ABSA Bank Kenya Plc – H1’2021

27th August 2021

Below is a summary of the ABSA Bank’s H1’2021 performance:

Balance Sheet	H1'2020	H1'2021	y/y change
Government Securities	133.9	121.3	(9.4%)
Net Loans and Advances	201.9	218.9	8.4%
Total Assets	**391.9**	**398.2**	**1.6%**
Customer Deposits	248.7	263.9	6.1%
Total Liabilities	348.9	346.2	(0.8%)
Shareholder's Funds	**43.0**	**52.0**	**20.9%**

Balance Sheet Ratios	H1'2020	H1'2021	% y/y change
Loan to Deposit Ratio	81.2%	82.9%	1.7%
Return on average equity	9.8%	19.3%	9.5%
Return on average assets	1.1%	2.3%	1.2%

Income Statement	H1'2020	H1'2021	y/y change
Net Interest Income	11.3	12.0	6.1%
Net non-Interest Income	5.5	5.8	6.1%
Total Operating income	**16.8**	**17.8**	**6.1%**
Loan Loss provision	(5.4)	(1.9)	(63.9%)
Total Operating expenses	(13.6)	(9.9)	(27.0%)
Profit before tax	**3.3**	**7.9**	143.8%
Profit after tax	**0.6**	**5.6**	846.0%
Core EPS	**0.1**	**1.0**	**846.0%**

Income statement ratios	H1'2020	H1'2021	% Points change
Yield from interest-earning assets	9.7%	9.2%	(0.5%)
Cost of funding	3.1%	2.8%	(0.3%)
Net Interest Margin	7.3%	7.0%	(0.3%)
Cost to Income	80.6%	55.5%	(25.1%)
Cost to Assets	2.1%	2.0%	(0.1%)
Net Interest Income as % of operating income	67.2%	67.2%	0.0%
Non-Funded Income as a % of operating income	32.8%	32.8%	0.0%)

Capital Adequacy Ratios	H1'2020	H1'2021
Core Capital/Total Liabilities	16.2%	17.7%
Minimum Statutory ratio	8.0%	8.0%
Excess	**8.2%**	**9.7%**
Core Capital/Total Risk Weighted Assets	13.8%	14.7%
Minimum Statutory ratio	10.5%	10.5%
Excess	**3.3%**	**4.2%**
Total Capital/Total Risk Weighted Assets	16.5%	17.3%
Minimum Statutory ratio	14.5%	14.5%
Excess	**2.0%**	**2.8%**

Liquidity Ratio	39.1%	38.1%
Minimum Statutory ratio	20.0%	20.0%
Excess	**19.1%**	**18.1%**
Adjusted Core Capital/Total Liabilities	**16.3%**	**17.8%**
Adjusted Core Capital/Total RWA	**13.9%**	**14.8%**
Adjusted Total Capital/Total RWA	**16.7%**	**17.4%**

Key Highlights in H1’2021

- ABSA Bank Kenya Plc disclosed that over 90.0% of the Kshs 59.0 bn of the restructured loans were performing as normal as at H1’2021. The number of restructured loan accounts totaled 59,000, with personal loans and credit cards accounting for 60.0% and 37.0% of the restructured loans. The loan book restructuring was in line with the CBK’s emergency measures for COVID-19 related loan restructuring which ran from 18th March 2020 to 2nd March 2021 in order to provide relief to borrowers during the pandemic.

Income Statement

- Core earnings per share increased by 846.0% to Kshs 1.0, from Kshs 0.1 in H1’2020, not in line with our expectation of an increase to Kshs 0.3. The performance was driven by a 6.1% increase in Net Interest Income to Kshs 12.0 bn, from Kshs 11.3 bn recorded in H1’2020. The variance in core earnings per share growth against our expectations was largely due a 27.0 % decline in Total operating expenses to Kshs 9.9 bn, against our expectations of a 7.7% increase to Kshs 14.6 bn,
- Total operating income rose by 6.1% to Kshs 17.8 bn, from Kshs 16.8 bn in H1’2020 supported by a matching increase of 6.1% in Net Interest Income (NII) and Non-Funded Income (NFI) to Kshs 12.0 bn and Kshs 5.8 bn, from Kshs 11.3 bn and Kshs 5.5 bn, respectively, in H1’2020,
- Interest income declined by 0.8% to Kshs 15.2 bn, from Kshs 15.3 bn in H1’2020, attributable to the 5.1% decline in interest income from government securities to Kshs 4.1 bn, from Kshs 4.3 bn in H1’2020 coupled with a 35.9% decline in interest income from placements to Kshs 80.2 mn, from Kshs 125.0 mn in H1’2020. The decline was however mitigated by a 1.3% increase in Interest income from Loans and Advances to Kshs 11.0 bn from Kshs 10.9 bn in H1’2020. The Yield on Interest-Earning Assets declined to 9.2%, from 9.7% in H1’2020, attributable to the faster 6.3% y/y increase in average interest earning assets to Kshs 342.2 bn, from Kshs 321.9 bn in H1’2020 that outpaced the 0.5% growth in trailing interest income. Trailing Interest Income refers to the performance of the interest income for the past 12 consecutive months,
- Interest expenses declined by 20.4% to Kshs 3.2 bn, from Kshs 4.0 bn in H1’2020, following a 74.7% decline in interest expense on placement liabilities to Kshs 0.2 bn, from Kshs 0.7 bn in H1’2020, coupled with a 7.4% decline in interest expense on customer deposits to Kshs 2.9 bn, from Kshs 3.2 bn in H1’2020. Cost of funds declined marginally by 0.3% points to 2.8%, from 3.1% in H1’2020, owing to a 6.7% growth in average interest bearing liabilities, against a 6.1% decline in trailing interest expense. Trailing interest expense refers to the performance of the interest expense for the past 12 consecutive months. Net Interest Margin (NIM) declined to 7.0%, from 7.3% in H1’2020, owing to a 6.3 % growth in average interest earning assets, which was faster than the 2.6% growth in Trailing Net Interest Income (NII),
- Non-Funded Income (NFI) increased by 6.1% to Kshs 5.8 bn, from Kshs 5.5 bn in H1’2020 mainly driven by a 26.1% increase in fees and commissions from loans to Kshs 0.9 bn, from Kshs 0.7 bn in H1’2020. The increase was also supported by a 5.6% increase in income from other fees and commissions to Kshs 2.2 bn, from Kshs 2.1 bn in H1’2020 and a 0.5% increase in Foreign Exchange trading income to Kshs 2.07 bn from

Kshs 2.06 bn in H1’2020. Notably, total fees and commission income increased by 10.7% to Kshs 3.1 bn, from Kshs 2.8 bn in H1’2020, attributable to the reversal of the waiver on fees on mobile banking transactions seen at the start of the year. The revenue mix remained at 67:33 as recorded in H1’2020, funded to non-funded income, owing to a matching 6.1% growth in both NII and NFI,

- Total operating expenses declined by 27.0% to Kshs 9.9 bn, from Kshs 13.6 bn in H1’2020, largely driven by a 63.9% decline in Loan Loss Provisions (LLP) to Kshs 1.9 bn in H1’2021, from Kshs 5.4 bn in H1’2020. However, the LLP increased 39.3% q/q from Kshs 1.3 bn in Q1’2021. The decline in operating expenses was also supported by a 12.0% decline in staff costs to Kshs 4.4 bn in H1’2021, from Kshs 5.0 bn in H1’2020,
- Cost to Income Ratio (CIR) improved to 55.5%, from 80.6% in H1’2020, owing to 27.0% decline in total operating expenses to Kshs 9.9 bn, from Kshs 13.6 bn in H1’2020 coupled with the 6.1% growth in total operating income to Kshs 17.8 bn, from Kshs 16.8 bn in H1’2020. Similarly, without LLP, the cost to income ratio improved to 44.6%, from 48.6% in H1’2020, an indication of improved efficiency, and,
- Profit before tax and exceptional items increased by 143.8% to Kshs 7.9 bn from Kshs 3.3 bn recorded in H1’2020. Profit after exceptional items before tax increased by 398.9% to Kshs 7.9 bn in H1’2021, from Kshs 1.6 bn in H1’2020. Profit after tax and exceptional items increased by 846.0% to Kshs 5.6 bn in H1’2021, from Kshs 0.6 bn in H1’2020, with the effective tax rate declined by 0.9% points to 29.9%, from 30.8% in H1’2020.

Balance Sheet

- The balance sheet recorded an expansion as total assets rose by 1.6% to Kshs 398.2 bn, from Kshs 391.9 bn in H1’2020. This growth was largely driven by an 8.4% growth in the loan book to Kshs 218.9 bn, from Kshs 201.9 bn in H1’2020, coupled with a 54.5% increase in Placements due from other banking institutions to Kshs 5.1 bn, from Kshs 3.3 bn in H1’2020. The growth was however weighed down by a 9.4% decline in government securities to Kshs 121.3 bn, from Kshs 133.9 bn in H1’2020,
- Total liabilities declined by 0.8% to Kshs 346.2 bn, from Kshs 348.9 bn in H1’2020, driven by a 19.6% decline in other liabilities to Kshs 75.6 bn from Kshs 94.0 bn in H1’2020. On the other hand, customer deposits increased by 6.1% to Kshs 263.9 bn, from Kshs 248.7 bn in H1’2020. Deposits per branch increased by 4.9% to Kshs 3.1 bn, from Kshs 3.0 bn in H1’2020, with the number of branches having increased to 85 in H1’2021, from 84 in H1’2020,
- The faster 8.4% growth in loans, which outpaced the 6.1% growth in deposits led to an increase in the loan to deposit ratio to 82.9%, from 81.2% recorded in H1’2020,
- Gross Non-Performing Loans (NPLs) increased by 7.8% to Kshs 18.3 bn from Kshs 17.0 recorded in H1’2020. The NPL ratio improved to 7.9% in H1’2021, from 8.0% in H1’2020, owing to the faster 9.0% growth in gross loans (after adding back interest suspense), which outpaced the 7.8% growth in gross NPLs. General Loan Loss Provisions rose by 26.4% to Kshs 10.6 bn, from Kshs 8.4 bn in H1’2020. The NPL coverage increased to 70.9% in H1’2021, from 63.6% in H1’2020, owing to the 26.4% increase in General Loan Loss Provisions, which outpaced the 7.8% growth in gross non-performing loans.
- Shareholders’ funds increased by 20.9% to Kshs 52.0 bn in H1’2021, from Kshs 43.0 bn in H1’2020, driven by a 23.6% increase in retained earnings to Kshs 48.1 bn, from Kshs 38.9 bn in H1’2020,
- ABSA Bank Kenya is currently sufficiently capitalized with a core capital to risk-weighted assets ratio of 14.7%, 4.2% points above the 10.5% statutory requirement. In addition, the total capital to risk-weighted assets ratio was 17.3%, exceeding the 14.5% statutory requirement by 2.8% points. Adjusting for IFRS 9, the core capital to risk weighted assets stood at 14.8%, while total capital to risk-weighted assets came in at 17.4%, and,
- The bank currently has a Return on Average Assets (ROaA) of 2.3%, and a Return on Average Equity (ROaE) of 19.3%.

Key Take-Outs:

1. The Cost to Income Ratio (CIR) improved to 55.5%, from 80.6% in H1’2020, attributable to the 63.9% decline in Loan Loss Provisions (LLP) to Kshs 1.9 bn in H1’2021, from Kshs 5.5 bn in H1’2020. However, the LLP increased 39.3% q/q from Kshs 1.3 bn in Q1’2021 indicating that the bank expects the loan repayments to continue being affected negatively by the COVID-19 pandemic even though that bank has strengthened its credit assessment methodologies, improving borrower credit assessment, and,
2. The bank’s asset quality improved, with the NPL ratio declining marginally to 7.9% in H1’2021, from 8.0% in H1’2020, owing to the faster 9.0% growth in gross loans (after adding back interest suspense), which outpaced the 7.8% growth in gross NPLs. Notably, the lender’s current NPL ratio of 7.9% is below the banking sector average of 14.0%, as of June 2021, mainly due to the improving business environment couple with an improved credit assessment metrics.

Going forward, we expect the bank’s growth to be driven by:

I. Increased Channel diversification, which is likely to help the bank to continue improving its operational efficiency. The benefits of this are already being felt with 87.0% of all transactions happening outside the branch as at H1’2021, as well as “Timiza” which is a digital banking App, that is already recording accelerated growth, and consequently higher Non-Interest Revenue. This coupled with the expansion of its agent-banking network and product offerings such as Bancassurance and fixed income trading will see the bank expand its top-line revenue going forward.

Valuation Summary

- We are of the view that ABSA Bank Kenya is a “**Accumulate**” with a target price of Kshs 11.3, representing an upside of 12.8%, from the current price of Kshs 11.0 as of 27th August 2021,
- ABSA Bank Kenya is currently trading at a P/TBV of 1.2x and a P/E of 6.5x vs an industry average of 1.0x and 8.2x, respectively.