NCBA Bank– H1’2023
25th August, 2023

Below is a summary of NCBA Group H1’2023 performance:

Balance Sheet	H1'2022	H1'2023	y/y change
Net Loans and Advances	250.5	292.4	16.7%
Government Securities	203.4	202.3	(0.5%)
Total Assets	**604.3**	**660.3**	**9.3%**
Customer Deposits	468.5	516.6	10.3%
Deposits Per Branch	4.5	6.0	33.4%
Total Liabilities	524.0	572.0	9.2%
Shareholders' Funds	**80.2**	**88.3**	**10.1%**

Balance Sheet Ratios	H1'2022	H1'2023	% points change
Loan to Deposit Ratio	53.5%	56.6%	3.1%
Government Securities to Deposit ratio	43.4%	39.2%	(4.2%)
Return on average equity	17.3%	18.2%	0.9%
Return on average assets	2.3%	2.4%	0.1%

Income Statement	H1'2022	H1'2023	y/y change
Net Interest Income	14.8	17.2	16.3%
Net non-Interest Income	14.2	13.8	(2.6%)
Total Operating income	**29.0**	**31.0**	**7.0%**
Loan Loss provision	5.6	4.4	(21.0%)
Total Operating expenses	**17.1**	**18.7**	**9.3%**
Profit before tax	11.2	12.4	10.5%
Profit after tax	**7.8**	**9.3**	**20.3%**
Core EPS	**4.7**	**5.7**	**20.3%**
Dividend Per Share	**2.00**	**1.75**	**(12.5%)**
Dividend payout ratio	**42.4%**	**30.8%**	**(11.6%)**

Income Statement Ratios	H1'2022	H1'2023	% points change
Yield from interest-earning assets	10.0%	10.5%	0.4%
Cost of funding	4.3%	4.7%	0.4%
Net Interest Spread	5.7%	5.7%	0.0%
Net Interest Margin	5.8%	6.0%	0.2%

Capital Adequacy Ratios	H1'2022	H1'2023	% points change
Core Capital/Total Liabilities	19.4%	16.7%	(2.7%)
Minimum Statutory ratio	8.0%	8.0%	
Excess	**11.4%**	**8.7%**	**(2.6%)**
Core Capital/Total Risk Weighted Assets	19.8%	17.9%	(1.9%)
Minimum Statutory ratio	10.5%	10.5%	
Excess	**9.3%**	**7.4%**	**(1.9%)**
Total Capital/Total Risk Weighted Assets	19.8%	18.0%	(1.8%)
Minimum Statutory ratio	14.5%	14.5%	
Excess	**5.3%**	**3.5%**	**(1.8%)**
Liquidity Ratio	64.3%	54.7%	(9.6%)
Minimum Statutory ratio	20.0%	20.0%	
Excess	**44.3%**	**34.7%**	**(9.6%)**

Income Statement

- Core earnings per share grew by 20.3% to Kshs 5.7, from Kshs 4.7 in H1’2022, driven by the 7.0% growth in total operating income to Kshs 31.0 bn, from Kshs 29.0 bn in H1’2022. However, the performance was weighed down by 9.3% growth in total operating expenses to Kshs 18.7 bn from Kshs 17.1 bn in H1’2022,
- The 7.0% growth in total operating income was mainly driven by a 16.3% growth in Net Interest Income to Kshs 17.2 bn from Kshs 14.8 bn in H1’2022, despite the 2.6% decrease in Non Funded Income (NFI) to Kshs 13.8 bn, from Kshs 14.2 bn in H1’2022,
- Interest income grew by 21.7% to Kshs 30.3 bn from Kshs 24.9 bn in H1’2022, mainly driven by a 29.2% growth in interest income from loans and advances to Kshs 16.5 bn from Kshs 12.8 bn in H1’2022 coupled with 11.6% increase in interest income from government securities to Kshs 13.3 bn, from Kshs 11.9 bn. As such, the Yield on Interest-Earning Assets (YIEA) increased to 10.5% from 10.0% recorded in H1’2022, mainly attributable to the faster 21.7% growth in interest income compared to a 13.3% increase in average interest earning assets to Kshs 552.0 bn, from Kshs 487.4 bn in H1’2022,
- Interest expenses rose by 29.7% to Kshs 13.1 bn from Kshs 10.1 bn in H1’2022, driven by 24.5% increase in interest expense on customer deposits to Kshs 12.1 bn from Kshs 9.7 bn in H1’2022, coupled with a 212.9% increase in interest expense on deposits and placements from banking institutions to Kshs 0.7 bn in H1’2023 from Kshs 0.2 bn recorded in H1’2022. Consequently, Cost of funds (COF) increased by 0.4% points to 4.7% from 4.3% recorded in H1’2022, owing to a faster 20.3% increase in Trailing interest expense to Kshs 24.7 bn from Kshs 20.6 bn recorded in H1’2022, compared to a 9.9% increase in average interest bearing liabilities to Kshs 522.1 bn from Kshs 475.1 bn in H1’2022.Trailing interest expense refers to the performance of the interest expense for the past 12 consecutive months. Net Interest Margin (NIM) increased by 0.2% points to 6.0% from 5.8% in H1’2022, attributable to a 16.5% increase in trailing net interest income to Kshs 33.1 bn from Kshs 28.4 bn recorded in H1’2022 which outpaced the 13.3% growth in average interest earning assets,
- Non-Funded Income (NFI) decreased by 2.6% to Kshs 13.8 bn from Kshs 14.2 bn in H1’2022, mainly attributable to an 18.4% decrease in the foreign exchange trading income to Kshs 4.3 bn from Kshs 5.3 bn in H1’2022, highlighting the bank’s reduced foreign exchange margins, coupled with a 11.3% decrease in other income to Kshs 1.2 bn, from Kshs 1.3 bn. However, NFI was supported by a 10.0% increase in income from total fees and commission to Kshs 8.3 bn from Kshs 7.6 bn. The revenue mix shifted to 55:45 from 51:49 for the funded to Non-funded income owing to the 16.3% growth in Funded Income, relative to 2.6% decrease in the Non Funded Income,
- Total operating expenses increased by 9.3% to Kshs 18.7 bn from Kshs 17.1 bn in H1’2022, driven by 29.3% increase in staff costs to Kshs 5.8 bn from Kshs 4.5 bn recorded in H1’2022, which outpaced 21.0% decrease in loan loss provision cost to Kshs 4.4 bn from Kshs 5.6 bn in H1’2022,
- Cost to Income Ratio (CIR) increased to 60.2% from 58.9% in H1’2022, owing to the 9.3% increase in total operating expense, which outpaced the 7.0% increase in total operating income. Similarly, CIR without LLP increased by 6.2% points to 46.0% from 39.8% recorded in H1’2022, and,
- Profit before tax increased by 10.5% to Kshs 12.4 bn from Kshs 11.2 bn in H1’2022, with effective tax rate decreasing to 24.4% in H1’2023 from 30.5% in H1’2022, leading to an 20.3% increase in profit after tax to Kshs 9.3 bn in H1’2023, from Kshs 7.8 bn in H1’2022.

Balance Sheet

- The balance sheet recorded an expansion as total assets grew by 9.3% to Kshs 660.3 bn, from Kshs 604.3 bn in H1’2022, driven by a 16.7% loan book expansion to Kshs 292.4 bn, from Kshs 250.5 bn in H1’2022, coupled with a 45.5% increase in placements to Kshs 57.7 bn from Kshs 39.7 bn in H1’2022,
- Total liabilities rose by 9.2% to Kshs 572.0 bn from Kshs 524.0 bn in H1’2022, mainly driven by a 10.3% growth in customer deposits to Kshs 516.6 bn, from Kshs 468.5 bn in H1’2022,

- The faster 16.7% growth in loans as compared to the 10.3% growth in deposit led to an increase in the loan to deposits ratio to 56.6%, from 53.5% in H1’2022,
- The bank’s Asset Quality improved, with Gross NPL ratio decreasing to 13.4% in H1’2023 from 13.6% in H1’2022, attributable to the 15.9% increase in gross loans to Kshs 317.0 bn, from Kshs 273.6 bn recorded in H1’2022, which outpaced the 14.6% increase in Gross non-performing loans to Kshs 42.6 bn, from Kshs 37.2 bn in H1’2022,
- General Provisions (LLP) increased by 8.9% to Kshs 15.7 bn in H1’2023, from Kshs 14.4 bn in H1’2022. The NPL coverage decreased to 57.8% in H1’2023, from 62.0% in H1’2022, attributable to the 14.6% increase in gross non-performing loans which outpaced the 3.5% increase in interest in suspense to Kshs 9.0 bn from 8.7 bn in H1’2022 coupled with the 8.9% increase in General Provisions.
- Shareholders’ funds increased by 10.1% to Kshs 88.3 bn in H1’2023, from Kshs 80.2 bn in H1’2022, supported by a 15.9% increase in retained earnings to Kshs 60.6 bn, from Kshs 52.3 bn in H1’2022,
- NCBA bank remains capitalized with a core capital to risk-weighted assets ratio of 17.9%, 7.4% 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 2.4%, and a Return on Average Equity (ROaE) of 18.2%.

Key Take-Outs:

1. **Strong earnings growth -** Core earnings per share (EPS) grew by 20.3% to Kshs 5.7, from Kshs 4.7 in H1’2022, driven by the 7.0% growth in total operating income to Kshs 31.0 bn, from Kshs 29.0 bn in H1’2022.

- **Improved asset quality –** The bank’s gross NPL ratio decreased to 13.4% in H1’2023 from 13.6% in H1’2022, attributable to the 15.9% increase in gross loans to Kshs 317.0 bn, from Kshs 273.6 bn recorded in H1’2022, which outpaced the 14.6% increase in Gross non-performing loans to Kshs 42.6 bn, from Kshs 37.2 bn in H1’2022,
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Going forward, the factors that would drive the bank’s growth would be:

- **Digitization**. The lender has capitalized on partnering with telecommunication companies to offer mobile based loaning services like Mshwari and Fuliza, which is expected to continue growing the revenue growth.

Valuation Summary

- We are of the view that NCBA bank is a “buy” with a target price of Kshs 43.4 representing an upside of 24.1%, from the current price of 38.3 as of 25th August 2023, 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 4.6x vs an industry average of 0.8x and 3.5x respectively.