Equity Group Holdings Plc – H1'2022
25th August, 2022

Below is a summary of Equity Group Holdings Plc H1'2022 performance:

Balance Sheet Items	H1'2021 (Kshs bn)	H1'2022 (Kshs bn)	y/y change
Government Securities	202.6	236.8	16.9%
Net Loans and Advances	504.8	650.6	28.9%
Total Assets	**1,119.7**	**1,333.9**	**19.1%**
Customer Deposits	819.7	970.9	18.5%
Deposits per Branch	2.7	2.8	5.7%
Total Liabilities	964.7	1,183.5	22.7%
Shareholders' Funds	**148.2**	**143.7**	**(3.0%)**

Balance Sheet Ratios	H1'2021	H1'2022	% points y/y change
Loan to Deposit Ratio	61.6%	67.0%	5.4%
Return on average equity	21.4%	31.9%	10.5%
Return on average assets	3.1%	3.8%	0.7%

Income Statement	H1'2021 (Kshs bn)	H1'2022 (Kshs bn)	y/y change
Net Interest Income	31.2	39.8	27.8%
Net non-Interest Income	20.8	25.8	24.4%
Total Operating income	**51.9**	**65.6**	**26.4%**
Loan Loss provision	(2.9)	(4.1)	40.3%
Total Operating expenses	(28.1)	(34.7)	23.6%
Profit before tax	23.8	30.9	29.7%
Profit after tax	**17.9**	**24.4**	**36.1%**
Core EPS	**4.8**	**6.5**	**36.1%**

Income Statement Ratios	H1'2021	H1'2022	% points y/y change
Yield from interest-earning assets	10.3%	10.0%	(0.3%)
Cost of funding	2.9%	2.8%	(0.1%)
Cost of risk	5.6%	6.2%	0.6%
Net Interest Margin	7.6%	7.3%	(0.3%)
Net Interest Income as % of operating income	60.0%	60.6%	0.6%
Non-Funded Income as a % of operating income	40.0%	39.4%	(0.6%)
Cost to Income Ratio	54.1%	52.9%	(1.2%)
Cost to Income Ratio without LLP	48.5%	46.7%	(1.8%)
Cost to Assets	2.7%	2.5%	(0.2%)

Capital Adequacy Ratios	H1'2021	H1'2022	% Points Change
Core Capital/Total Liabilities	15.8%	17.0%	1.2%
Minimum Statutory ratio	8.0%	8.0%	0.0%
Excess	**7.8%**	**9.0%**	**1.2%**
Core Capital/Total Risk Weighted Assets	14.0%	15.5%	1.5%
Minimum Statutory ratio	10.5%	10.5%	0.0%
Excess	**3.5%**	**5.0%**	**1.5%**
Total Capital/Total Risk Weighted Assets	17.5%	20.2%	2.7%
Minimum Statutory ratio	14.5%	14.5%	0.0%
Excess	**3.0%**	**5.7%**	**2.7%**
Liquidity Ratio	62.4%	53.2%	(9.2%)

Minimum Statutory ratio	20.0%	20.0%	0.0%
Excess	**42.4%**	**33.2%**	**(9.2%)**
Adjusted core capital/ total deposit liabilities	15.8%	17.1%	1.3%
Adjusted core capital/ total risk weighted assets	14.1%	15.5%	1.4%
Adjusted total capital/ total risk weighted assets	17.6%	20.2%	2.6%

Key Highlights

- Equity Group Holdings (EGH), announced the completion of the incorporation of a subsidiary, Equity Group Insurance Holdings Limited, a non-operating insurance holding company and issuance of a life insurance license to Equity Life Assurance Kenya (ELAK) Limited. ELAK, which is fully owned by Equity Group Insurance Holdings Limited, will conduct and undertake long-term insurance business in Kenya. This came after EGH obtained the prerequisite approvals from its shareholders and the Central Bank of Kenya (CBK), before subsequent registration and licensing from the Insurance Regulatory Authority (IRA) on 10th January 2022. For more information, please see our Cytonn Weekly #02/2022,
- The International Finance Corporation (IFC) and the IFC Financial Institutions Growth (FIG) Fund, jointly acquired 6.7% stake in Equity Group in a sale agreement with Britam Holdings (the parent company), and Britam Life Assurance (subsidiary). Britam Holdings sold 166,390,750 shares in EGH (110,901,488 shares to IFC and 55,489,262 shares to the IFC FIG Fund), constituting 4.4% of EGH’s issued shares, while Britam Life Assurance Company sold 86,719,611 shares (53,620,247 shares to IFC and 33,099,364 shares to the IFC FIG Fund), and constituting 2.3% of EGH’s issued capital. For more information, please see our Cytonn Weekly #14/2022 and Cytonn Weekly #19/2022, and,
- Equity Group Holdings Plc announced that it had injected USD 100.0 mn (Kshs 11.5 bn) to its subsidiary in the Democratic Republic of Congo (DRC), Equity BCDC, in order to fund development projects as well as large manufacturing and mining companies in the DRC given the country’s diverse and immense natural resources as well as the sectors contribution to economic growth. Notably, the two sectors contribute only 7.0% to the Group’s loan book, as at FY’2021, thus providing an opportunity that the bank can tap into, to diversify its revenues and risk exposure. For more information, please see our Cytonn Weekly #15/2022.

Income Statement

- Core earnings per share increased by 36.1% to Kshs 6.5 in H1’2022, from Kshs 4.8 recorded in H1’2021, higher than our projections of a 4.2% increase to Kshs 5.0. The performance was driven by a 26.4% growth in total operating income to Kshs 65.6 bn, from Kshs 51.9 bn in H1’2021, faster than the 23.6% growth in total operating expenses to Kshs 34.7 bn, from Kshs 28.1 bn in H1’2021,
- Total Operating Income rose by 26.4% to Kshs 65.6 bn, from Kshs 51.9 bn recorded in H1’2021 driven by a 27.8% increase in Net Interest Income (NII) to Kshs 39.8 bn, from Kshs 31.2 bn in H1’2021, coupled with a 24.4% increase in Non-Funded Income (NFI) to Kshs 25.8 bn, from Kshs 20.8 bn in H1’2021,
- Interest income increased by 28.6% to Kshs 55.0 bn, from Kshs 42.7 bn in H1’2021 driven by a 20.8% increase in interest income from loans and advances to Kshs 35.3 bn, from Kshs 29.2 bn recorded in H1’2021, coupled with a 50.4% increase in interest income from government securities to Kshs 19.1 bn, from Kshs 12.7 bn in H1’2021. The Yield on Interest-Earning Assets, however, declined by 0.3% points to 10.0%, from 10.3% in H1’2021, as the average interest-earning assets grew faster by 30.4% to Kshs 1,062.8 bn, from Kshs 815.2 bn in H1’2021 compared to the 27.3% increase in trailing interest income. Trailing Interest Income refers to the performance of the interest income for the past 12 consecutive months,
- Interest expenses rose by 30.9% to Kshs 15.2 bn, from Kshs 11.6 bn in H1’2021, following a 13.3% increase in interest expense on customer deposits to Kshs 10.5 bn, from Kshs 9.3 bn in H1’2021, coupled

with a 72.1% increase in other interest expenses to Kshs 3.6 bn, from Kshs 2.1 bn in H1’2021. Cost of funds declined by 0.1% points to 2.8%, from 2.9% recorded in H1’2021, as the average interest-bearing liabilities grew faster by 34.9% to Kshs 1,027.8 bn, from Kshs 761.7 bn in H1’2021 compared to the 32.0% growth in trailing interest expense. Trailing interest expense refers to the performance of the interest expenses for the past 12 consecutive months. The Net Interest Margin (NIM) also declined to 7.3%, from 7.6% in H1’2021, attributable to the 30.4% growth in average interest-earning assets, which outpaced the 27.3% growth in trailing Net Interest Income (NII),

- Non-Funded Income (NFI) rose by 24.4% to Kshs 25.8 bn, from Kshs 20.8 bn in H1’2021. The increase was mainly driven by a 31.0% growth in income from other fees and commissions to Kshs 12.7 bn, from Kshs 9.7 bn in H1’2021, coupled with a 23.3% increase in foreign exchange trading income to Kshs 5.0 bn, from Kshs 4.1 bn in H1’2021. Income from fees and commissions on loans also increased by 21.4% to Kshs 4.2 bn , from Kshs 3.5 bn in H1’2021. Equity Group’s total fees and commission increased by 28.5% to Kshs 16.9 bn, from Kshs 13.1 bn in H1’2021. Consequently, the revenue mix shifted to 61:39 from 60:40, funded to non-funded income, recorded in H1’2021, owing to the faster 27.8% increase in net funded income compared to the 24.4% growth in non-funded income,
- Total operating expenses increased by 23.6% to Kshs 34.7 bn in H1’2022, from Kshs 28.1 bn recorded in H1’2021, mainly due to a 40.3% increase in Loans Loss Provision to Kshs 4.1 bn in H1’2022, from Kshs 2.9 bn recorded in H1’2021 coupled with a 27.0% increase in staff cost to Kshs 10.8 bn, from Kshs 8.5 bn in H1’2021. The increased provisioning level points towards more risk aversion and increased credit risk on the back of the high cost of living,
- Cost to Income Ratio (CIR) with LLP improved by 1.2% points to 52.9%, from 54.1% in H1’2021 due to the 26.4% increase in total income which outpaced the 23.6% growth in total expenses. Without LLP, the Cost to Income ratio also improved, declining by 1.8% points to 46.7%, from 48.5% in H1’2021, an indication of improved efficiency levels in the Banks, and,
- Profit before tax increased by 29.7% to Kshs 30.9 bn, from Kshs 23.8 bn in H1’2021 with the effective tax rate declining to 21.0% from 24.7% in H1’2021. Similarly, the profit after tax increased by 36.1% to Kshs 24.4 bn in H1’2022, from Kshs 17.9 bn recorded in H1’2021.

Balance Sheet

- The balance sheet recorded an expansion as total assets increased by 19.1% to Kshs 1,333.9 bn in H1’2022, from Kshs 1,119.7 bn recorded in H1’2021, largely driven by the 28.9% growth in the loan book to Kshs 650.6 bn, from Kshs 504.8 bn recorded in H1’2021, coupled with a 16.9% growth in Government securities to Kshs 236.8 bn in H1’2022, from Kshs 202.6 bn in H1’2021,
- Total liabilities rose by 22.7% to Kshs 1,183.5 bn, from Kshs 964.7 bn in H1’2021, driven by an 18.5% increase in customer deposits to Kshs 970.9 bn, from Kshs 819.7 bn in H1’2021. Deposits per branch increased by 5.7% to Kshs 2.8 bn, from Kshs 2.7 bn in H1’2021, with the number of branches increasing by 5 to 342 branches in H1’2022, from 337 in H1’2021, with Equity Bank Uganda contributing 2 while Equity Bank Rwanda, Kenya and Tanzania contributed 3 additional branches, I from each,
- The faster 28.9% growth in loans as compared to the 18.5% growth in customer deposits led to an increase in the Loans to deposit ratio to 67.0% from 61.6% in H1’2021,
- Gross Non-Performing Loans (NPLs) reduced by 1.9% to Kshs 61.0 bn in H1’2022, from Kshs 62.2 bn recorded in H1’2021. Consequently, the group’s asset quality improved, with the NPL ratio declining to 8.8% in H1’2022, from 11.4% recorded in H1’2021, attributable to the 1.9% decline in Gross Non-Performing Loans (NPLs) coupled with a 26.7% growth in gross loans.
- The NPL coverage improved to 64.1%, from 63.2% in H1’2021 on the back of a 39.7% increase in interest in suspense to Kshs 11.6 bn, from Kshs 8.3 bn in H1’2021 coupled with the 1.9% decline in Gross Non-Performing Loans,

- Shareholders’ funds declined by 3.0% to Kshs 143.7 bn in H1’2022, from Kshs 148.2 bn in H1’2021, mainly due to a 640.5% increase in revaluation reserve to Kshs 43.6 bn, from Kshs 5.9 bn in H1’2021,
- Equity Group is currently sufficiently capitalized with a core capital to risk-weighted assets ratio of 15.5%, 5.0% points above the minimum statutory requirement of 10.5%. In addition, the total capital to risk-weighted assets ratio was 20.2%, exceeding the minimum statutory requirement of 14.5% by 5.7% points. Adjusting for IFRS 9, the core capital to risk-weighted assets stood at 15.5% while total capital to risk-weighted assets came in at 20.2%, and,
- The bank currently has a Return on Average Assets (ROaA) of 3.8%, and a Return on Average Equity (ROaE) of 31.9%.

Key Take-Outs:

1. **The Group’s diversification strategy deemed profitable** - The Group’s geographical diversification strategy has continued to emerge as a net positive, with the bank’s various subsidiaries in Uganda, DRC, Rwanda, Tanzania, and South Sudan cumulatively contributing 28.0% to the bank’s total profitability and 40.0% to the group’s total asset base. Cumulatively, the group’s subsidiaries, excluding Equity Bank Kenya Ltd, recorded an 85.7% growth in their Profit after Tax (PAT) to Kshs 6.6 bn, from Kshs 3.5 bn in H1’2021, with the Equity BCDC in DRC recording a 447.0% growth in PAT to Kshs 1.6 bn from Kshs 0.4 bn in H1’2021, mainly driven by favorable operating business environment coupled with low banking penetration which providing more opportunities for profitability. However, concerns remain high on the high NPL levels in the group’s Tanzanian subsidiary of 23.8% and we expect the group to improve its credit assessment in the country to bring down the high NPL ratio,
2. I**nnovation and digitization continue to enhance high value transaction** - increased innovation and digitization have seen 99.0% of all transactions of the bank being done on alternative channels, with mobile and internet transactions taking up 83.7% of all transactions, and agency banking contributing 5.9% of all transactions. In terms of the value of transactions, digital banking, branches and diaspora remittances contributed 49.9%, 25.6% and 4.4%, respectively. This highlights the transformation of branches to handle high-value transactions which aid the bank by offering its ecosystem banking products to retail and SME clients, and,
3. **Asset quality improves** - the group’s asset quality improved as evidenced by the 2.6% points decline in the NPL ratio to 8.8% in H1’2022, from 11.4% recorded in H1’2021, attributable to the 1.9% decline in Gross Non-Performing Loans (NPLs) coupled with a 26.7% growth in gross loans. The main sectors that contributed to the Non-Performing Loans were MSMEs and Agriculture, which contributed 20.9% and 7.1%, respectively. The group’s Tanzanian subsidiary recorded the highest NPL ratio, coming in at 23.8% in H1’2022, with Equity Bank Kenya recording an NPL ratio of 8.4% in H1’2022.

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

I. **Channeled diversification** – This will aid in further improvement on efficiency with emphasis on alternative channels of transactions, as the bank rides on the digital revolution wave, thereby further improving the cost to income ratio by cost rationalization and revenue expansion. This will likely propel the bank’s prospects of achieving sustainable growth, as it replicates its successful business model across its various regional subsidiaries,

II. **The bank’s operating model** – The banks operating model focuses on enhancing the balance sheet agility which is likely to place the bank in a prime position to take advantage of any opportunities that may arise, such as attractive inorganic growth via acquisitions or fast lending with the repeal of the interest rate cap law and the recent approval of the risk-based pricing lending model. The bank’s balance sheet agility is seen with a liquidity ratio of 53.2%, an improving loan to deposit ratio of 67.0% and a core capital to risk-weighted asset ratio of 15.5%, and,

III. Continued expansion through acquisition of other banks in Kenya as well as in the region, including a consideration to purchase back a stake in Housing Finance (HF) Group. Equity Group previously owned 24.7% stake in HF Group but sold all their shares in 2014.

Valuation Summary

- We are of the view that Equity Group is a “***Buy***” with a target price of Kshs 63.7 representing an upside of 29.5%, from the current price of Kshs 49.2 as of 26th August 2022, and,
- Equity Group is currently trading at a P/TBV of 1.2x and a P/E of 4.3x vs an industry average of 0.7x and 4.5x, respectively.