ABSA Bank Kenya – FY'2023

18th March, 2024

Below is a summary of ABSA Bank Kenya's FY'2023 performance:

Balance Sheet	FY'2022 (Kshs bn)	FY'2023 (Kshs bn)	y/y change
Net Loans and Advances	283.6	335.7	18.4%
Kenya Government Securities	90.6	74.7	(17.5%)
Total Assets	**477.2**	**519.8**	**8.9%**
Customer Deposits	303.8	362.7	19.4%
Deposits Per Branch	3.7	4.4	20.9%
Total Liabilities	**413.6**	**450.6**	**8.9%**
Shareholders' Funds	**63.6**	**69.2**	**8.8%**

Key Ratios	FY'2022	FY'2023	% points change
Loan to Deposit ratio	93.4%	92.5%	(0.9%)
Government Securities to Deposits ratio	29.8%	20.6%	(9.2%)
Return on Average Equity	24.3%	24.6%	0.3%
Return on Average Assets	3.2%	3.3%	0.1%
Dividend Yield	11.0%	11.1%	1.1%
Dividend Payout ratio	50.3%	51.4%	1.1%

Income Statement	FY'2022 (Kshs bn)	FY'2023 (Kshs bn)	y/y change
Net interest Income	32.3	40.0	23.9%
Net non-interest income	13.7	14.5	6.3%
Total Operating income	**46.0**	**54.6**	**18.7%**
Loan loss provision	(6.5)	(9.2)	42.7%
Total Operating expenses	**(25.1)**	**(30.9)**	**22.9%**
Profit before tax	**20.8**	**23.7**	13.6%
Profit after tax	**14.6**	**16.4**	**12.2%**
Core EPS	**2.7**	**3.0**	**12.2%**

Income Statement Ratios	FY'2022	FY'2023	% points change
Yield from interest-earning assets	10.3%	12.7%	2.4%
Cost of funding	2.9%	4.1%	1.2%
Net Interest Margin	8.2%	9.4%	1.2%
Net Interest Income as % of operating income	70.3%	73.4%	3.1%
Non-Funded Income as a % of operating income	29.7%	26.6%	(3.1%)
Cost to Income Ratio	54.7%	56.6%	1.9%
Cost to Income without LLP	40.6%	39.7%	(0.9%)
Cost to Assets	3.9%	4.2%	0.3%

Capital Adequacy Ratios	FY'2022	FY'2023	% points change
Core Capital/Total Liabilities	18.4%	16.7%	(1.7%)
Minimum Statutory ratio	8.0%	8.0%	
Excess	**10.4%**	**8.7%**	**(1.7%)**
Core Capital/Total Risk Weighted Assets	14.6%	13.6%	(1.0%)
Minimum Statutory ratio	10.5%	10.5%	
Excess	**4.1%**	**3.1%**	**(1.0%)**
Total Capital/Total Risk Weighted Assets	18.6%	18.1%	(0.5%)
Minimum Statutory ratio	14.5%	14.5%	
Excess	**4.1%**	**3.6%**	**(0.5%)**
Liquidity Ratio	33.6%	31.1%	(2.5%)
Minimum Statutory ratio	20.0%	20.0%	
Excess	**13.6%**	**11.1%**	**(2.5%)**

Income Statement

- Core earnings per share increased by 12.2% to Kshs 3.0, from Kshs 2.7 in FY'2022, driven by the 18.7% growth in total operating income to Kshs 54.6 bn, from Kshs 46.0 bn in FY'2022. However the performance was weighed down by the 22.9% growth in total operating expenses to Kshs 30.9 bn from Kshs 25.1 bn in FY'2022,
- The 18.7% growth in total operating income was mainly driven by a 23.9% growth in Net Interest Income (NII) to Kshs 40.0 bn from Kshs 32.3 bn in FY'2022, coupled with a 6.3% growth in Non-Interest Income (NFI) to Kshs 14.5 bn, from Kshs 13.7 bn in FY'2022,
- Interest income grew by 32.8% to Kshs 54.3 bn from Kshs 40.9 bn in FY'2022, mainly driven by a 44.2% growth in interest income from loans and advances to Kshs 44.3 bn from Kshs 30.7 bn in FY'2022, coupled with a 10.8% increase in interest income from deposits and placements to Kshs 0.8 bn, from Kshs 0.7 bn in FY'2022. As such, the Yield on Interest-Earning Assets (YIEA) increased to 12.7% from 10.3% recorded in FY'2022, mainly attributable to the faster 32.8% growth in trailing interest income compared to a 7.9% increase in average interest-earning assets to Kshs 427.3 bn, from Kshs 395.9 bn in FY'2022,
- Interest expenses increased by 66.5% to Kshs 14.2 bn from Kshs 8.5 bn in FY'2022, mainly driven by a 70.3% increase in interest expense on customer deposits to Kshs 11.9 bn from Kshs 7.0 bn in FY'2022, coupled with a 50.5% increase in interest expense from other interest expenses to Kshs 0.2 bn in FY'2023 from Kshs 0.1 bn recorded in FY'2022. Consequently, Cost of funds (COF) increased by 1.2% points to 4.1% from 2.9% recorded in FY'2022, owing to the 66.5% increase in Trailing interest expense to Kshs 14.2 bn from Kshs 8.5 bn recorded in FY'2022, compared to a 17.8% increase in average interest-bearing liabilities to Kshs 347.9 bn from Kshs 295.3 bn in FY'2022. Trailing interest expense refers to the performance of the interest expense for the past 12 consecutive months. Net Interest Margin (NIM) increased by 1.2% points to 9.4% from 8.2% in FY'2022, attributable to a 23.9% increase in trailing net interest income to Kshs 40.0 bn from Kshs 32.3 bn recorded in FY'2022 which outpaced the 7.9% growth in average interest-earning assets,
- Non-Funded Income (NFI) increased by 6.3% to Kshs 14.5 bn from Kshs 13.7 bn in FY'2022, mainly driven by a 20.6% increase in other fees and commissions to Kshs 5.8 bn from Kshs 4.8 bn in FY'2022, coupled with a 11.6% increase in fees and commissions to Kshs 1.5 bn from Kshs 1.4 bn in FY'2022. The growth in NFI was however weighed down by a 2.0% decrease in foreign exchange income to 6.5 bn from 6.6 bn in FY'2022 indicating a decrease in the bank's foreign exchange margins. Total fees and commissions increased 18.6% to Kshs 7.3 bn, from Kshs 6.2 bn in FY'2022 . The revenue mix shifted to 73:27 from 70:30 for the funded to Non-funded income owing to the 23.9% growth in funded income which outpaced the 6.3% growth in NFI,
- Total operating expenses increased by 22.9% to Kshs 30.9 bn from Kshs 25.1 bn in FY'2022, driven by a 42.7% increase in loan loss provisions to Kshs 9.2 bn from Kshs 6.5 bn recorded in FY'2022 reflecting the bank's continued active management of the credit portfolio, coupled with an 11.8% increase in staff costs to Kshs 11.7 bn from Kshs 10.5 bn in FY'2022. The increase in provisioning is partly attributable to rising credit risk as a result deteriorated economic environment as evidenced by the 2023 Purchasing Managers Index (PMI) averaging 48.1, down from an average of 49.2 in 2022,
- Cost to Income Ratio (CIR) increased to 56.6% from 54.7% in FY'2022, owing to the 22.9% increase in total operating expenses, which outpaced the 18.7% increase in total operating income. Notably, CIR without LLP decreased by 0.9% points to 39.7% from 40.6% recorded in FY'2022, and,
- Profit before tax increased by 13.6% to Kshs 23.7 bn from Kshs 20.8 bn in FY'2022, with the effective tax rate increasing to 30.9% in FY'2023 from 30.0% in FY'2022. As such, profit after tax increased by 12.2% to Kshs 16.4 bn in FY'2023, from Kshs 14.6 bn in FY'2022.

Balance Sheet

- The balance sheet recorded an expansion as total assets grew by 8.9% to Kshs 519.8 bn, from Kshs 477.2 bn in FY'2022, driven by an 18.4% expansion of the loan book to Kshs 335.7 bn, from Kshs 283.6 bn in FY'2022, coupled with a 42.3% increase in other assets to Kshs 17.6 bn, from Kshs 12.4bn in FY'2022, which outpaced the 17.5% decline in investment securities to Kshs 74.7 bn, from Kshs 90.6 bn in FY'2022,
- Total liabilities rose by 8.9% to Kshs 450.6 bn from Kshs 413.6 bn in FY'2022, driven by a 19.4% growth in customer deposits to Kshs 362.7 bn, from Kshs 303.4 bn in FY'2022, coupled with a 29.6% increase in placements to Kshs 11.7 bn, from Kshs 9.0 bn in FY'2022,
- The faster 19.4% growth in customer deposits as compared to the 18.4% growth in loans led to a slight decrease in the loan to deposits ratio to 92.5%, from 93.4% in FY'2022,
- The bank's Asset Quality declined, with Gross NPL ratio increasing to 9.9% in FY'2023 from 7.5% in FY'2022, attributable to 57.0% increase in Gross non-performing loans to Kshs 35.4 bn, from Kshs 22.5 bn in FY'2022, compared to the 19.0% increase in gross loans to Kshs 358.9 bn, from Kshs 301.7 bn recorded in FY'2022,
- General Provisions (LLP) increased by 30.2% to Kshs 17.4 bn in FY'2023 from Kshs 13.3 bn in FY'2022. The NPL coverage decreased to 65.6% in FY'2023, from 80.5% in FY'2022, attributable to the slower 30.2% increase in provisions coupled with a 21.6% increase in interest in suspense, compared to the 57.0% increase in Gross non-performing loans,
- Shareholders' funds increased by 8.8% to Kshs 69.2 bn in FY'2023, from Kshs 63.6 bn in FY'2022, supported by a 13.7% increase in retained earnings to Kshs 63.6 bn, from Kshs 56.0 bn in FY'2022,
- ABSA Bank Kenya Plc remains capitalized with a core capital to risk-weighted assets ratio of 13.6%, 3.1% points above the statutory requirement of 10.5%. In addition, the total capital to risk-weighted assets ratio came in at 18.1%, exceeding the statutory requirement of 14.5% by 3.6% points, and,
- The bank currently has a Return on Average Assets (ROaA) of 3.3%, and a Return on Average Equity (ROaE) of 24.6%.

Key Take-Outs:

1. **Strong earnings growth -** Core earnings per share increased by 12.2% to Kshs 3.0, from Kshs 2.7 in FY'2022, driven by the 18.7% growth in total operating income to Kshs 54.6 bn, from Kshs 46.0 bn in FY'2022
2. **Declined asset quality –** The bank's Gross NPL ratio increased to 9.9% in FY'2023 from 7.5% in FY'2022, attributable to a 57.0% increase in Gross non-performing loans to Kshs 35.4 bn, from Kshs 22.5 bn in FY'2022, compared to the 19.0% increase in gross loans to Kshs 358.9 bn, from Kshs 301.7 bn recorded in FY'2022,
3. **Improved Lending –** The bank's loan book increased by 18.4% to Kshs 335.7 bn, from Kshs 283.6 bn in FY'2022, compared to the 17.5% decline in government securities to Kshs 74.7 bn, from Kshs 90.6 bn in FY'2022, emphasizing the bank's approach to boosting lending via digital transformation, concurrently with the effective management of its non-performing loan portfolio, and,
4. **Increased dividends –** Dividends paid increased by 14.8% to Kshs 1.55 in FY'2023, from Kshs 1.35 in FY'2022 translating to a dividend yield of 11.1% and a dividend payout ratio of 51.4% in 2023 compared to a dividend yield of 11.0% and a dividend payout ratio of 50.3% in 2022.

Going forward, the factors that would drive the bank's growth would be:

- **Digital transformation and Improved Branding** - The lender has capitalized on digital innovation for service delivery, expanding their digital distribution resulting in a 40.0% increase in digital loan disbursments as well as a 68.0% increase in consumer business in Timiza Insurance, which has been a key factor in its financial performance. Additionally, 98.0% of the banks' transactions are now processed on alternate channels with the lender experiencing a 25.0% increase in digitally active clients. The bank also launched a new brand promise in February 2024, 'Your Story Matters' to ensure that Absa's entire suite of services and offerings lives up to this crucial pivot towards a more human-centred, empathetic banking service ethos across the continent, coupled with the 94.0% brand awareness achieved in 2023.

Valuation Summary

- We are of the view that ABSA Bank Kenya is a "buy" with a target price of Kshs 17.2 representing an upside of 33.6%, from the current price of 14.0 as of 22nd March 2024, inclusive of a dividend yield of 11.1%.
- ABSA Bank Kenya is currently trading at a P/TBV of 1.1x and a P/E of 4.6x vs an industry average of 0.8x and 4.0x respectively.