ABSA Bank Kenya Plc – Q1'2022

27th May 2022

Below is a summary of ABSA Bank's Q1'2022 performance;

Balance Sheet Items	Q1'2021	Q1'2022	y/y change
Government Securities	126.7	136.7	7.9%
Net Loans and Advances	218.3	242.7	11.2%
Total Assets	**384.1**	**438.5**	**14.2%**
Customer Deposits	257.1	269.5	4.8%
Total Liabilities	**335.4**	**379.3**	13.1%
Shareholder's Funds	**48.7**	**59.2**	**21.6%**

Balance sheet ratios	Q1'2021	Q1'2022	% point change
Loan to Deposit Ratio	84.9%	90.0%	5.1%
Return on average equity	10.2%	21.2%	11.0%
Return on average assets	1.2%	2.8%	1.6%

Income Statement Items	Q1'2021	Q1'2022	y/y change
Net Interest Income	6.0	6.9	15.4%
Net non-Interest Income	2.9	3.0	5.8%
Total Operating income	**8.8**	**9.9**	**12.3%**
Loan Loss provision	(1.4)	(1.2)	(15.3%)
Total Operating expenses	**(5.4)**	**(5.6)**	3.6%
Profit before tax	**3.4**	**4.3**	26.1%
Profit after tax	**2.4**	**3.0**	22.1%
Core EPS	**0.4**	**0.5**	**22.1%**

Income statement ratios	Q1'2021	Q1'2022	% point change
Yield from interest-earning assets	9.3%	9.1%	(0.2%)
Cost of funding	3.0%	2.6%	(0.4%)
Net Interest Margin	7.0%	7.1%	0.1%
Cost to Income	61.3%	56.6%	(4.7%)
Cost to Assets	1.0%	1.0%	-
Net Interest Income as % of operating income	67.7%	69.5%	1.8%
Non-Funded Income as a % of operating income	32.3%	30.5%	(1.8%)

Capital Adequacy Ratios	Q1'2021	Q1'2022
Core Capital/Total Liabilities	17.5%	18.4%
Minimum Statutory ratio	8.0%	8.0%
Excess	**9.5%**	**10.4%**
Core Capital/Total Risk Weighted Assets	14.4%	14.5%
Minimum Statutory ratio	10.5%	10.5%
Excess	**3.9%**	**4.0%**
Total Capital/Total Risk Weighted Assets	17.0%	17.0%
Minimum Statutory ratio	14.5%	14.5%
Excess	**2.5%**	**2.5%**
Liquidity Ratio	38.3%	36.7%
Minimum Statutory ratio	20.0%	20.0%
Excess	**18.3%**	**16.7%**
Adjusted Core Capital/Total Liabilities	**17.7%**	**18.5%**

Adjusted Core Capital/Total RWA	**14.5%**	**14.6%**
Adjusted Total Capital/Total RWA	**17.1%**	**17.1%**

Income Statement

- Core earnings per share increased by 22.1% to Kshs 0.5 in Q1’2022, from Kshs 0.4 in Q1’2021, in line with our expectations of an 18.7% increase to Kshs 0.5. The EPS growth was driven by Total operating income, which increased by 12.3% to Kshs 9.9 bn, from Kshs 8.8 bn recorded in Q1’2021, while total operating expenses, on the other hand, recorded a 3.6% increase to Kshs 5.6 bn, from Kshs 5.4 bn recorded in Q1’2021. Notably, the improved earnings were supported by a 15.3% decline in Loan Loss Provision (LLP) to Kshs 1.2 bn in Q1’2022, from Kshs 1.4 bn in Q1’2021 on the back of an improved business operating environment,
- Total operating income rose by 12.3% to Kshs 9.9 bn, from Kshs 8.8 bn recorded in Q1’2021 driven by a 15.4% increase in Net Interest Income (NII) to Kshs 6.9 bn, from Kshs 6.3 bn in Q1’2021, coupled with a 5.8% gain in Non-Funded Income (NFI) to Kshs 3.0 bn, from Kshs 2.9 bn in Q1’2021,
- Interest income grew by 15.6% to Kshs 8.8 bn in Q1’2022, from Kshs 7.6 bn in Q1’2021, mainly driven by a 14.1% increase in interest income from loans and advances to Kshs 6.3 bn, from Kshs 5.5 bn in Q1’2021, coupled with a 8.3% increase in interest income from Government securities to Kshs 2.2 bn, from Kshs 2.0 bn in Q1’2021. The Yield on Interest-Earning Assets (YIEA) however declined to 9.1%, from 9.3% recorded in Q1’2021, attributable to the faster 6.0% growth in average interest earning assets which outpaced the 5.7% growth in trailing interest income. Trailing Interest Income refers to the performance of the interest income for the past 12 consecutive months,
- Interest expenses increased by 16.2% to Kshs 1.9 bn, from Kshs 1.6 bn in Q1’2021, following a 55.7% increase in interest expenses from deposits and placements with banking institutions to Kshs 0.3 bn, from Kshs 0.2 bn in Q1’2021, coupled with a 12.3% increase in other interest expenses from customer deposits to Kshs 1.6 bn, from Kshs 1.4 bn in Q1’2021. However, other interest expenses declined by 18.1% by Kshs 27.9 mn from Kshs 33.9 mn in Q1’2021. The bank was able to mobilize cheaper deposits with the Cost of funds (COF) declining by 0.4% points to 2.6%, from 3.0% in Q1’2021, owing to the 8.6% decline in the trailing interest expense coupled with a 6.0% growth in average interest-bearing liabilities. Trailing interest expense refers to the performance of the interest expense for the past 12 consecutive months. Net Interest Margin (NIM) increased to 7.1% from 7.0% in Q1’2021, attributable to the faster 10.4% increase in trailing net interest income, which outpaced the 6.0% growth in interest earning assets,
- Non-Funded Income (NFI) increased by 5.8% to Kshs 3.0 bn, from Kshs 2.9 bn in Q1’2021, mainly driven by a 31.3% increase in Foreign Exchange trading income to Kshs 1.2 bn, from Kshs 0.9 bn in Q1’2021, coupled with a 12.9% increase in other income to Kshs 327.7 mn, from Kshs 290.4 mn in Q1’2021. The increase was however weighed down by the 29.8% increase in income from fees and advances on loans and advances to Kshs 0.3 bn from Kshs 0.4 bn in Q1’2021. Other fees and commissions income remained relatively unchanged at Kshs 1.2 bn as was recorded in Q1’2021. Notably, the bank’s total fees and commissions declined by 10.0% to Kshs 1.5 bn, from Kshs 1.6 bn in Q1’2021. The revenue mix shifted to 70:30, funded to non-funded income, from 68:32, funded to non-funded income recorded in Q1’2021, attributable to the faster 15.6% increase in NII which outpaced the 5.8% increase in NFI,
- Total operating expenses increased by 3.6% to Kshs 5.6 bn in Q1’2022, from Kshs 5.0 bn in Q1’2021, mainly attributable to a 26.4% increase in other operating expenses to Kshs 2.2 bn from Kshs 1.7 bn in Q1’2021. On the other hand, Loan Loss Provisions (LLPs) declined by 15.3% to Kshs 1.2 bn, from Kshs 1.4 bn in Q1’2021, while staff costs declined by 2.0% to Kshs 2.26 bn from Kshs 2.30 bn in Q1’2021. The reduced provisioning level was due to declining credit risk on the back of increased business activities in Q1’2022 driven by the gradual economic recovery,

- Cost to Income Ratio (CIR) improved to 56.6%, from 61.3% in Q1’2021, owing to the 12.3% growth in total operating income, which outpaced the 3.6% increase in total operating expenses. Without LLP, the cost to income ratio improved as well to 44.6%, from 45.5% in Q1’2021, an indication of improved efficiency, and,
- Profit before tax and exceptional items increased by 26.1% to Kshs 4.3 bn in Q1’2022, from Kshs 3.4 bn in Q1’2021. Profit after tax increased by 22.1% to Kshs 3.0 bn in Q1’2022, from Kshs 2.4 bn in Q1’2021 with the effective tax rate increasing to 30.0%, from 29.0% in Q1’2021.

Balance Sheet

- The balance sheet recorded an expansion as total assets grew by 14.2% to Kshs 438.5 bn in Q1’2022, from Kshs 384.1 bn in Q1’2021. This growth was largely driven by an 11.2% growth in the loan book to Kshs 242.7 bn, from Kshs 218.3 bn in Q1’2021 coupled with a 7.9% increase in investments in government and other securities to Kshs 136.7 bn, from Kshs 126.7 bn in Q1’2021. Placements in other banks increased significantly by 129.9% to Kshs 6.5 bn, from Kshs 2.8 bn recorded in Q1’2021,
- Total liabilities rose by 13.1% to Kshs 379.3 bn, from Kshs 335.4 bn in Q1’2021, driven by a 4.8% increase in customer deposits to Kshs 269.5 bn, from Kshs 257.1 bn in Q1’2021. Placements by other banking institutions increased by 28.5% increase to Kshs 4.3 bn, from Kshs 6.0 bn in Q1’2021. Deposits per branch rose by 4.8% to Kshs 3.2 bn, from Kshs 3.1 bn in Q1’2021 with the number of branches remaining unchanged at 84,
- The faster 11.2% growth in loans compared to the 4.8% increase in customer deposits led to an increase in the loans to deposit ratio to 90.0%, from 84.9% recorded in Q1’2021. Key to note, this is the highest loan to deposit ratio the bank has recorded since FY’2017, when the loan to deposit ratio came in at 90.5%,
- Gross Non-Performing Loans (NPLs) increased by 12.9% to Kshs 19.5 bn in Q1’2022, from Kshs 17.3 bn recorded in Q1’2021. Consequently, the NPL ratio rose to 7.6%, from 7.5% recorded in Q1’2021. The asset quality deterioration is attributable to the faster 12.9% growth in Gross Non-Performing Loans (NPLs), compared to the relatively slower 11.5% increase in gross loans. The sectors that contributed to this deterioration are the Hospitality and Tourism sector which recorded a slow recovery in 2021 due to the emergence of new strains which hampered economic growth. The NPL coverage increased to 76.2% in Q1’2022, from 73.4% in Q1’2021, owing to the faster 21.9% increase in General Loan Loss Provisions, which outpaced the 12.9% growth in Gross Non-Performing Loans (NPLs),
- Shareholders’ funds increased by 21.6% to Kshs 59.2 bn, from Kshs 48.7 bn recorded in Q1’2021. The increase can be attributed to the 11.7% increase in Retained earnings to Kshs 50.2 bn, from Kshs 44.9 bn in Q1’2021,
- ABSA Bank Kenya is currently sufficiently capitalized with a core capital to risk-weighted assets ratio of 14.5%, 4.0% points above the 10.5% statutory requirement. In addition, the total capital to risk-weighted assets ratio was 17.0%, exceeding the 14.5% statutory requirement by 2.5% points. Adjusting for IFRS 9, the core capital to risk-weighted assets stood at 14.6% while total capital to risk-weighted assets came in at 17.1%, and,
- The bank currently has a Return on Average Assets (ROaA) of 2.8%, and a Return on Average Equity (ROaE) of 21.2%.

Key Take-Outs:

1. Total operating income rose by 12.3% to Kshs 9.9 bn, from Kshs 8.8 bn recorded in Q1’2021 driven by a 15.4% increase in Net Interest Income (NII) to Kshs 6.9 bn, from Kshs 6.3 bn in Q1’2021, coupled with a 5.8% gain in Non-Funded Income (NFI) to Kshs 3.0 bn, from Kshs 2.9 bn in Q1’2021,
2. Cost to Income Ratio (CIR) improved to 56.6%, from 61.3% in Q1’2021, owing to the 12.3% growth in total operating income which outpaced the 3.6% decline in total operating expenses. The growth in total

operating income is largely attributable to the 15.4% increase in NII, coupled with the 5.8% increase in NFI. Without LLP, the cost to income ratio improved as well to 44.6%, from 45.5% in Q1’2021, an indication of improved efficiency levels,

3. The bank’s asset quality deteriorated, with the NPL ratio increasing to 7.6% in Q1’2022, from 7.5% in Q1’2021, owing to the faster 12.9% growth in Gross Non-Performing Loans (NPLs), compared to the relatively slower 11.5% increase in gross loans. The sectors that contributed to this deterioration are the Hospitality and Tourism sector which recorded a slow recovery in 2021 due to the emergence of new strains which hampered economic growth. However, the NPL ratio declined on a q/q basis to 7.6% from 7.9%, attributable to improved business environment in Q1’2022 driven by the gradual economic recovery. The NPL coverage increased to 76.2% in Q1’2022, from 73.4% in Q1’2021, owing to the faster 21.9% increase in General Loan Loss Provisions, which outpaced the 12.9% growth in Gross Non-Performing Loans (NPLs), and,
4. Profit after tax increased by 22.1% to Kshs 3.0 bn in Q1’2022, from Kshs 2.4 bn in Q1’2021 mainly attributable to the completion of the separation and transition process of Barclays Africa Group to Absa Group which saw the bank not incurring exceptional expenses during the year compared to the Kshs 3.2 bn incurred in Q1’2021.

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

I. Increased diversification, which is expected to reduce the bank’s reliance on interest income as well as increasing the bottom line. The bank has continued to grow its product offerings to include business lines such as to Banc-assurance, Investment banking advisory and Asset Management which will continue growing the Non-Funded Income (NFI). The bank has also invested in its digital offerings especially after the onset of the COVID-19 pandemic. The benefits of this are already being felt with 90.0% of all transactions happening outside the branch as at Q1’2022, coupled with uptake of “Timiza” which is a digital banking App, that is already recording accelerated growth, and consequently higher Non-Interest income. This coupled with the expansion of its agent-banking network and product offerings such as 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 an “***BUY***” with a target price of Kshs 13.1, representing an upside of 30.6%, from the current price of Kshs 10.1 as of 27th May 2022, inclusive of a dividend yield of 10.9%,
- ABSA Bank Kenya is currently trading at a P/TBV of 0.9x and a P/E of 4.8x vs an industry average of 0.8x and 4.8x, respectively.