dividend following the full year results. Absa paid out a KES 0.20 interim dividend in Q3'2022.

Valuation and Investments Recommendation – Absa Bank

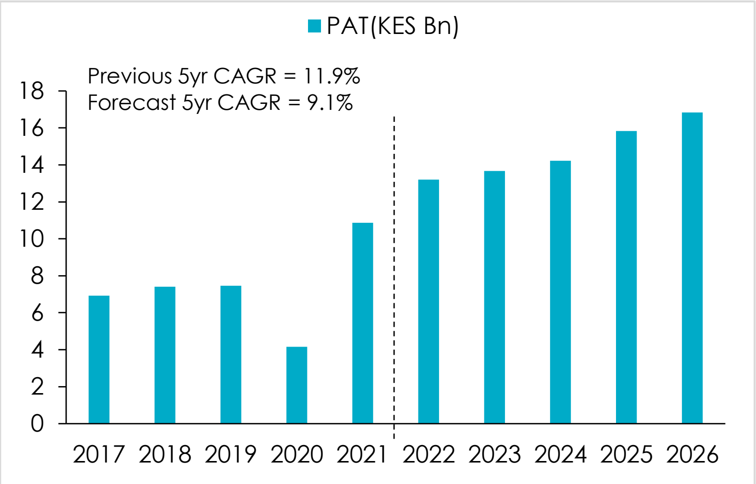
Assumptions

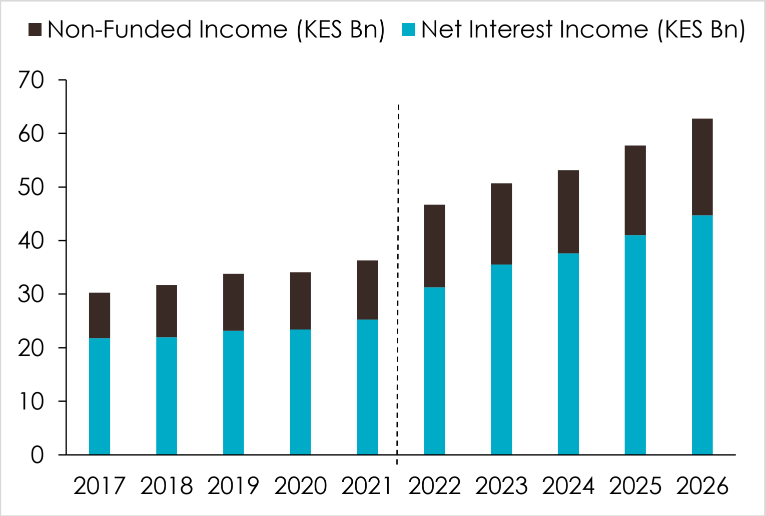
- Risk free rate of 12.45% based on the 10-year Treasury bond historical yields.
- Tax rate of 30%
- Equity risk premium of 5.4%
- Beta of 1.1 on stock's relative volatility on the index.
- Long term growth rate of 5.0% based on average GDP forecast.

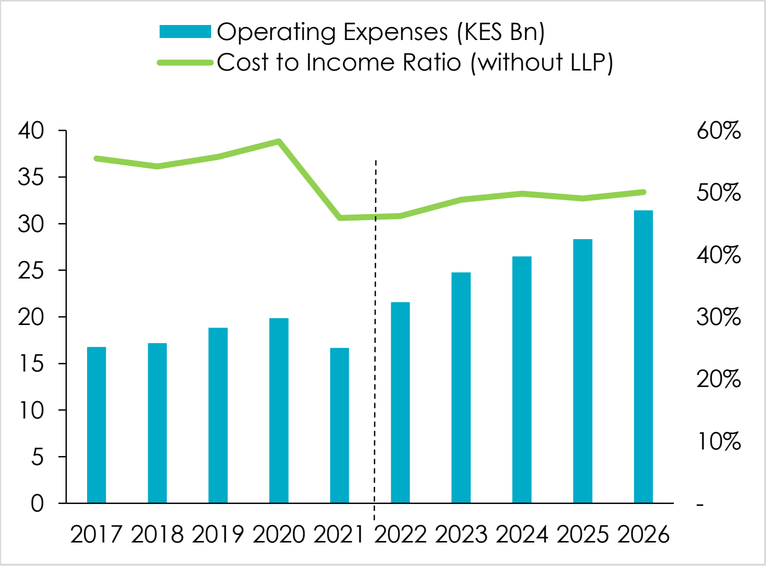
Valuation Methodology	Implied Price	Weighting	Weighted Value
Residual Income	16.68	40%	6.67
DDM	16.74	30%	5.02
P/BV	9.39	25%	2.35
P/E	9.57	5%	0.48
Fair Value		**100%**	**14.52**
Current Price			**12.45**
Upside/(Downside)			16.6%

Source: NCBA IB Research Estimates

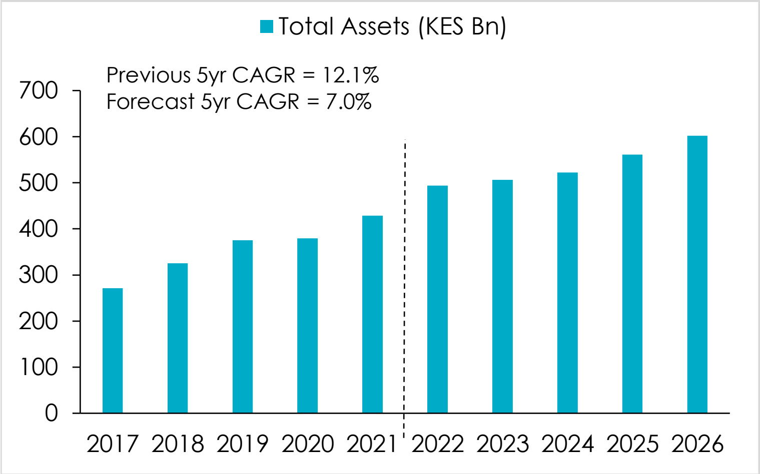
Income Statement Projections – Absa Bank

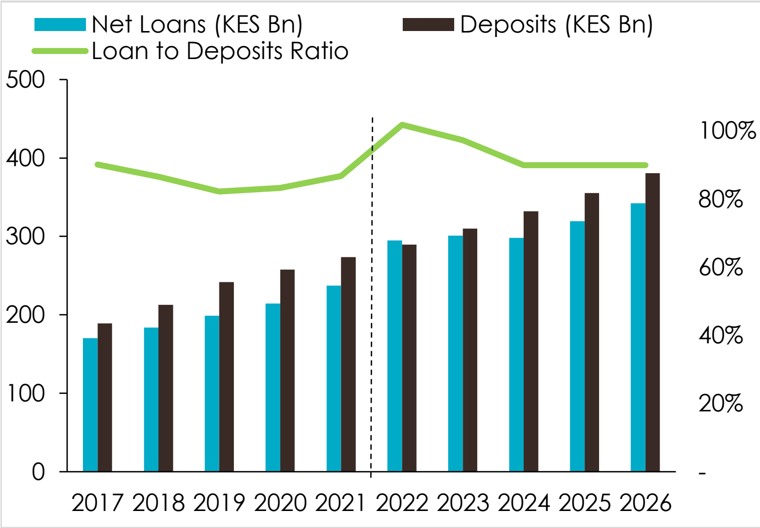


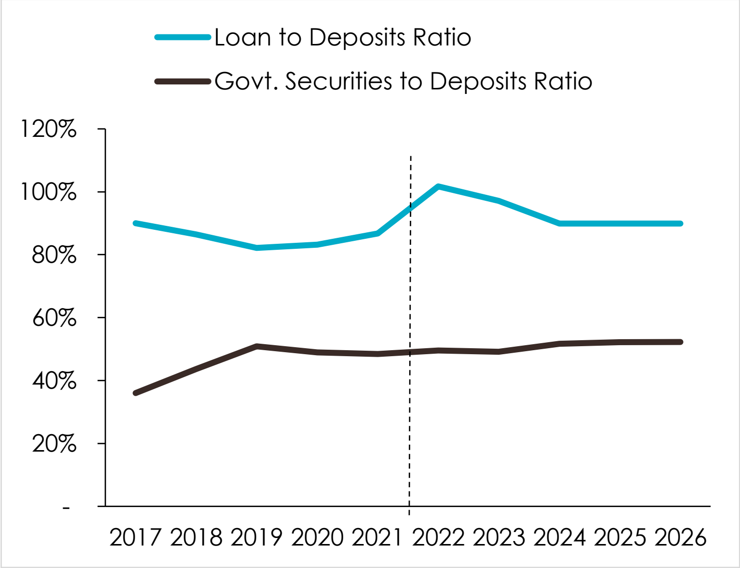




Balance Sheet Projections – Absa Bank







KCB GROUP PLC

We maintain our **BUY** recommendation based on a target price of KES 53.80 implying a 41.2% upside, from the current price of KES 38.10 as of 31st January 2023, exclusive of dividend yield.

We expect the bank to record strong profit and asset growth owing to its strong capital base facilitating balance sheet expansion, entry into DRC market in December 2022 through acquisition of TMB Bank, management efforts to improve asset quality, and loan book resiliency.

At the current market price, the stock is trading below its fair value and presents a value pick for long-term investors.

Share Data	KCB Group
Ticker	KNCB KN
RECOMMENDATION	**BUY**
Current Price (KES)	38.10
Target Price (KES)	53.80
Upside(Excl. Div. Yield)	41.2%
52WK High (KES)	48.00
52WK Low (KES)	32.50
Market Cap (KES Bn)	122.43
Free Float	77.6%
P/B	0.7x
P/E (Annualized)	3.0x
Current Price = as of 31st Jan 2023	

Source: Bloomberg, NSE, NCBA IB Research

Q3'2022 Performance (% = y/y performance)

- **Earnings:** PAT grew by 21.4% y/y driven by a 30.2% growth in Non-Funded Income coupled with a 22.1% decline in loan provisions. Overall, EPS improved to KES 12.6 from KES 10.4 in Q3'2021.

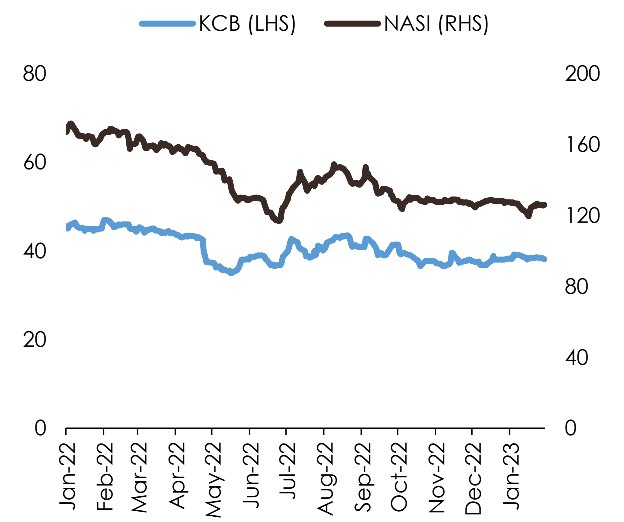
- **Balance Sheet**: Total Assets grew by 13.7% to KES 1.3Tn boosted by loan book expansion of 16.4%. The growth on loans was faster than that of deposits (7.4%) leading to the loan deposit ratio increasing to 82% from 76%.

- **Asset Quality:** The lender's Asset Quality remains a key concern as the NPL ratio worsened to 17.8% from13.7% in 3'2021. This was a slight improvement from H1'2022 when it stood at 21.4% but still noticeably higher than the industry average.
- More worrying is the fact that the lender reduced its period provisioning levels y/y leading to a worsening of the NPL Coverage ratio to 52.8% from 63.4% in Q3'2021.
- Management expects the NPL ratio to improve to ~17% as of FY'2022 and reduce gradually in 2023.

- **Subsidiaries Performance:** As of FY'2021, regional subsidiaries contributed 11% of profitability against management's guidance of 20%, implying that there is still room for growth.
- National Bank of Kenya (NBK) profits decreased by 25% y/y in Q3'2022 to KES 0.8Bn while NPL ratio declined by 25.3%.

- **TMB Acquisition:** KCB has concluded acquisition of 85% of DRC-based Trust Merchant Bank (TMB). TMB, the 3rd largest bank in DRC, offers significant bottom-line growth given its loan to deposit ratio of 32% offering opportunity for balance sheet realignment. It also operates in a region in which US Dollar is widely used hence it would bolster KCB's FX access.

KCB vs NASI Performance (LTM)



Source: NSE, NCBA IB Research

Outlook

We expect KCB Group to continue recording strong performance due to:

1. **Continued loan book growth** which will be boosted by both organic growth and the TMB Bank acquisition.

2. **Subsidiaries growth:** The Group intends to undertake cost rationalization measures of KES 750Mn in NBK and ~KES 250Mn BPR (Rwanda), with the intention of improving the performance of the two subsidiaries. The success of these measures coupled by improving NPL ratios is expected to support KCB's long term growth.

- A key downside risk is their worsening asset quality should the macroeconomic conditions deteriorate.

- **Dividend Outlook:** We expect KCB Group to issue a full year dividend following its strong performance. KCB paid out a KES 1.00 interim dividend in Q4'2022.

Valuation and Investments Recommendation – KCB Group

Assumptions

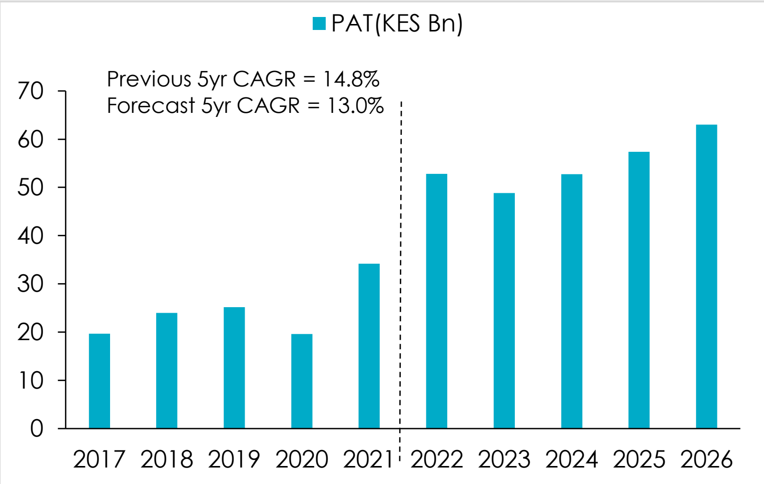
- Risk free rate of 12.45% based on the 10-year Treasury bond historical yields.
- Tax rate of 30%
- Equity risk premium of 5.4%
- Beta of 1.2 on stock's relative volatility on the index.
- Long term growth rate of 5.0% based on average GDP forecast.

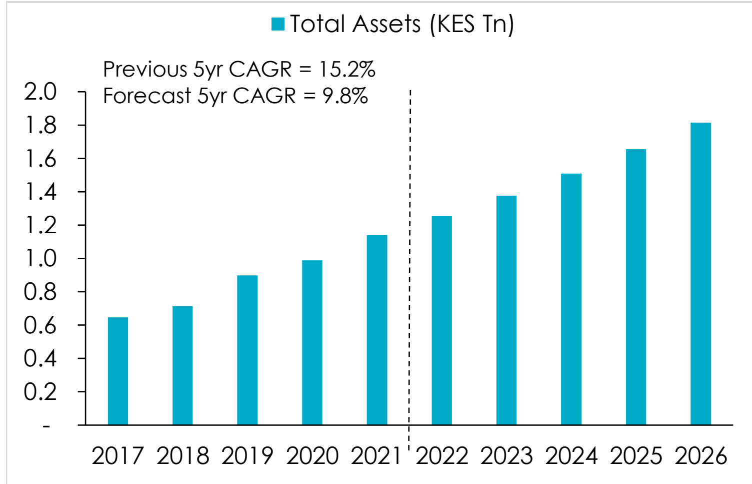
Valuation Methodology	Implied Price	Weighting	Weighted Value
Residual Income	57.36	35%	20.07
DDM	58.36	20%	11.67
P/BV	48.78	40%	19.51
P/E	50.85	5%	2.54
Fair Value		**100%**	**53.80**
Current Price			**38.10**
Upside/(Downside)			41.2%

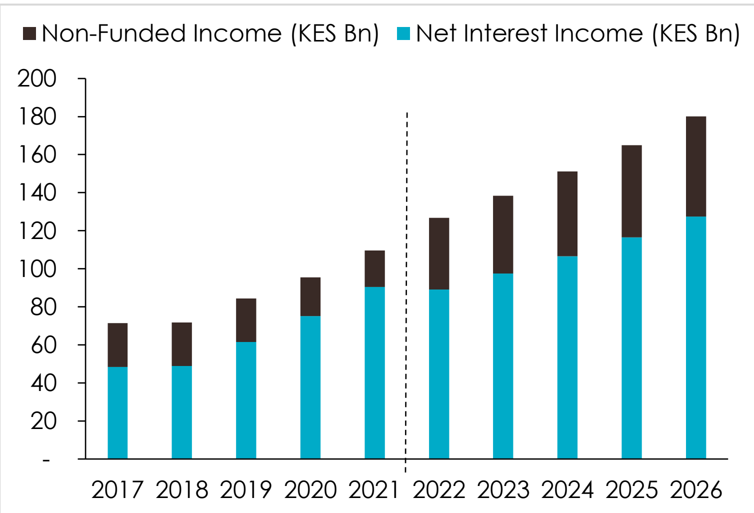
Source: NCBA IB Research Estimates

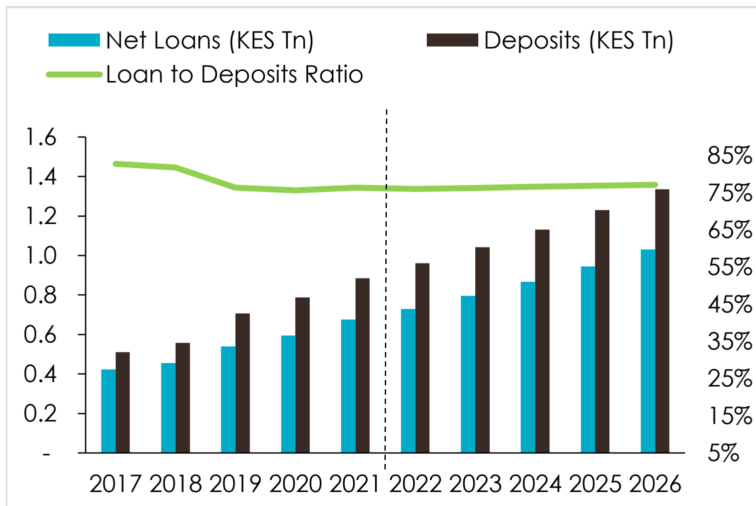
Income Statement Projections – KCB Group

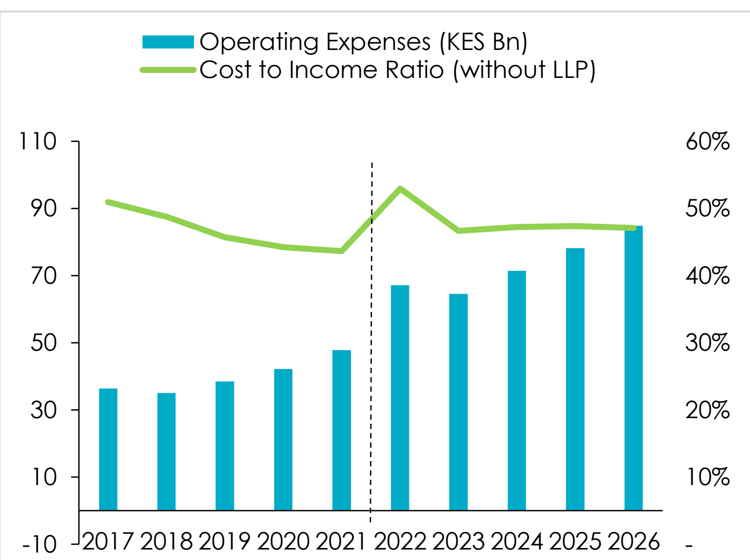
Balance Sheet Projections – KCB Group

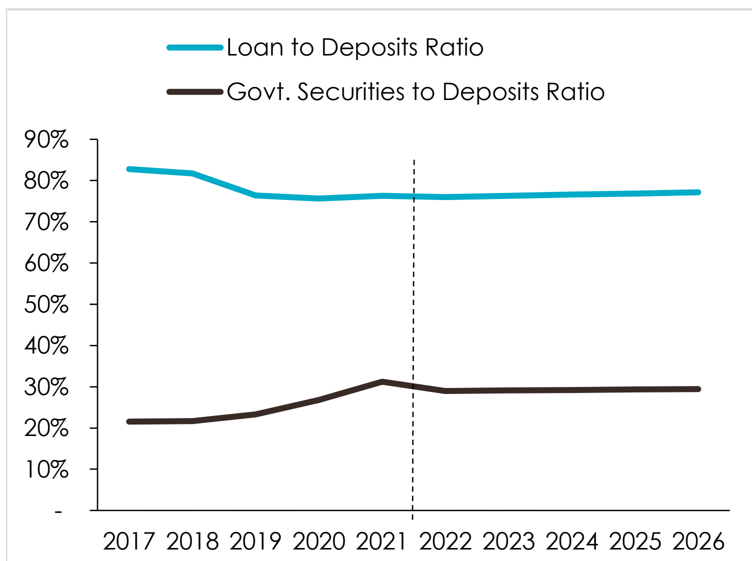












CO-OPERATIVE BANK OF KENYA

Share Data	Co-operative Bank
Ticker	COOP KN
RECOMMENDATION	**BUY**
Current Price (KES)	12.40
Target Price (KES)	15.10
Upside(Excl. Div. Yield)	21.8%
52WK High (KES)	14.00
52WK Low (KES)	10.00
Market Cap (KES Bn)	72.75
Free Float	13.5%
P/B	0.8x
P/E (Annualized)	3.2x
Current Price = as of 31st Jan 2023	

Source: Bloomberg, NSE, NCBA IB Research

We have updated our recommendation to **BUY** based on a target price of KES 15.10 implying a 25.8% upside, from the current price of KES 12.40 as of 31st January 2023, exclusive of dividend yield.

We expect the bank to continue to generate long-term profitability based on its focus on digital lending, strong customer base, impressive asset quality, and, healthy cost to income ratios.

At the current market price, the stock is trading within its fair value but presents a value pick for long-term investors owing to its reliable dividend payouts.

Q3'2022 Performance (% = y/y performance)

- **Earnings:** PAT grew by 47.0% y/y attributed to double-digit growth in both Net Interest Income and Non-Funded Income. As a result, EPS improved to KES 2.9 from KES 2.0 in Q3'2021.

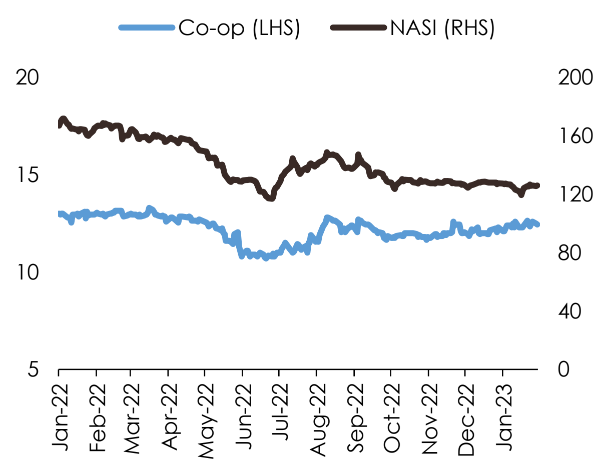
- **Non-Funded Income** grew faster than Net Interest Income, mainly driven by a 71.6% y/y in FX income as banks continue to take advantage of the arbitrage opportunities arising from the weakening KES against the USD. Fees and commissions also rose by 52.0% on account of increased loans and advances to customers.

- **Balance Sheet**: Faster growth in loan book in comparison to customer deposits led the Loan to Deposit ratio to increase to 77.6% from 72.9%. Notably, government securities holding shrunk by 5.7% y/y to KES 182.4 against market trend.
Total Assets stand at KES 622.1Bn.

- **Asset Quality:** The lender's NPL ratio improved to 14.0% from 14.6% in Q3'2021, but remained above the industry average. The improvement was brought about by faster growth in gross loans than gross NPLs.

- **NPL Coverage:** Coverage rose to 69.3% from 65.5% as the bank sought to cover itself against possible future losses.

Co-op vs NASI Performance (LTM)



Source: NSE, NCBA IB Research

Outlook

We expect Co-operative Bank's future growth to be propelled by:

1. **Improved efficiency levels:** The bank's cost to income ratio without loan loss provisions decreased to 45.8% in Q3'2022, owing to management efforts to contain recurrent expenditures. These efforts, if sustained, will lead to increased profitability for the lender in the long-term as focus shifts to the topline.

2. **Digital loans growth supported by a strong customer base:** The bank's main clients, co-operatives, will continue to provide a stable source of revenue. The bank's focus on digital lending through its products such as M-Co-op Cash will also support NFI line growth. Additionally, we expect the bank to swiftly implement the risk-based pricing model to boost loan interest income in the short term.

- **Dividend Outlook:** We expect Co-operative Group to issue full year dividends following its improved performance in 2022.

Valuation and Investments Recommendation – Co-operative Bank of Kenya

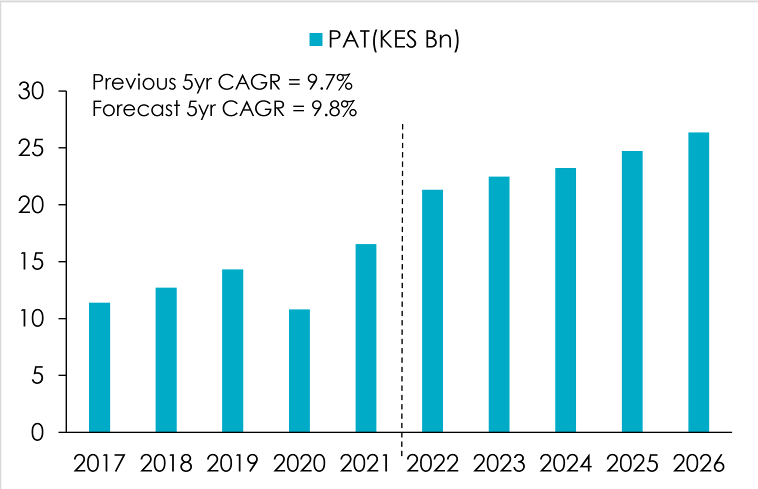
Assumptions

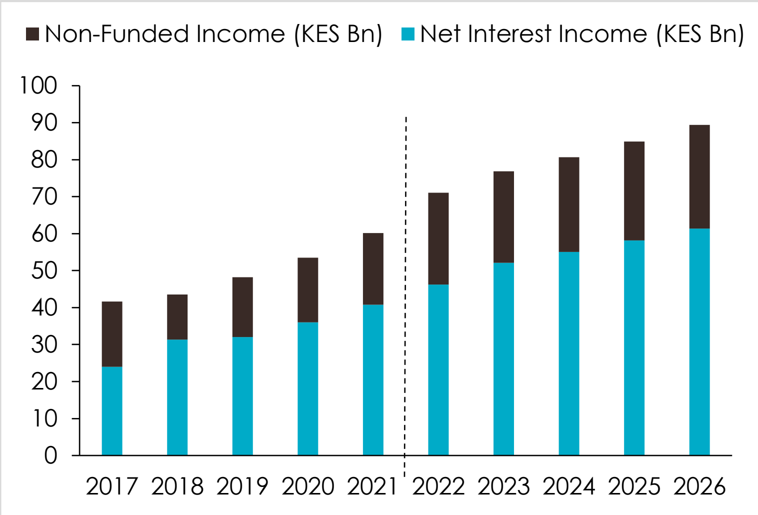
- Risk free rate of 12.45% based on the 10-year Treasury bond historical yields.
- Tax rate of 30%
- Equity risk premium of 5.4%
- Beta of 0.97 on stock's relative volatility on the index.
- Long term growth rate of 5.0% based on average GDP forecast.

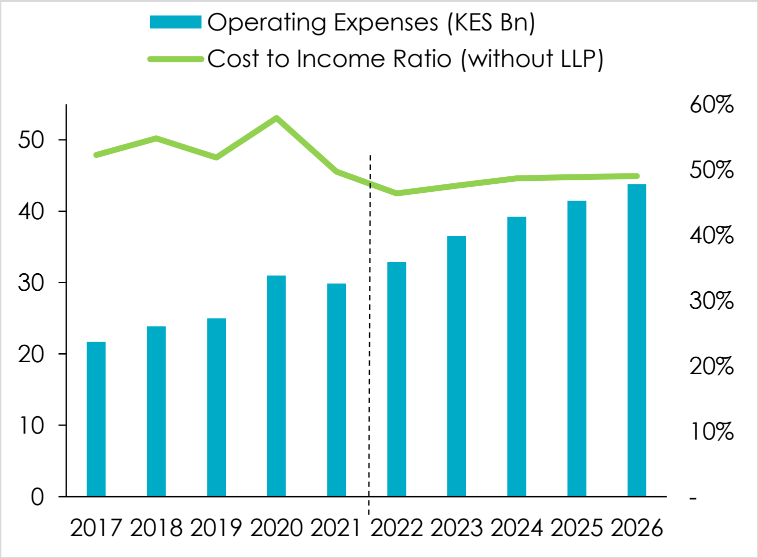
Valuation Methodology	Implied Price	Weighting	Weighted Value
Residual Income	14.35	40%	5.74
DDM	16.55	15%	2.48
P/BV	15.51	40%	6.20
P/E	13.48	5%	0.67
Fair Value		**100%**	**15.10**
Current Price			**12.40**
Upside/(Downside)			21.8%

Source: NCBA IB Research Estimates

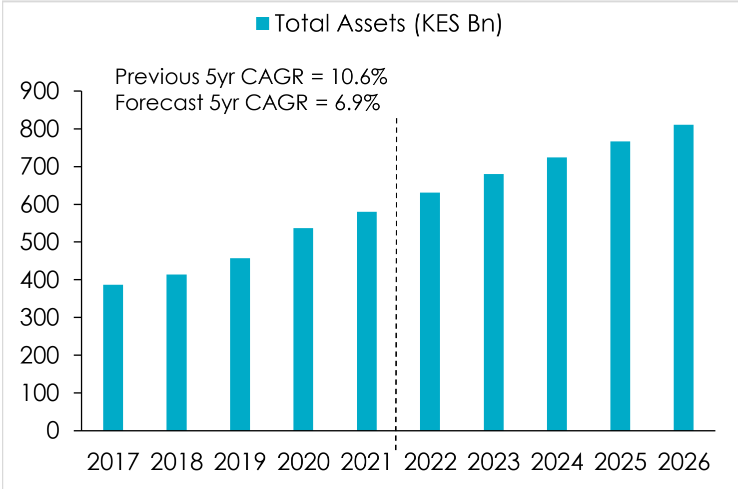
Income Statement Projections – Co-operative Bank

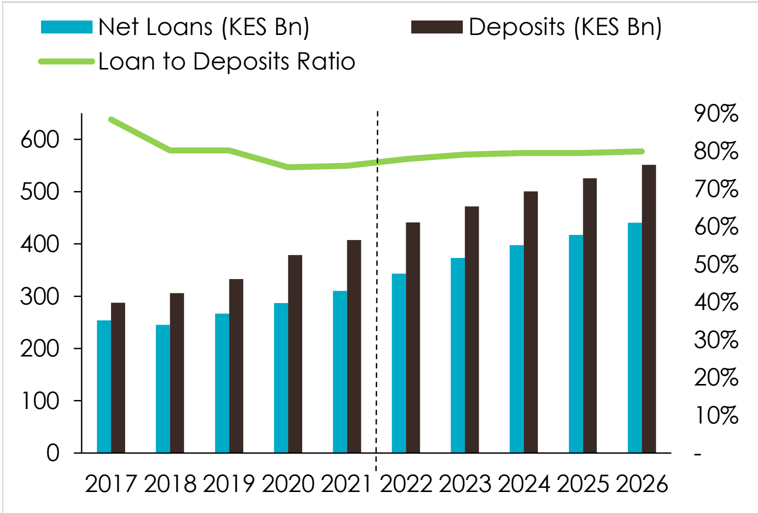


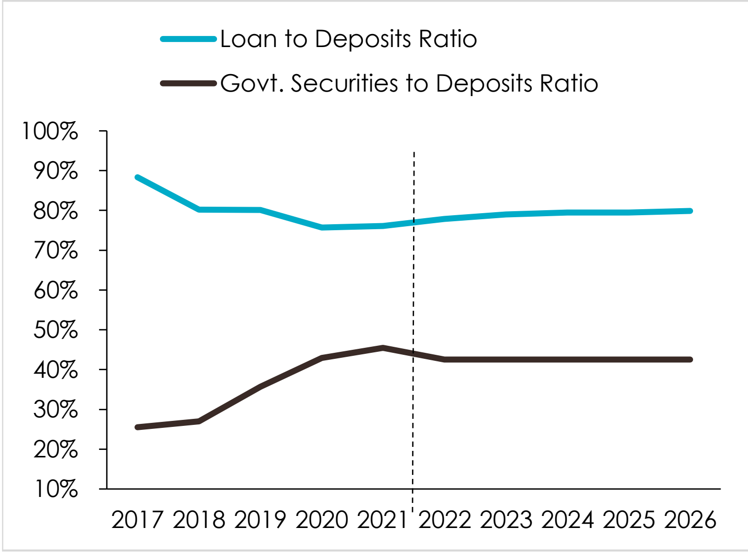




Balance Sheet Projections – Co-operative Bank







STANDARD CHARTERED BANK OF KENYA

We have updated our recommendation to **HOLD** based on a target price of KES 156.39 at par with the current price of KES 157.00 as of 31st January 2023, exclusive of dividend yield.

We expect the bank to register long-term profitability based on its continued focus on channel diversification boosted by its wealth management offerings and rising government bond yields.

At the current market price, the stock is trading within its fair value but presents a value pick for long-term investors owing to its reliable dividend payout.

Share Data	Standard Chartered
Ticker	SCBL KN
RECOMMENDATION	**HOLD**
Current Price (KES)	157.00
Target Price (KES)	156.93
Upside(Excl. Div. Yield)	0.0%
52WK High (KES)	155.25
52WK Low (KES)	115.00
Market Cap (KES Bn)	59.32
Free Float	24.0%
P/B	1.2x
P/E (Annualized)	5.1x
Current Price = as of 31st Jan 2023	

Source: Bloomberg, NSE, NCBA IB Research

Q3'2022 Performance (% = y/y performance)

- **Earnings:** Profit after Tax grew by 37.1% y/y mainly driven by a 66%% growth in FX Trading Income coupled with a 76.8% decline in loan provisions. Overall, EPS improved to KES 22.6 from KES 16.5 in Q3'2021.

- **Efficiency:** The bank's Cost to income ratio excluding provisions improved marginally to 47.4% from 48.0% in Q3'2021 due to the faster operating income growth compared to expenses.
Inclusive of provisions, cost to income ratio dropped to 49.9% from 60.1% in Q3'2021, following the reduced provisions to KES 0.6Bn from KES 2.7Bn.

- **Balance Sheet**: The Bank maintained its cautious stance on lending as loans grew by 3.3% compared to Customer Deposits 10.7% growth. This led to bank having the least Loan to Deposit ratio amongst listed banks of 48%.

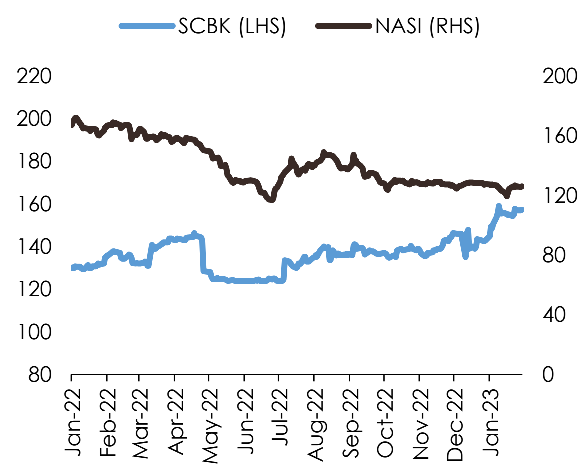
- The slow loan book expansion is a concern as it limits the lender's topline growth potential compared to its peers.

- Notably, Standard Chartered Global Group exited fully from 7 countries in Africa & Middle East region (Angola, Cameroon, Gambia, Zimbabwe, Sierra Lion, Jordan and Lebanon). It also exited the consumer and private banking business in Tanzania and Cote d'Ivoire. The contribution to PBT by these markets was ~1% as of 2021. It retained full operations in Kenya which contributes 10% to the region's Income and 0.7% to the Group.

- **Asset Quality:** Gross NPLs increased by 4.42% y/y to KES 24.03Bn, leading to the NPL ratio increasing to 15.4% from 15.3% in Q3'2021 and notably above the latest industry average of 13.70%. NPL coverage further declined marginally to 82.4% from 82.8% in Q3'21 but remained highest among its peers.

- We are however concerned about the asset quality given that the NPL ratio has been above 13.8% since Q1'2018 – averaging 15.1% in that period.

SCBK vs NASI Performance (LTM)



Source: NSE, NCBA IB Research

Outlook

We expect Standard Chartered Bank to record gradual growth boosted by:

1. **Revenue diversification:** The bank derives more than a third of its revenue from non-funded income mainly driven by its strong wealth management offering coupled by FX trading income.

2. **Improving Government Securities' Yields:** The bank is poised to benefit from the rise in yield curve due to its increased allocation to government securities.

- **Dividend Outlook:** We expect Standard Chartered to issue full year dividends following its strong performance, at an estimated 79.5% dividend payout ratio. SCBK paid out a KES 6.00 interim dividend in Q4'2022.

Valuation and Investments Recommendation – Standard Chartered Bank of Kenya

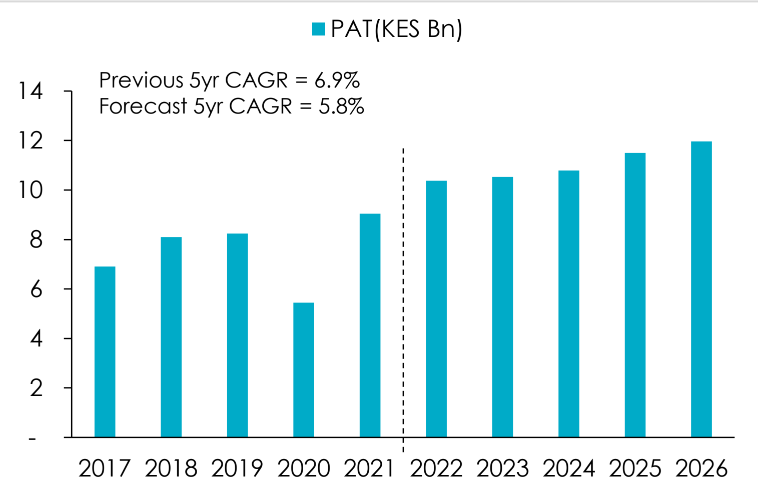
Assumptions

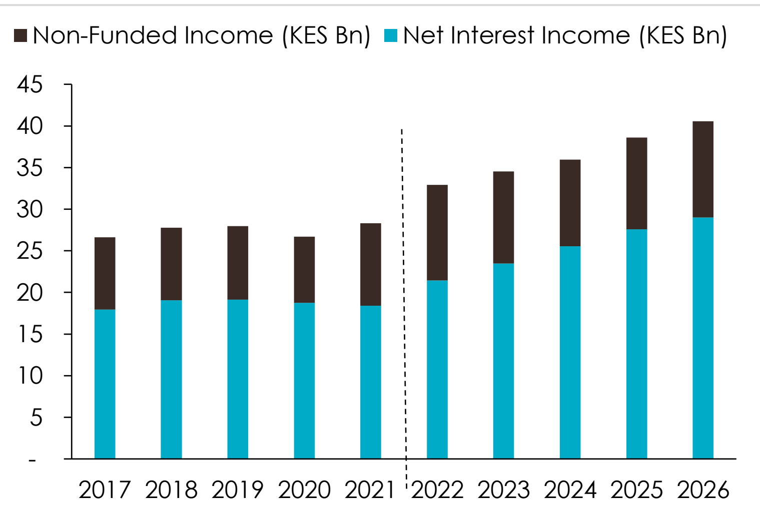
- Risk free rate of 12.45% based on the 10-year Treasury bond historical yields.
- Tax rate of 30%
- Equity risk premium of 5.4%
- Beta of 0.7 on stock's relative volatility on the index.
- Long term growth rate of 5.0% based on average GDP forecast.

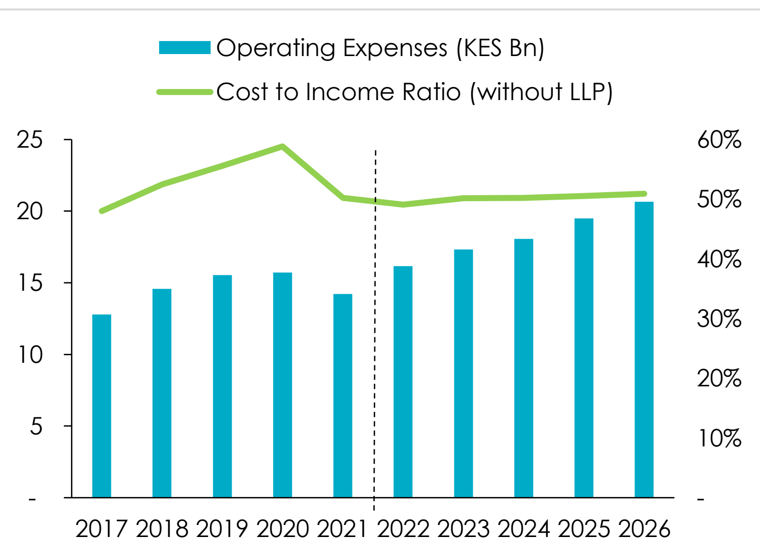
Valuation Methodology	Implied Price	Weighting	Weighted Value
Residual Income	173.73	40%	69.49
DDM	178.43	25%	44.61
P/BV	124.66	30%	37.40
P/E	108.65	5%	5.43
Fair Value		**100%**	**156.93**
Current Price			**157.00**
Upside/(Downside)			0.0%

Source: NCBA IB Research Estimates

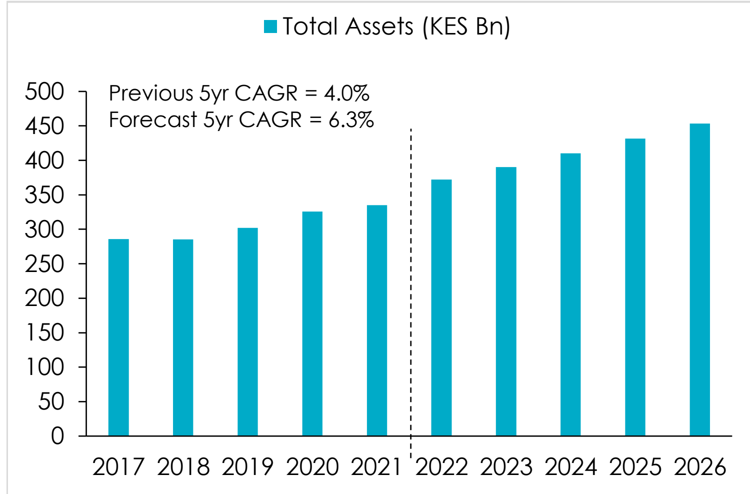
Income Statement Projections – SCBK

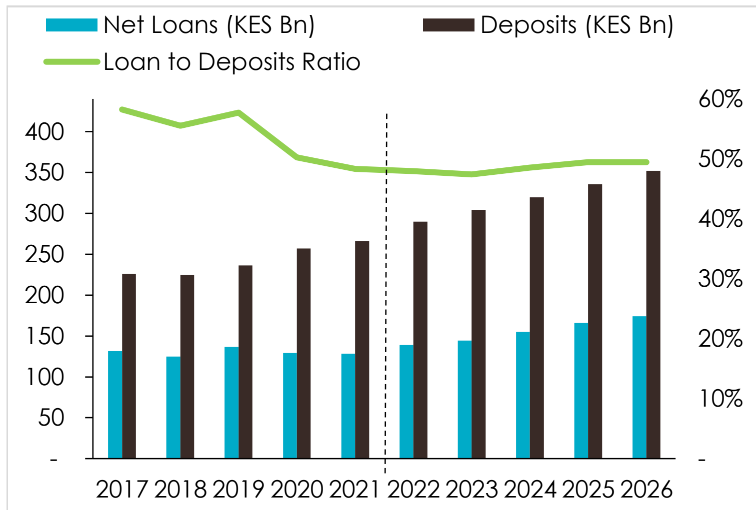


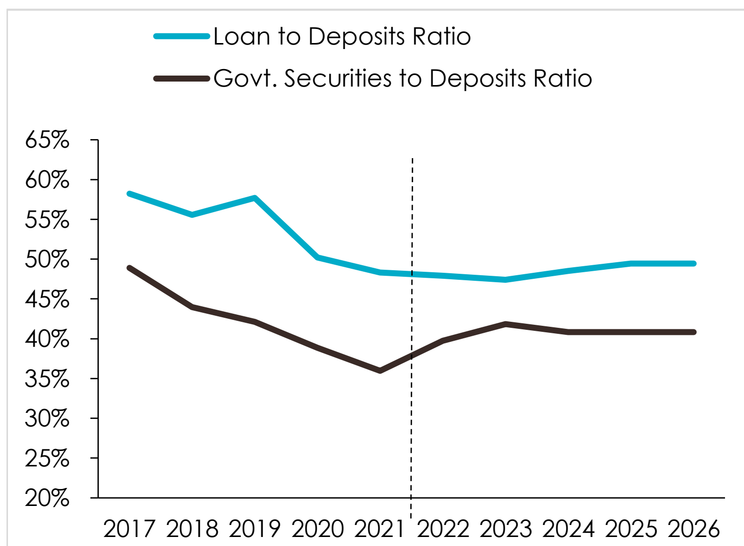




Balance Sheet Projections – SCBK







STANBIC HOLDINGS

We have updated our recommendation to **HOLD** based on a target price of KES 113.03 implying a 2.1% upside, from the current price of KES 110.75 as of 31st January 2023, exclusive of dividend yield.

We expect the bank to register long-term profitability based on its revenue diversification and sustained loan book growth. The lender's asset quality was notably better than industry average.

At the current market price, the stock is trading within its fair value but presents a value pick for long-term investors owing to its reliable dividend payout.

Share Data	Stanbic Holdings
Ticker	SBIC KN
RECOMMENDATION	**HOLD**
Current Price (KES)	110.75
Target Price (KES)	113.03
Upside(Excl. Div. Yield)	2.1%
52WK High (KES)	112.00
52WK Low (KES)	82.00
Market Cap (KES Bn)	43.78
Free Float	25.1%
P/B	0.9x
P/E (Annualized)	4.7x
Current Price = as of 31st Jan 2023	

Source: Bloomberg, NSE, NCBA IB Research

Q3'2022 Performance – Stanbic Kenya (% = y/y performance)

- **Earnings:** Profit After Tax grew by 36.8% y/y mainly driven by a 69.3% growth in FX Trading Income coupled with a 47.0% decline in loan provisions.

- **Efficiency:** The bank's Cost to income ratio excluding provisions dropped to 45.4% from 51.1% in Q3'2021 due to the faster operating income growth compared to expenses.
- Inclusive of provisions, cost to income ratio dropped to 57.9% from 59.8% in Q3'2021.

- **Balance Sheet**: The Bank's loan book grew by 34.1% to KES 236.9Bn boosting overall assets which grew by 25.9%. Government securities on the other hand recorded a 38.3% growth to KES 63.0Bn from KES 45.6Bn in Q3'2021.

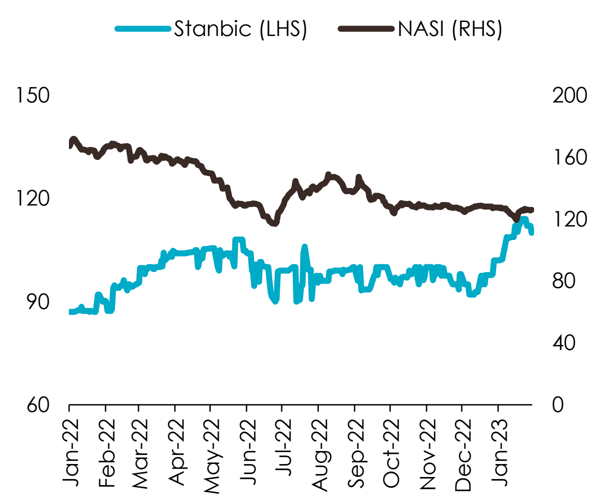
- Customer Deposits increased by 25.6% to KES 267.3Bn taking the loan to deposit ratio to 88.6% from 83.0% in Q3'2021. The bank leveraged more on borrowed funds and bank deposit liabilities to fund its investments.

- **Asset Quality:** Gross NPLs increased by18.0% y/y to KES 25.6Bn, slower than the 34.3% growth in Gross loans leading to the NPL ratio reducing to 10.1% from 11.5% in Q3'2021. This was below the latest industry average of 13.70%.

- NPL coverage increased to 63.4% from 54.9% in Q3'2021 owing to an 88.8% increase in loan loss provisions – a testament to the increased credit risk during the year.

- **Share Acquisition by Parent:** During H1'2022, Stanbic Africa Holdings completed acquisition of further shares in Stanbic Holdings to 74.92% of total shares. This speaks to the expected organic growth we see in the bank driven by aggressive lending.
- The bank also enjoys support from the Group in terms of access to forex and we expect this, together with continued digitization, to support NFI growth.

Stanbic vs NASI Performance (LTM)



Source: NSE, NCBA IB Research

Outlook

We expect Stanbic Holdings to record gradual growth boosted by:

1. **Loan Book Growth:** The bank has sustained an average loan book growth of 16% over the last 5 years excluding 2020. We see this impressive loan book growth enduring and translating into topline growth momentum. With a traditionally high loan to deposit ratio, we envisage for the bank to reap full dividends from the recently approved credit pricing model.
   The lender's asset quality was also notably better than industry average.

2. **High Government Securities' Yields:** The bank is poised to benefit from the rise in yield curve due to its increased allocation to government securities.

3. **Revenue Diversification**: Stanbic has sustained an impressive NFI to operating income contribution of 43%-46% over the last 5 years driven largely by FX trading income. The bank also enjoys support from the Group in terms of access to forex and we expect this, together with continued digitization initiatives to support NFI growth.

- **Dividend Outlook:** We expect Stanbic to issue full year dividends following its strong performance and dividend payment consistency.
- Historically, Stanbic's Dividend Payout ratio average has been 41%. A similar payout ratio in FY'2022 implies a final dividend of KES 9.30 – 9.90 according to our full year estimates. Notably the bank did not issue interim dividends in 2022.

Valuation and Investments Recommendation – Stanbic Holdings

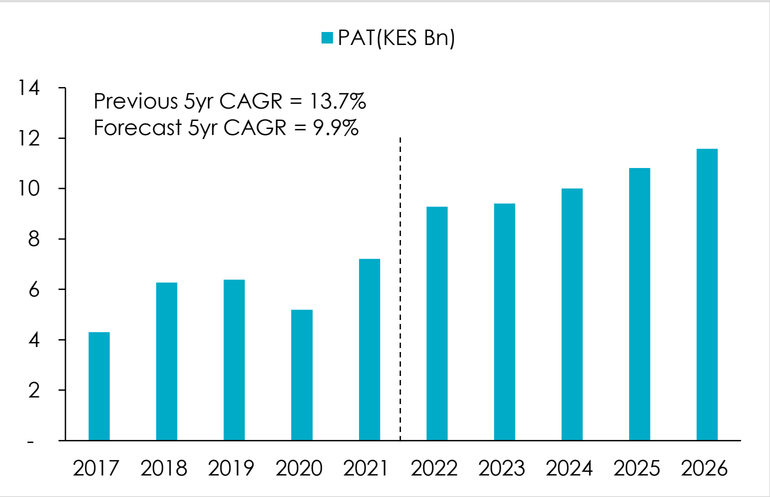
Assumptions

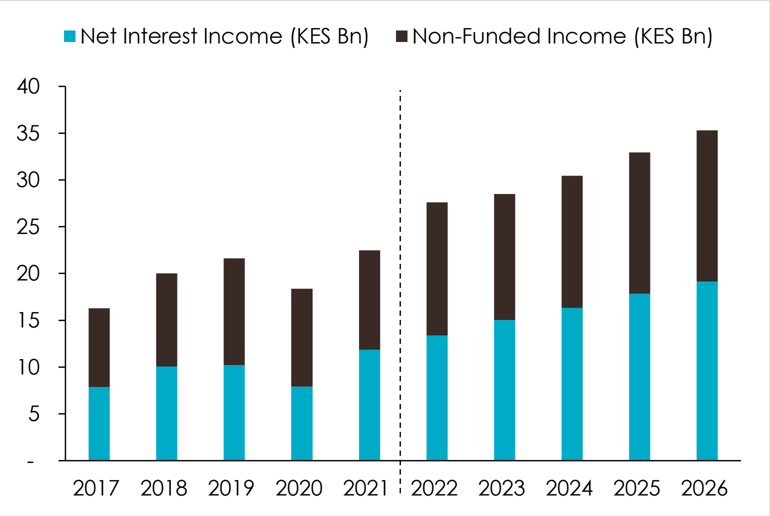
- Risk free rate of 12.45% based on the 10-year Treasury bond historical yields.
- Tax rate of 30%
- Equity risk premium of 5.4%
- Beta of 0.7 on stock's relative volatility on the index.
- Long term growth rate of 5.0% based on average GDP forecast.

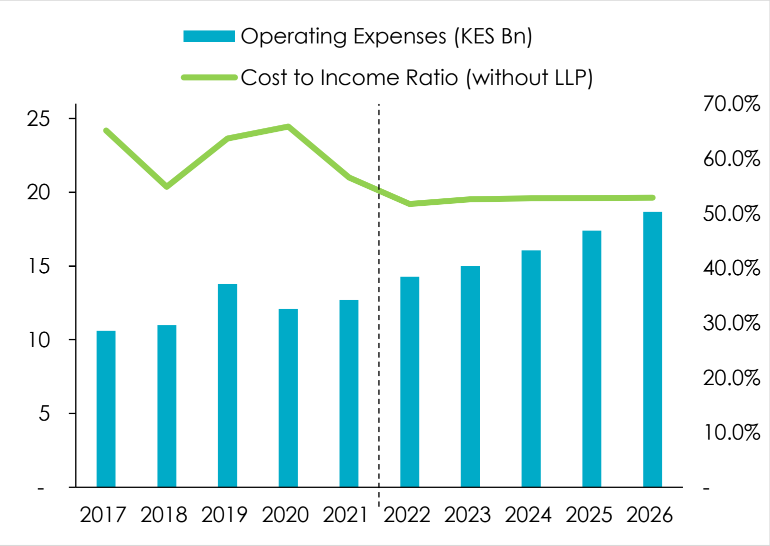
Valuation Methodology	Implied Price	Weighting	Weighted Value
Residual Income	111.95	40%	44.78
DDM	130.64	15%	19.60
P/BV	109.47	40%	43.79
P/E	97.39	5%	4.87
Fair Value		**100%**	**113.03**
Current Price			**110.00**
Upside/(Downside)			2.1%

Source: NCBA IB Research Estimates

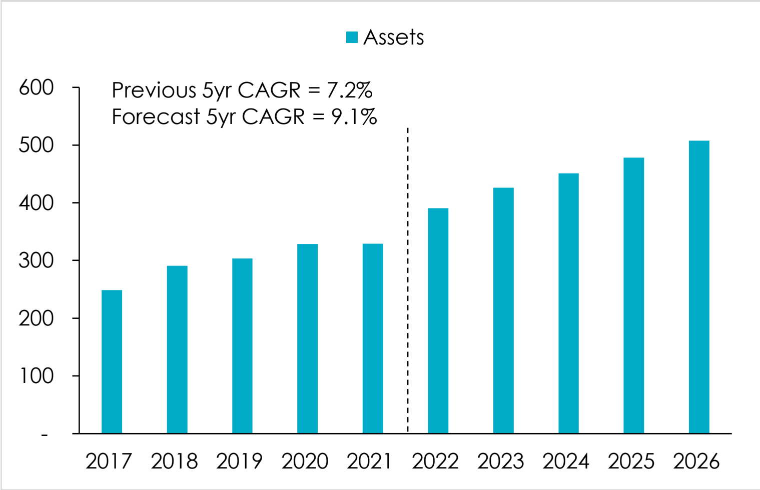
Income Statement Projections – Stanbic

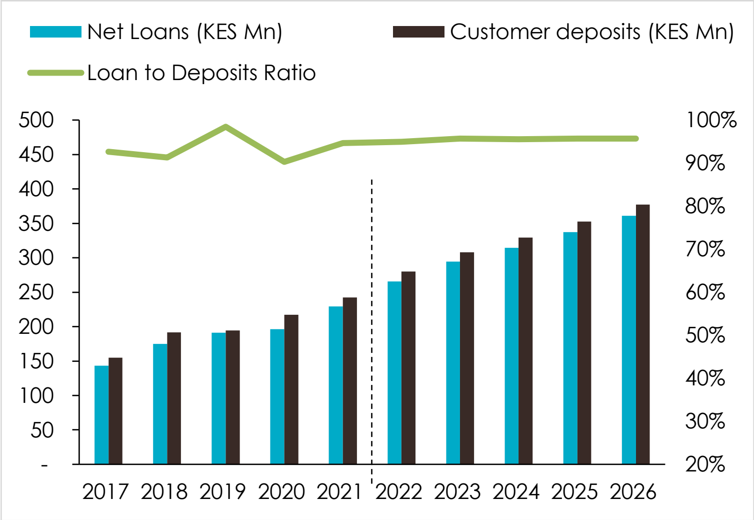


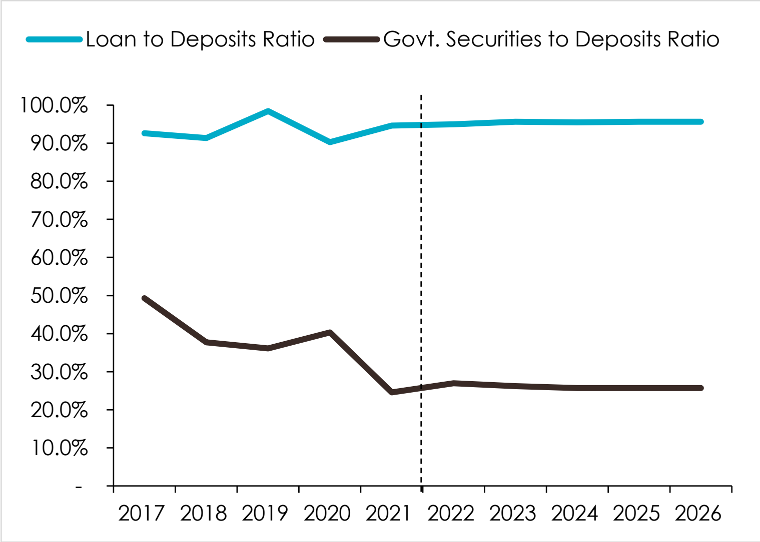




Balance Sheet Projections – Stanbic







I&M HOLDINGS

We maintain our **BUY** recommendation based on a target price of KES 23.40 implying a 37.6% upside, from the current price of KES 17.00 as of 31st January 2023, exclusive of dividend yield.

We expect the bank to register long-term profitability based on its strong asset quality, improving cost efficiency and topline growth as the implementation of the risk-based credit pricing model starts.

At the current market price, the stock is trading below its fair value and presents a value pick for long-term investors.

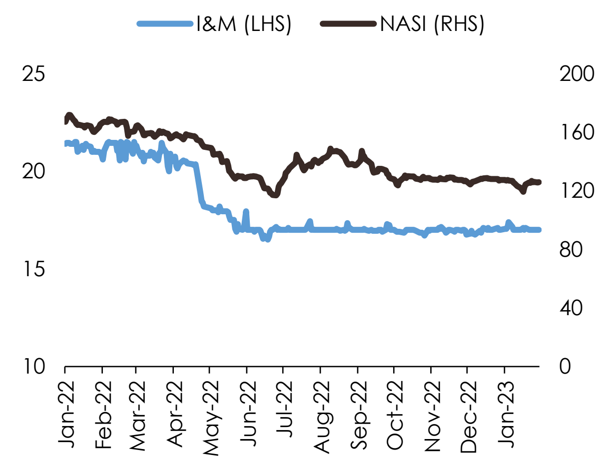
Q3'2022 Performance (% = y/y performance)

- **Earnings:** Profit After Tax grew by 25.0% y/y mainly driven by a 220% growth in FX Trading Income coupled with a 16% topline growth.
- **Efficiency:** The bank's Cost to income ratio excluding provisions improved to 45.3% from 48.1% in Q3'2021 due to the faster FX-boosted operating income growth compared to expenses. Inclusive of provisions, cost to income ratio dropped to 59.7% from 62.1% in Q3'2021, despite a 27.5% increase in loan loss provisions.
- **Balance Sheet**: Total Assets grew by 7.4% driven by an 11.4% loan book expansion.
- **Notably the lender pivoted away from investments in government securities,** as seen through a 9.4% decline in government securities y-o-y.
- Loan to deposit ratio, on the other hand increased to 75.1% from 71.9% as loan book growth outpaced the 6.7% growth in customer deposits.
- **Asset Quality:** I&M's credit management continues to impress, recording the second best NPL Ratio and third highest NPL Coverage rate.
- The NPL ratio improved to 9.5% in Q3'2022 from 10.2% Q3'2021 and significantly below the industry average of 13.7%. This is attributed to slower 4.2% growth in Gross NPLs compared to 11.4% growth in Gross loans.
- NPL Coverage increased to 75.4% from 70.6% driven by 27.5% increase in loan loss provisions in the first three quarters of 2022.

Share Data	I&M Holdings
Ticker	IMH KN
RECOMMENDATION	**BUY**
Current Price (KES)	17.00
Target Price (KES)	23.40
Upside(Excl. Div. Yield)	37.6%
52WK High (KES)	23.00
52WK Low (KES)	16.00
Market Cap (KES Bn)	28.11
Free Float	21.8%
P/B	0.4x
P/E (Annualized)	3.1x
Current Price = as of 31st Jan 2023	

Source: Bloomberg, NSE, NCBA IB Research

I&M vs NASI Performance (LTM)



Source: NSE, NCBA IB Research

Outlook

We expect I&M Holdings to record gradual growth boosted by:

1. **Improving Cost Efficiency:** We expect the bank's cost to income ratio to keep improving primarily due to organic growth in interest income. Relatedly, a high NPL coverage ratio reduces their need to increase provisioning. This should help bolster the bank's profitability and return on equity.

2. **Asset Quality:** The bank's strong asset quality and high coverage ratio bodes well and shifts its focus to lending. Further, this implies better interest repayments which will lead to sustainable topline growth.

- **Dividend Outlook:** We expect I&M Holdings to issue full year dividends following its strong performance in 2022.

Valuation and Investments Recommendation – I&M Holdings

Assumptions

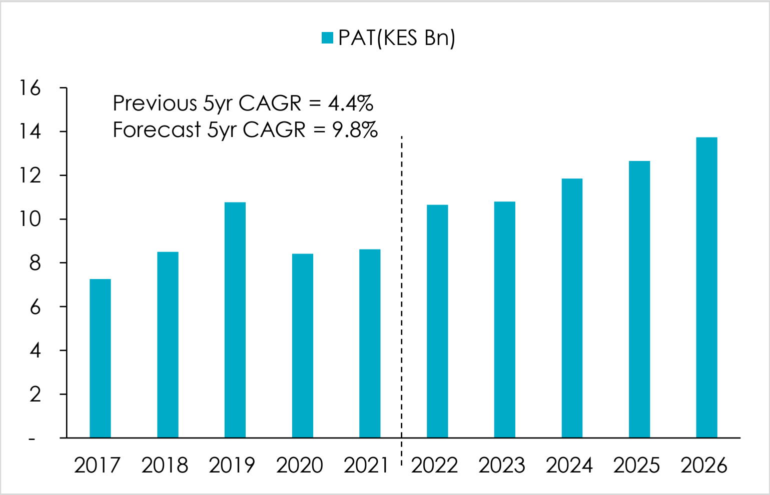
- Risk free rate of 12.45% based on the 10-year Treasury bond historical yields.
- Tax rate of 30%
- Equity risk premium of 5.4%
- Beta of 0.5 on stock's relative volatility on the index.
- Long term growth rate of 5.0% based on average GDP forecast.

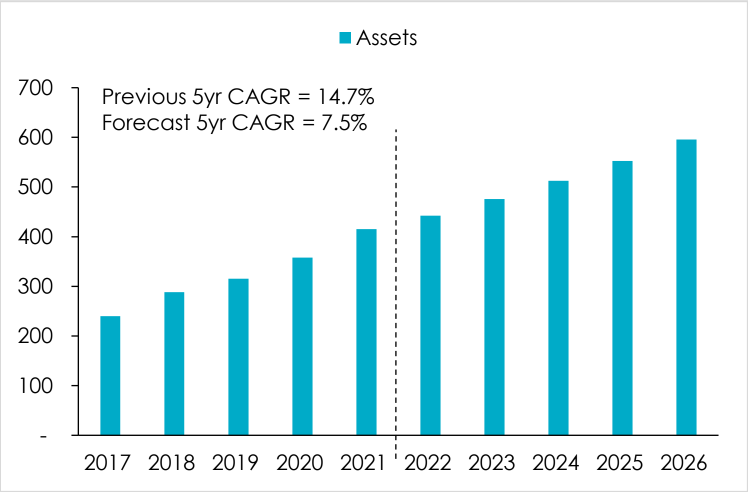
Valuation Methodology	Implied Price	Weighting	Weighted Value
Residual Income	25.40	40%	10.16
DDM	35.95	15%	5.39
P/BV	17.25	40%	6.90
P/E	18.82	5%	0.94
Fair Value		**100%**	**23.40**
Current Price			**17.00**
Upside/(Downside)			37.6%

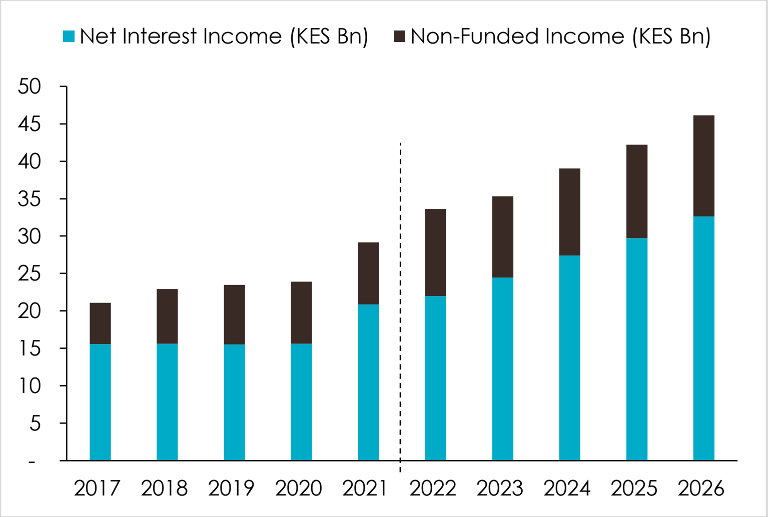
Source: NCBA IB Research Estimates

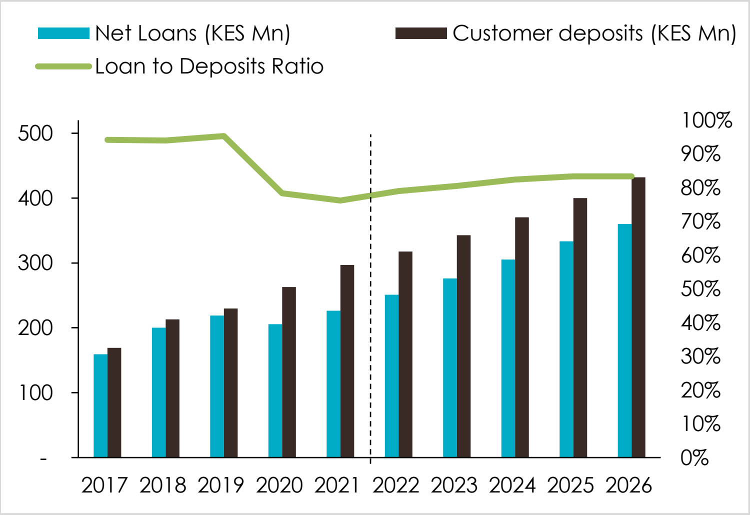
Income Statement Projections – I&M Holdings

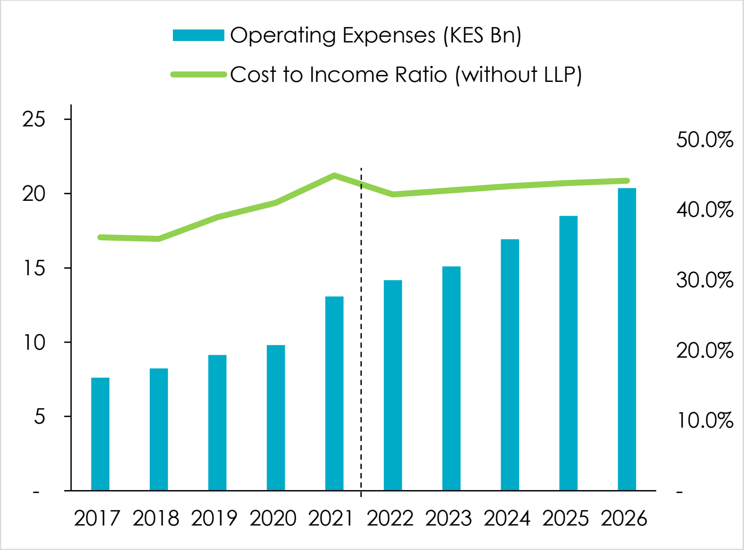
Balance Sheet Projections – I&M Holdings

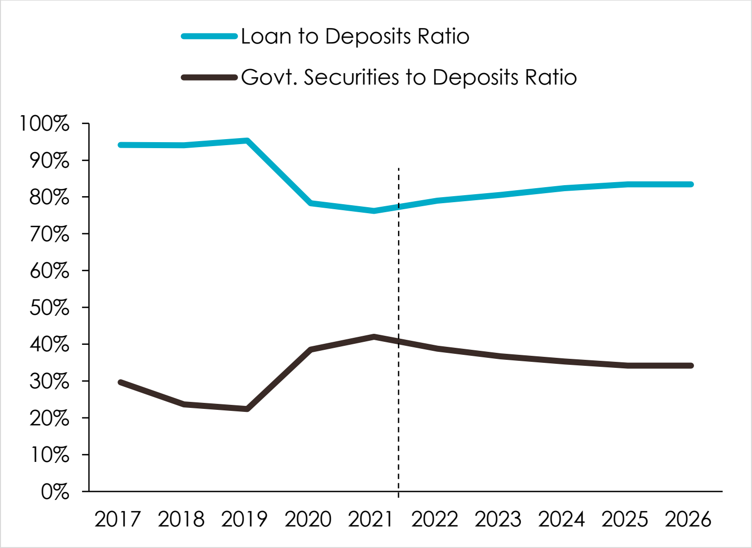












DIAMOND TRUST BANK OF KENYA (DTB-K)

We have updated our recommendation to **BUY** based on a target price of KES 62.53 implying a 25.1% upside, from the current price of KES 50.00 as of 31st January 2023, exclusive of dividend yield.

We expect the bank's performance going forward to be driven by its branch expansion drive and its investment in digital technology. The bank opened 6 branches in 2022 and targets to open 35 – 40 more branches in 2023. The branches are expected to boost the lenders' deposit mobilization drive and loan book expansion.

At the current market price, the stock is trading below its fair value and presents a value pick for long-term investors.

Share Data	Standard Chartered
Ticker	DTK KN
RECOMMENDATION	**BUY**
Current Price (KES)	50.00
Target Price (KES)	62.53
Upside(Excl. Div. Yield)	25.1%
52WK High (KES)	65.50
52WK Low (KES)	44.50
Market Cap (KES Bn)	13.98
Free Float	24.0%
P/B	0.2x
P/E (Annualized)	1.8x
Current Price = as of 31st Jan 2023	

Source: Bloomberg, NSE, NCBA IB Research

Q3'2022 Performance (% = y/y performance)

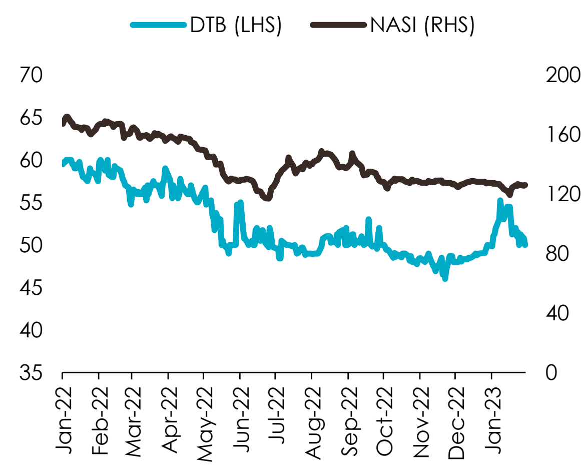
- **Earnings:** Profit After Tax grew by 19.7% y/y driven by growth in both Net Interest Income and Non-Funded Income, both growing by KES 2.1 Bn y/y. Non-funded income performance was boosted an 81%% growth in FX Trading Income.
- **Looking back over the last three years,** DTB has recorded losses in the last quarter of the year mainly due to significant increases in loan loss provisions. Bearing this in mind and the elevated credit risk in 2022, we may witness a similar ramp up in provisions in the FY'2022 results.
- As of Q3'2022, loan loss provisions stood at KES 4.0Bn a 31% increase y/y.

- **Efficiency:** The bank's Cost to income ratio excluding provisions improved marginally to 45.2% from 46.3% in Q3'2021 due to the faster operating income growth compared to expenses.
- We expect the cost to income ratio to worsen in the short run owing to the bank's expansion drive which will lead to increased staff costs and other setup costs before the new branches break even.
- Inclusive of provisions, cost to income ratio remained largely unchanged at 62.1% - the highest amongst its peers.

- **Balance Sheet**: DTB recorded an impressive loan book growth of 18.5% partially attributed to a strong bank deposit liabilities 4.9x growth to KES 37.1Bn from KES 7.6Bn in Q3'2021.
- Deposits grew at a slower rate of 11.1% meaning loan to deposit ratio grew to 67.7% from 63.5% a year earlier.

- **Asset Quality:** Gross NPLs increased 28.1% y/y to KES 33.0Bn, leading to the NPL ratio deteriorating to 12.7% from 11.9% in Q3'2021 but still below the latest industry average of 13.70%.
- NPL coverage remains a key concern with DTB having the lowest rate among its peers - average of 66.1% while DTB's improved but stood at 45.2%. The concern is driven by the challenging business environment which could lead to crystallization of credit risk.

DTB-K vs NASI Performance (LTM)



Source: NSE, NCBA IB Research

Outlook

We expect Diamond Trust Bank (DTB)'s performance going forward to driven by:

1. **Branch Expansion Drive:** The bank opened 6 branches in 2022 in a bid to broaden its reach to micro and small enterprise market segment and plans on opening at least 35 more in 2023 (Total Cost = KES 0.7Bn). The branch expansion initiative is likely to lead to mobilization of more deposits and subsequently loan book and asset size expansion, translating to topline growth.

2. **Digitization Drive:** The bank invested KES 2.4Bn in 2018-2021 and expects to invest KES 3.5Bn in the period 2022-2024, in a bid to boost digital transactions way. As of Q3'2022, digital transactions accounted for 78% in terms of value and 86% in quantum amounts. Success of the initiative will lead to increased NFI revenues as well as improve cost efficiency in the long term.

3. **Strong Regional Subsidiaries Performance**: Regional subsidiaries contribution to PBT increased to 25.8% in Q3'2022 from 21.7% in Q3'2021 (Driven by Tanzania's performance – 12.0% contribution from 7.0% in Q3'2021). Additionally, its contribution to the loan book increased to 28.1% from 25.3% in Q3'2021.

- **Dividend Outlook:** We expect DTB Bank to issue full year dividend with a similar DPS to FY'2021.

Valuation and Investments Recommendation – Diamond Trust Bank Kenya

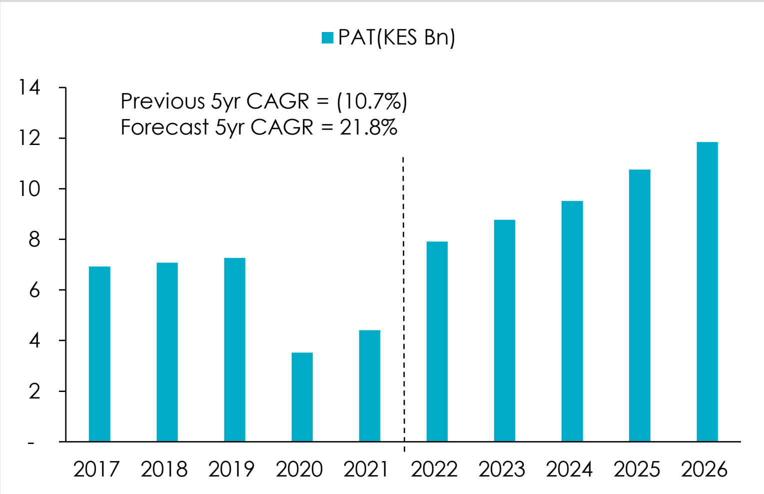
Assumptions

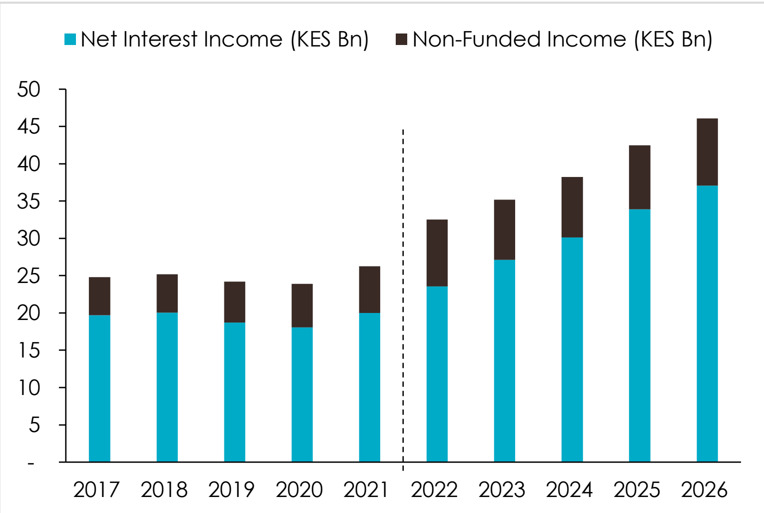
- Risk free rate of 12.45% based on the 10-year Treasury bond historical yields.
- Tax rate of 30%
- Equity risk premium of 5.4%
- Beta of 0.8 on stock's relative volatility on the index.
- Long term growth rate of 5.0% based on average GDP forecast.

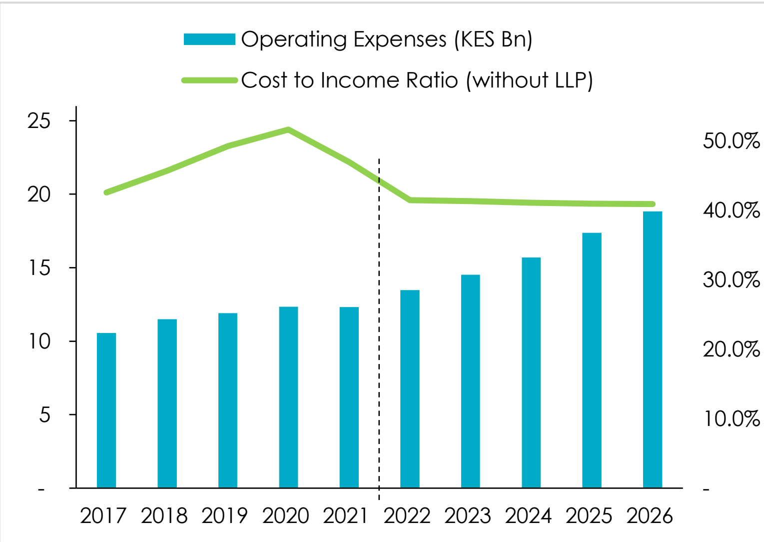
Valuation Methodology	Implied Price	Weighting	Weighted Value
Residual Income	54.06	40%	21.62
DDM	95.83	5%	4.79
P/BV	62.54	40%	25.02
P/E	73.97	15%	11.10
Fair Value		**100%**	**62.53**
Current Price			**50.00**
Upside/(Downside)			25.1%

Source: NCBA IB Research Estimates

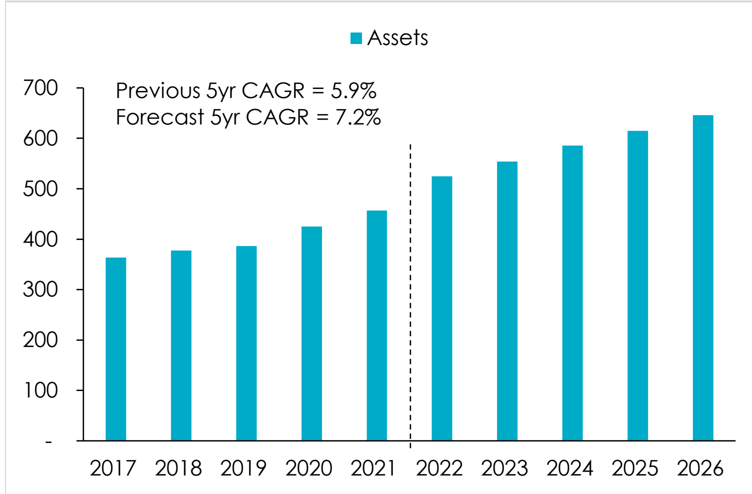
Income Statement Projections – DTB-K

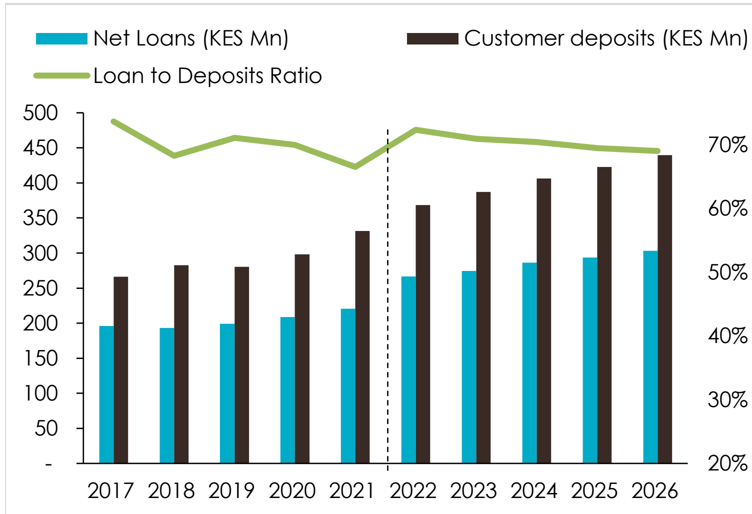


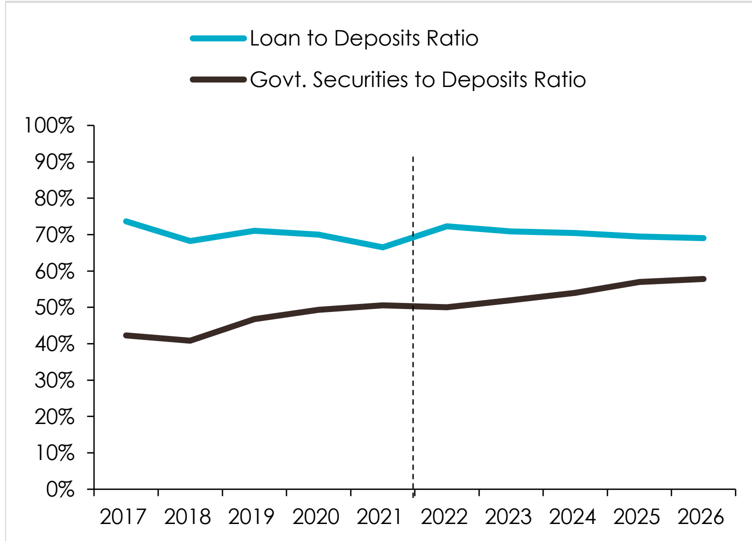




Balance Sheet Projections –DTB-K







About NCBA Investment Bank

NCBA Investment Bank is a subsidiary of NCBA Group. The services offered by the brokerage department include equities trading for listed securities, fixed income trading for both corporate and government bonds, Over the Counter (OTC) equity transactions as well as execution of equities transactions across the East African countries. Additionally, NCBA Investment Bank backs these activities with solid advice from the research team to enable investors meet their return objectives. NCBA Investment Bank deploys simple and convenient client driven technologies, robust risk management, highly competent and experienced staff and has the backing of robust research capabilities to differentiate itself from other players in the market.

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Certification

The following analyst(s) who prepared this research report: Justin N Mwangi and Victoria Mututu hereby certifies(y) that: (i) all of the views and opinions expressed in this research report accurately reflect the research analyst's(s') personal views about the subject investment(s) and companies (y) and (ii) no part of the analyst's(s') compensation was, is or will be directly or indirectly related to the specific recommendations or views expressed by the analyst(s) in this research report.

Rating Definitions

BUY – Total expected 12-month return (incl. dividends) greater than 20%
ACCUMULATE - Total expected 12-month return (incl. dividends) between 10% - 20%
HOLD – Total expected 12-month return (incl. dividends) between 0% -10%
SELL – Total expected 12-month return (incl. dividends) less than 0%

Disclaimer

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