NCBA Group PLC– FY’2023

27th March, 2024

Below is a summary of NCBA Group FY’2023 performance:

Balance Sheet	FY'2022 (Kshs bn)	FY'2023 (Kshs bn)	y/y change
Net Loans and Advances	278.9	337.0	20.8%
Kenya Government Securities	205.4	203.4	(1.0%)
Total Assets	**619.7**	**734.6**	18.6%
Customer Deposits	502.7	579.4	15.3%
Deposits Per Branch	5.1	5.6	9.7%
Total Liabilities	537.2	638.0	18.7%
Shareholders' Funds	**82.4**	**96.7**	**17.3%**

Key Ratios	FY'2022	FY'2023	% point change
Loan to Deposit Ratio	55.5%	58.2%	2.7%
Government Securities to Deposit ratio	40.9%	35.1%	(5.7%)
Return on average equity	17.2%	24.0%	6.8%
Return on average assets	2.3%	3.2%	0.9%
Dividend Payout Ratio	50.8%	36.5%	(14.3%)
Dividend Yield	13.0%	10.8%	(2.2%)

Income Statement	FY'2022 (Kshs bn)	FY'2023 (Kshs bn)	y/y change
Net interest Income	30.7	34.6	12.8%
Net non-interest income	30.3	29.1	(3.9%)
Total Operating income	**60.9**	**63.7**	**4.5%**
Loan loss provision	13.1	9.2	(29.9%)
Total Operating expenses	**37.9**	**38.2**	**0.8%**
Profit before tax	22.5	25.5	13.3%
Profit after tax	**13.8**	**21.5**	**55.7%**
Core EPS	**8.4**	**13.0**	**55.7%**

Income Statement Ratios	FY'2022	FY'2023	y/y change
Yield from interest-earning assets	10.1%	11.1%	1.0%
Cost of funding	4.3%	5.5%	1.2%
Net Interest Spread	5.7%	5.5%	(0.2%)
Net Interest Margin	5.9%	5.9%	(0.0%)
Net Interest Income as % of operating income	50.3%	54.3%	4.0%
Non-Funded Income as a % of operating income	49.7%	45.7%	(4.0%)
Cost to Income Ratio	62.2%	60.0%	(2.2%)
Cost to Income Ratio without LLP	40.8%	45.7%	4.9%

Capital Adequacy Ratios	FY'2022	FY'2023	% points change
Core Capital/Total Liabilities	16.3%	16.3%	0.0%
Minimum Statutory ratio	8.0%	8.0%	0.0%
Excess	**8.3%**	**8.3%**	**0.0%**
Core Capital/Total Risk Weighted Assets	18.4%	18.0%	(0.4%)
Minimum Statutory ratio	10.5%	10.5%	0.0%
Excess	**7.9%**	**7.5%**	**(0.4%)**
Total Capital/Total Risk Weighted Assets	18.4%	18.0%	(0.4%)
Minimum Statutory ratio	14.5%	14.5%	0.0%
Excess	**3.9%**	**3.5%**	**(0.4%)**
Liquidity Ratio	53.2%	55.1%	1.9%
Minimum Statutory ratio	20.0%	20.0%	0.0%

Excess	**33.2%**	**35.1%**	**1.9%**

Income Statement

- Core earnings per share grew by 55.7% to Kshs 13.0, from Kshs 8.4 in FY'2022, driven by the 4.5% growth in total operating income to Kshs 63.7 bn, from Kshs 60.9 bn in FY'2022. However, the performance was weighed down by a 0.8% growth in total operating expenses to Kshs 38.2 bn from Kshs 37.9 bn in FY'2022,
- The 28.8% growth in total operating income was driven by a 12.8% growth in Net Interest Income (NII) to Kshs 34.6 bn from Kshs 30.7 bn in FY'2022, which outpaced the 3.9% decline in Non Interest Income (NFI) to Kshs 29.1 bn, from Kshs 30.3 bn in FY'2022,
- Interest income grew by 24.5% to Kshs 65.2 bn from Kshs 52.4 bn in FY'2022, mainly driven by a 35.6% growth in interest income from loans and advances to Kshs 36.4 bn from Kshs 26.8 bn in FY'2022, coupled with a 9.7% increase in interest income from government securities to Kshs 27.2 bn, from Kshs 24.8 bn in FY'2022. As such, the Yield on Interest-Earning Assets (YIEA) increased to 11.1% from 10.1% recorded in FY'2022, mainly attributable to the faster 24.5% growth in interest income compared to a 13.0% increase in average interest earning assets to Kshs 588.5 bn, from Kshs 520.7 bn in FY'2022,
- Interest expenses rose by 41.0% to Kshs 30.6 bn from Kshs 21.7 bn in FY'2022, mainly driven by a 36.9% increase in interest expense on customer deposits to Kshs 28.4 bn from Kshs 20.8 bn in FY'2022, coupled with a 123.9% increase in interest expense from other deposits and placements to Kshs 1.5 bn in FY'2023 from Kshs 0.7 bn recorded in FY'2022. Consequently, Cost of funds (COF) increased by 1.2% points to 5.5% from 4.3% recorded in FY'2022, owing to a faster 41.0% increase in Trailing interest expense to Kshs 30.6 bn from Kshs 21.7 bn recorded in FY'2022, compared to a 10.2% increase in average interest bearing liabilities to Kshs 553.1 bn from Kshs 501.8 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) remained relatively unchanged from the 5.9% recorded in FY'2022, attributable to a 13.0% increase in average interest earning assets, which muted the 12.8% increase in trailing net interest income to Kshs 34.6 bn from Kshs 30.7 bn recorded in FY'2022,
- Non-Funded Income (NFI) decreased by 3.9% to Kshs 29.1 bn from Kshs 30.3 bn in FY'2022, mainly driven by a 33.0% decrease in income from foreign exchange trading to Kshs 8.4 bn , from Kshs 12.5 bn in FY'2022, indicating decreased foreign exchange margins, which outpaced the 6.0% increase in income from fees and commissions from loans to Kshs 11.9 bn, from 11.3 bn in FY'2022, coupled with a 37.8% increase in income from other fees and commissions to Kshs 5.5 bn, from Kshs 4.0 bn in FY'2022. Total fees and commissions increased by 14.3% to Kshs 17.4 bn, from Kshs 15.3 bn in FY'2022. The revenue mix shifted to 54:46 from 50:50 for the funded to Non-funded income owing to the 12.8% growth in Funded Income compared to 3.9% decline in the Non Funded Income,
- Total operating expenses increased by 0.8% to Kshs 38.2 bn from Kshs 37.9 bn in FY'2022, driven by 19.7% increase in staff costs to Kshs 12.1 bn from Kshs 10.1 bn recorded in FY'2022, coupled with a 15.2% increase in other operating expenses to Kshs 17.0 bn from Kshs 14.7 bn in FY'2022, which outpaced the 29.9% decrease in loan loss provision to Kshs 9.2 bn, from Kshs 13.1 bn in FY'2022,
- Cost to Income Ratio (CIR) decreased to 60.0% from 62.2% in FY'2022, owing to the 4.5% increase in total operating income, which outpaced the 0.8% increase in total operating expenses. Notably, CIR without LLP increased by 4.9% points to 45.7% from 40.8% recorded in FY'2022, and,
- Profit before tax increased by 13.3% to Kshs 25.5 bn from Kshs 22.5 bn in FY'2022, with effective tax rate decreasing to 15.8% in FY'2023 from 38.7% in FY'2022, leading to a 55.7% increase in profit after tax to Kshs 21.5 bn in FY'2023, from Kshs 13.8 bn in FY'2022.

Balance Sheet

- The balance sheet recorded an expansion as total assets grew by 18.6% to Kshs 734.6 bn, from Kshs 619.7 bn in FY'2022, driven by a by a 20.8% expansion of the loan book to Kshs 337.0 bn, from Kshs 278.9 bn in FY'2022, coupled with a 159.8% increase in placements to Kshs 66.7 bn, from Kshs 25.7 bn in FY'2022, which outpaced the 4.4% decline in Kenya government securities available for sale (AFS) to Kshs 78.3 bn, from Kshs 81.9 bn in FY'2022 and 4.5% decrease in property and equipment to Kshs 2.3 bn, from Kshs 2.4 bn in FY'2022,

- Total liabilities rose by 18.7% to Kshs 638.0 bn from Kshs 537.2 bn in FY'2022, driven by a 15.3% growth in customer deposits to Kshs 579.4 bn, from Kshs 502.7 bn in FY'2022, coupled with a 52.4% increase in borrowings to 6.4 bn from Kshs 4.2 bn recorded in FY'2022, and a 29.2% increase in placements to Kshs 7.6 bn, from Kshs 5.9 bn in FY'2022. With 109 branches in total, compared to 101 branches in FY'2022, deposits per branch increased by 6.8% to Kshs 5.3 bn, from Kshs 5.0 bn in FY'2022,
- The faster 20.8% growth in customer loans and advances as compared to the 15.3% growth in deposits led to an increase in the loan to deposits ratio to 58.2%, from 55.5% in FY'2022,
- The bank's Asset Quality improved, with Gross NPL ratio decreasing to 12.3% in FY'2023 from 13.0% in FY'2022, attributable to the 13.9% increase in Gross non-performing loans to Kshs 44.6 bn, from Kshs 39.1 bn in FY'2022, compared to the faster 19.8% increase in gross loans to Kshs 361.6 bn, from Kshs 301.8 bn recorded in FY'2022,
- General Provisions (LLP) decreased marginally by 0.5% to Kshs 15.5 bn in FY'2023 from Kshs 15.6 bn in FY'2022. The NPL coverage decreased to 55.2% in FY'2023, from 58.5% in FY'2022, attributable to the 13.9% increase in Gross non-performing loans to Kshs 44.6 bn, from Kshs 39.1 bn in FY'2022, coupled with the 0.5% decrease in general provisions,
- Shareholders' funds increased by 17.3% to Kshs 96.7 bn in FY'2023, from Kshs 82.4 bn in FY'2022, supported by a 26.6% increase in retained earnings to Kshs 64.9 bn, from Kshs 51.3 bn in FY'2022,
- NCBA bank remains capitalized with a core capital to risk-weighted assets ratio of 18.0%, 7.5% points above the statutory requirement of 10.5%. In addition, the total capital to risk-weighted assets ratio came in at 18.0%, exceeding the statutory requirement of 14.5% by 3.5% points, and,
- The bank currently has a Return on Average Assets (ROaA) of 3.2%, and a Return on Average Equity (ROaE) of 24.0%.

Key Take-Outs:

1. **Strong earnings growth -** Core earnings per share (EPS) grew by 55.7% to Kshs 13.0, from Kshs 8.4 in FY'2022, driven by the 4.5% growth in total operating income to Kshs 63.7 bn, from Kshs 60.9 bn in FY'2022, coupled with a reduced effective tax rate to 15.8%, from 38.7% in FY'2022,
2. **Improved asset quality –** The bank's gross NPL ratio decreased to 12.3% in FY'2023 from 13.0% in FY'2022, attributable to 13.9% increase in Gross non-performing loans to Kshs 44.6 bn, from Kshs 39.1 bn in FY'2022, compared to the faster 19.8% increase in gross loans to Kshs 361.6 bn, from Kshs 301.8 bn recorded in FY'2022,
3. **Increased dividends-** Dividends per share increased by 4.75% to Kshs 4.75 in FY'2023, from Kshs 4.25 in FY'2022 translating to a dividend yield of 10.8% and a dividend payout ratio of 36.5% in 2023 compared to a dividend yield of 13.0% and a dividend payout ratio of 50.8% in 2022.

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

- **Digital transformation**. The lender has capitalized on digital innovation for service delivery over the past years to improve its operational efficiency, which has been a key factor in its financial performance. In March 2024, the lender disclosed that they had disbursed a total of Kshs 930.0 bn via digital banking avenues, including Fuliza, Mshwari and Loop, remaining a market leader in digital lending.

- **Revenue diversification**. The lender has also capitalized on revenue diversification and increasing the bottom line contribution of all the business lines. Notably, subsidiary contribution to group's probitability has increased over the period, standing at Kshs 4.0 bn in FY'2023. Further, the planned 100.0% acquisition of AIG Kenya Insurance is set to increase the non-funded revenue base more.

Valuation Summary

- We are of the view that NCBA Group is a "buy" with a target price of Kshs 56.3 representing an upside of 28.5%, from the current price of 43.8 as of 28th March 2024, inclusive of a dividend yield of 10.8%.
- NCBA group is currently trading at a P/TBV of 0.8x and a P/E of 3.4x vs an industry average of 0.8x and 6.0x respectively.