

Below is a summary of NCBA Group's Q3'2023 performance:

| Balance Sheet (Kshs bn) | Q3'2022 | Q3'2023 | y/y change |
|----------------------------|--------------|--------------|--------------|
| Net Loans and Advances | 266.1 | 308.7 | 16.0% |
| Government Securities | 206.8 | 200.8 | (2.9%) |
| Total Assets | 595.4 | 678.8 | 14.0% |
| Customer Deposits | 462.1 | 548.1 | 18.6% |
| Total Liabilities | 514.5 | 590.3 | 14.7% |
| Shareholders' Funds | 80.9 | 88.5 | 9.4% |

| Balance Sheet Ratios | Q3'2022 | Q3'2023 | % points change |
|--|---------|---------|-----------------|
| Loan to Deposit Ratio | 57.6% | 56.3% | (1.3%) |
| Government Securities to Deposit ratio | 44.8% | 36.6% | (8.1%) |
| Return on average equity | 21.2% | 18.4% | (2.8%) |
| Return on average assets | 2.8% | 2.5% | (0.4%) |

| Income Statement (Kshs bn) | Q3'2022 | Q3'2023 | y/y change |
|---------------------------------|-------------|-------------|--------------|
| Net Interest Income | 23.2 | 26.0 | 11.7% |
| Net non-Interest Income | 22.5 | 20.7 | (8.0%) |
| Total Operating income | 45.8 | 46.7 | 2.0% |
| Loan Loss provision | 8.3 | 6.1 | (27.1%) |
| Total Operating expenses | 26.9 | 28.1 | 4.7% |
| Profit before tax | 18.2 | 18.6 | 2.1% |
| Profit after tax | 12.8 | 14.6 | 14.4% |
| Core EPS (Kshs) | 7.8 | 8.9 | 14.4% |

| Income Statement Ratios | Q3'2022 | Q3'2023 | % points change |
|------------------------------------|---------|---------|-----------------|
| Yield from interest-earning assets | 10.1% | 10.9% | 0.8% |
| Cost of funding | 4.4% | 5.2% | 0.8% |
| Net Interest Spread | 5.7% | 5.7% | 0.0% |
| Net Interest Margin | 6.0% | 6.0% | 0.1% |

| Capital Adequacy Ratios | Q3'2022 | Q3'2023 | % points change |
|--|--------------|--------------|-----------------|
| Core Capital/Total Liabilities | 16.9% | 15.6% | (1.3%) |
| Minimum Statutory ratio | 8.0% | 8.0% | 0.0% |
| Excess | 8.9% | 7.6% | (1.3%) |
| Core Capital/Total Risk Weighted Assets | 18.4% | 17.2% | (1.2%) |
| Minimum Statutory ratio | 10.5% | 10.5% | 0.0% |
| Excess | 7.9% | 6.7% | (1.2%) |
| Total Capital/Total Risk Weighted Assets | 18.4% | 17.2% | (1.2%) |
| Minimum Statutory ratio | 14.5% | 14.5% | 0.0% |
| Excess | 3.9% | 2.7% | (1.2%) |
| Liquidity Ratio | 55.6% | 52.5% | (3.1%) |
| Minimum Statutory ratio | 20.0% | 20.0% | 0.0% |
| Excess | 35.6% | 32.5% | (3.1%) |

Income Statement

- Core earnings per share increased by 14.4% to Kshs 8.9, from Kshs 7.8 in Q3'2022, driven by the 2.0% growth in total operating income to Kshs 46.7 bn, from Kshs 45.8 bn in Q3'2022. However, the performance was weighed down by 4.7% growth in total operating expenses to Kshs 28.1 bn from Kshs 26.9 bn in Q3'2022,
- The 2.0% growth in total operating income was mainly driven by a 11.7% growth in Net Interest Income to Kshs 26.0 bn from Kshs 23.2 bn in Q3'2022, which outweighed the 8.0% decrease in Non Funded Income (NFI) to Kshs 20.7 bn, from Kshs 22.5 bn in Q3'2022,
- Interest income increased by 21.1% to Kshs 47.0 bn from Kshs 38.8 bn in Q3'2022, mainly driven by a 29.4% growth in interest income from loans and advances to Kshs 25.9 bn from Kshs 20.0 bn in Q3'2022 coupled with 9.7% increase in interest income from government securities to Kshs 20.0 bn, from Kshs 18.2 bn. As a result, the Yield on Interest-Earning Assets (YIEA) increased marginally to 10.9% from 10.1% recorded in Q3'2022, mainly attributable to the faster 18.6% growth in trailing interest income compared to a 9.9% increase in average interest earning assets to Kshs 554.8 bn, from Kshs 504.8 bn in Q3'2022,
- Interest expenses rose by 35.5% to Kshs 21.0 bn from Kshs 15.5 bn in Q3'2022, driven by 33.9% increase in interest expense on customer deposits to Kshs 19.4 bn from Kshs 14.5 bn in Q3'2022, coupled with a 138.4% increase in interest expense on deposits and placements from banking institutions to Kshs 1.1 bn in Q3'2023 from Kshs 0.25bn recorded in Q3'2022. Consequently, Cost of funds (COF) increased by 0.8% points to 5.2% from 4.4% recorded in Q3'2022, owing to a faster 29.6% increase in Trailing interest expense to Kshs 27.2 bn from Kshs 21.0 bn recorded in Q3'2022, compared to a 10.1% increase in average interest bearing liabilities to Kshs 521.5 bn from Kshs 473.5 bn in Q3'2022. Trailing interest expense refers to the performance of the interest expense for the past 12 consecutive months. Net Interest Margin (NIM) increased by 0.1% points to 6.0% from 5.9% in Q3'2022, attributable to a 11.0% increase in trailing net interest income to Kshs 33.4 bn from Kshs 30.1 bn recorded in Q3'2022 which outpaced the 9.9% growth in average interest earning assets,
- Non-Funded Income (NFI) decreased by 8.0% to Kshs 20.7 bn from Kshs 22.5 bn in Q3'2022, mainly attributable to an 34.3% decline in the foreign exchange trading income to Kshs 6.0 bn from Kshs 9.2 bn in Q3'2022, highlighting the bank's reduced foreign exchange margins. However, NFI was supported by a 36.3% increase in income from other fees and commission to Kshs 4.0 bn from Kshs 2.9 bn. Consequently, the revenue mix shifted to 56:44 from 51:49 for the funded to Non-funded income owing to the 11.7% growth in Funded Income, relative to 8.0% decrease in the Non Funded Income,
- Total operating expenses increased by 4.7% to Kshs 28.1 bn from Kshs 26.9 bn in Q3'2022, driven by 31.1% increase in staff costs to Kshs 9.3 bn from Kshs 7.1 bn recorded in Q3'2022, which offset the 27.1% decrease in loan loss provision cost to Kshs 6.1 bn from Kshs 8.3 bn in Q3'2022,
- Cost to Income Ratio (CIR) increased to 60.2% from 58.7% in Q3'2022, owing to the 4.7% increase in total operating expense, which outpaced the 2.0% increase in total operating income. Similarly, CIR without LLP increased by 6.7% points to 47.2% from 40.5% recorded in Q3'2022, and,
- Profit before tax increased by 2.1% to Kshs 18.6 bn from Kshs 18.2 bn in Q3'2022, with effective tax rate decreasing to 21.1% in Q3'2023 from 29.6% in Q3'2022, leading to an 14.4% increase in profit after tax to Kshs 8.9 bn in Q3'2023, from Kshs 7.8 bn in Q3'2022.

Balance Sheet

- The balance sheet recorded an expansion as total assets grew by 14.0% to Kshs 678.8 bn, from Kshs 595.4 bn in Q3'2022, driven by a 16.0% loan book expansion to Kshs 308.7 bn, from Kshs 266.1 bn in Q3'2022, which outweighed the 2.9% decline in investments in government securities to Kshs 200.8 bn from Kshs 206.8 bn in Q3'2022,
- Total liabilities rose by 14.7% to Kshs 590.3 bn from Kshs 514.5 bn in Q3'2022, mainly driven by a 18.6% growth in customer deposits to Kshs 548.1 bn, from Kshs 462.1 bn in Q3'2022, which outweighed the 12.8% decline in placements to Kshs 11.3 bn from Kshs 13.0 bn on Q3'2022

- The faster 18.6% growth in customer deposits as compared to the 16.0% growth in loans and advances led to an decline in the loan to deposits ratio to 56.3%, from 57.6% in Q3'2022,
- The bank's Asset Quality improved, with Gross NPL ratio decreasing to 12.0% in Q3'2023 from 12.6% in Q3'2022, attributable to the 14.3% increase in gross loans to Kshs 331.3 bn, from Kshs 289.9 bn recorded in Q3'2022, which outpaced the 9.2% increase in Gross non-performing loans to Kshs 39.7 bn, from Kshs 36.4 bn in Q3'2022,
- General Provisions (LLP) decreased by 13.7% to Kshs 14.5 bn in Q3'2023, from Kshs 16.8 bn in Q3'2022. The NPL coverage decreased to 56.8% in Q3'2023, from 65.3% in Q3'2022, attributable to the 9.2% increase in gross non-performing loans which outweighed the 16.3% increase in interest in suspense to Kshs 8.1 bn from 6.9 bn in Q3'2022 coupled with the 13.7% decrease in General Provisions.
- Shareholders' funds increased by 9.4% to Kshs 88.5 bn in Q3'2023, from Kshs 80.9 bn in Q3'2022, supported by a 16.6% increase in retained earnings to Kshs 63.0 bn, from Kshs 54.1 bn in Q3'2022,
- NCBA bank remains capitalized with a core capital to risk-weighted assets ratio of 17.2%, 6.7% points above the statutory requirement of 10.5%. In addition, the total capital to risk-weighted assets ratio came in at 17.2%, exceeding the statutory requirement of 14.5% by 2.7% points, and,
- The bank currently has a Return on Average Assets (ROaA) of 2.5%, and a Return on Average Equity (ROaE) of 18.4%.

Key Take-Outs:

1. **Strong earnings growth** - Core earnings per share (EPS) increased by 14.4% to Kshs 8.9, from Kshs 7.8 in Q3'2022, driven by the 2.0% growth in total operating income to Kshs 46.7 bn, from Kshs 45.8 bn in Q3'2022.
2. **Improved asset quality** – The Group's gross NPL ratio decreased to 12.0% in Q3'2023 from 12.6% in Q3'2022, attributable to the 14.3% increase in gross loans to Kshs 331.3 bn, from Kshs 289.9 bn recorded in Q3'2022, which outpaced the 9.2% increase in Gross non-performing loans to Kshs 39.7 bn, from Kshs 36.4 bn in Q3'2022,
3. **Improved Lending** – The Group's loan book increased by 16.0% to kshs 308.7 bn, from kshs 266.1 bn in Q3'2022, which outweighed the 2.9% decline in investment in government securities to Kshs 200.8 bn from Kshs 206.8 bn in Q3'2022, highlighting the Group's strategy to increase lending.

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

- **Continued Digitization.** The Group 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. In addition, NCBA continues to advance its digital transformation through the enhanced one plus mobile platforms with the lender reporting Kshs 695.0 bn in digital lending during the quarter
- **Branch expansion.** The lender has continued to grow its foothold on the Kenyan market through addition of new branches in the country, with the latest additions being the Muranga, Kenol, Chwele, Migori, Kahawa Sukari, Eastleigh, Wote, and Ruaka taking the total number of branches to 107. This expansion has enabled the bank to bring services closer to its clients while also tapping into new regions.

Valuation Summary

- We are of the view that NCBA Group is an "accumulate" with a target price of Kshs 43.5 representing an upside of 14.2%, from the current price of 38.1 as of 24th November 2023, inclusive of a dividend yield of 11.2%.
- NCBA Group is currently trading at a P/TBV of 0.8x and a P/E of 4.6x against an industry average of 0.8x and 3.5x respectively.