Equity Group Holdings Plc – Q1’2022
13th May, 2022

Below is a summary of Equity Group Holdings Plc Q1’2022 performance:

Balance Sheet Items	Q1’2021 (Kshs bn)	Q1’2022 (Kshs bn)	y/y change
Government Securities	183.0	233.9	27.9%
Net Loans and Advances	487.7	623.6	27.8%
Total Assets	**1,066.4**	**1,269.5**	**19.0%**
Customer Deposits	789.9	900.9	14.0%
Total Liabilities	**926.0**	**1,095.3**	**18.3%**
Shareholders’ Funds	**133.9**	**167.2**	**24.9%**

Balance Sheet Ratios	Q1’2021	Q1’2022	% points y/y change
Loan to Deposit Ratio	61.7%	69.2%	7.5%
Return on average equity	18.9%	28.7%	9.8%
Return on average assets	2.7%	3.7%	1.0%

Income Statement	Q1’2021 (Kshs bn)	Q1’2022 (Kshs bn)	y/y change
Net Interest Income	14.8	19.4	30.6%
Net non-Interest Income	10.9	11.9	9.7%
Total Operating income	**25.7**	**31.3**	**21.7%**
Loan Loss provision	(1.3)	(1.8)	42.4%
Total Operating expenses	(14.0)	(16.0)	14.3%
Profit before tax	11.7	15.3	30.6%
Profit after tax	**8.7**	**11.9**	**36.0%**
Core EPS	**2.3**	**3.1**	**36.0%**

Income Statement Ratios	Q1’2021	Q1’2022	% points y/y change
Yield from interest-earning assets	10.3%	9.9%	(0.4%)
Cost of funding	2.8%	2.8%	-
Cost of risk	4.9%	5.8%	0.9%
Net Interest Margin	7.6%	7.2%	(0.4%)
Net Interest Income as % of operating income	57.7%	61.9%	4.2%
Non-Funded Income as a % of operating income	42.3%	38.1%	(4.2%)
Cost to Income Ratio	54.4%	51.1%	(3.3%)
Cost to Income Ratio without LLP	49.5%	45.3%	(4.2%)
Cost to Assets	1.4%	1.2%	(0.2%)

Capital Adequacy Ratios	Q1'2021	Q1'2022	% Points Change
Core Capital/Total Liabilities	15.8%	16.3%	0.5%
Minimum Statutory ratio	8.0%	8.0%	0.0%
Excess	**7.8%**	**8.3%**	**0.5%**
Core Capital/Total Risk Weighted Assets	14.2%	13.9%	(0.3%)
Minimum Statutory ratio	10.5%	10.5%	0.0%
Excess	**3.7%**	**3.4%**	**(0.3%)**
Total Capital/Total Risk Weighted Assets	18.0%	18.7%	0.7%
Minimum Statutory ratio	14.5%	14.5%	0.0%
Excess	**3.5%**	**4.2%**	**0.7%**
Liquidity Ratio	60.6%	56.9%	(3.7%)
Minimum Statutory ratio	20.0%	20.0%	0.0%

Excess	**40.6%**	**36.9%**	**(3.7%)**
Adjusted core capital/ total deposit liabilities	15.9%	16.3%	0.4%
Adjusted core capital/ total risk weighted assets	14.3%	13.9%	(0.4%)
Adjusted total capital/ total risk weighted assets	18.1%	18.7%	0.6%

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.

Below are the key Equity Group highlights so far in Q2’2022:

- 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,
- 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 36.0% to Kshs 3.1 in Q1’2022, from Kshs 2.3 recorded in Q1’2021, higher than our projections of a 25.3% increase to Kshs 2.9. The performance was driven by a 21.7% growth in total operating income to Kshs 31.3 bn, from Kshs 25.7 bn in Q1’2021, faster than the 14.3% growth in total operating expenses to Kshs 16.0 bn, from Kshs 14.0 bn in Q1’2021,
- Total Operating Income rose by 21.7% to Kshs 31.3 bn, from Kshs 25.7 bn recorded in Q1’2021 driven by a 30.6% increase in Net Interest Income (NII) to Kshs 19.4 bn, from Kshs 14.8 bn in Q1’2021, coupled with a 9.7% increase in Non-Funded Income (NFI) to Kshs 11.9 bn, from Kshs 10.9 bn in Q1’2021,
- Interest income increased by 31.1% to Kshs 26.7 bn, from Kshs 20.3 bn in Q1’2021 driven by a 20.9% increase in interest income on loans and advances to Kshs 17.1 bn, from Kshs 14.2 bn recorded in Q1’2021, coupled with a 58.7% increase in interest income from government securities to Kshs 9.3 bn, from Kshs 5.9 bn in Q1’2021. The Yield on Interest-Earning Assets, however, declined by 0.4% points to 9.9%, from 10.3% in Q1’2021, as the average interest-earning assets grew faster by 32.8% to Kshs 1,018.7 bn, from Kshs 767.2 bn in Q1’2021 compared to the 28.0% increase in trailing interest income. Trailing Interest Income refers to the performance of the interest income for the past 12 consecutive months,
- Interest expense rose by 32.6% to Kshs 7.3 bn, from Kshs 5.5 bn in Q1’2021, following a 19.2% increase in interest expense on customer deposits to Kshs 5.0 bn, from Kshs 4.2 bn in Q1’2021, coupled with a

67.6% increase in other interest expenses to Kshs 1.8 bn, from Kshs 1.1 bn in Q1'2021. Cost of funds remained relatively unchanged at 2.8%, as recorded in Q1'2021, owing to the 34.9% growth in trailing interest expense, and a 34.4% growth in the average interest-bearing liabilities,. Trailing interest expense refers to the performance of the interest expense for the past 12 consecutive months. Net Interest Margin (NIM) however declined to 7.2%, from 7.6% in Q1'2021, attributable to the 32.8% growth in average interest-earning assets, which outpaced the 25.5% growth of trailing Net Interest Income (NII),

- Non-Funded Income (NFI) rose by 9.7% to Kshs 11.9 bn, from Kshs 10.9 bn in Q1'2021. The increase was mainly driven by a 23.1% growth in income from other fees and commissions to Kshs 6.0 bn, from Kshs 4.9 bn in Q1'2021, coupled with a 17.7% increase in income from Fees and commissions on loans and advances to Kshs 1.9 bn, from Kshs 1.7 bn in Q1'2021. Equity Group's total fees and commission increased by 21.7% to Kshs 8.0 bn, from Kshs 6.6 bn in Q1'2021. Notably, the revenue mix shifted to 62:38 from 58:42, funded to non-funded income, recorded in Q1'2021, owing to the faster 30.6% increase in net funded income compared to the 9.7% growth in non-funded income,
- Total operating expenses increased by 14.3% to Kshs 16.0 bn in Q1'2022, from Kshs 14.0 bn recorded in Q1'2021, mainly due to a 42.4% increase in Loans Loss Provision to Kshs 1.8 bn in Q1'2022, from Kshs 1.3 bn recorded in Q1'2021 coupled with a 23.8% increase in staff cost to Kshs 5.0 bn, from Kshs 4.0 bn in Q1'2021. The increased provisioning level points towards more risk aversion as Equity Group's NPL ratio rose to 9.0% in Q1'2022 from 8.6% in FY'2021 and increased credit risk on the back of the increasing cost of living,
- As a result of the 21.7% increase in total income which outpaced the 14.3% growth in total expenses, Cost to Income Ratio (CIR) with LLP improved by 3.3% points to 51.1%, from 54.4% in Q1'2021. Without LLP, the Cost to Income ratio also improved, declining by 4.1% points to 45.3%, from 49.5% in Q1'2021, an indication of improved efficiency levels in the Banks, and,
- Profit after tax increased by 36.0% to Kshs 11.9 bn in Q1'2022, from Kshs 8.7 bn recorded in Q1'2021, driven by a 21.7% growth in total operating income to Kshs 31.3 bn, from Kshs 25.7 bn in Q1'2021, which outpaced the 14.3% increase in total operating expenses to Kshs 16.0 bn, from Kshs 14.0 bn in Q1'2021. Profit before tax increased by 30.6% to Kshs 15.3 bn, from Kshs 11.7 bn in Q1'2021 with the effective tax rate declining to 22.4% from 25.5% in Q1'2021.

Balance Sheet

- The balance sheet recorded an expansion as total assets increased by 19.0% to Kshs 1,269.5 bn in Q1'2022, from Kshs 1,066.4 bn recorded in Q1'2021. This growth was largely driven by the 27.8% growth of the loan book to Kshs 623.6 bn, from Kshs 487.7 bn recorded in Q1'2021, coupled with a 24.9% growth in Government securities to Kshs 233.9 bn in Q1'2022, from Kshs 183.0 bn in Q1'2021,
- Total liabilities rose by 18.3% to Kshs 1,095.3 bn, from Kshs 926.0 bn in Q1'2021, driven by a 14.0% increase in customer deposits to Kshs 900.9 bn, from Kshs 789.9 bn in Q1'2021. Deposits per branch increased by 13.7% to Kshs 2.7 bn, from Kshs 2.4 bn in Q1'2021, with the number of branches increasing by 1 to 337 branches in Q1'2022, from 336 in Q1'2021, with Equity Bank Rwanda contributing 1 additional branch,
- The faster 27.8% growth in loans as compared to the 14.0% growth in customer deposits led to an increase in the Loans to deposit ratio to 69.2% from 61.7% in Q1'2021,
- Gross Non-Performing Loans (NPLs) reduced by 6.5% to Kshs 59.4 bn in Q1'2022, from Kshs 63.5 bn recorded in Q1'2021. The group's asset quality improved, with the NPL ratio declining to 9.0% in Q1'2022, from 12.1% recorded in Q1'2021, attributable to the 6.5% 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 Micro-Small and Medium-sized Enterprises (MSMEs) and Agriculture, which contributed 9.1% and 7.6%, respectively. The group's Tanzanian subsidiary recorded the highest NPL ratio, coming in at 24.7% in Q1'2022, with Equity Bank Kenya recording an NPL ratio of 8.4% in Q1'2022,

- The NPL coverage improved to 66.0%, from 55.5% in Q1’2021 on the back of a 3.0% increase in the general Loan Loss Provisions to Kshs 28.3 bn, from Kshs 27.5 bn in Q1’2021 coupled with the 6.5% decline in the Gross Non-Performing Loans, an indication of sufficient provisioning,
- Shareholders’ funds grew by 24.9% to Kshs 167.2 bn in Q1’2022, from Kshs 133.9 bn in Q1’2021, mainly supported by a 23.9% growth in retained earnings to Kshs 157.8 bn, from Kshs 127.4 bn in Q1’2021,
- Equity Group is currently sufficiently capitalized with a core capital to risk-weighted assets ratio of 13.9%, 3.4% points above the minimum statutory requirement of 10.5%. In addition, the total capital to risk-weighted assets ratio was 18.7%, exceeding the minimum statutory requirement of 14.5% by 4.2% points. Adjusting for IFRS 9, the core capital to risk-weighted assets stood at 13.9% while total capital to risk-weighted assets came in at 18.7%, and,
- The bank currently has a Return on Average Assets (ROaA) of 3.7%, and a Return on Average Equity (ROaE) of 28.7%.

<u>Key Take-Outs:</u>

1. 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 27.7% to the bank’s total profitability and 43.8% to the group’s total asset base. However, given the high NPL levels in the group’s Tanzania subsidiary of 24.7%, the group will need to improve its credit assessment in the country to bring down the high NPL ratio. Cumulatively, the group’s subsidiaries, excluding Equity Bank Kenya Ltd, recorded a 87.5% growth in their Profit after Tax (PAT) to Kshs 4.5 bn, from Kshs 2.4 bn in Q1’2021, with the DRC subsidiary, Equity BCDC, recording a growth of 269.0% in their Profit After Tax to Kshs 1.4 bn in Q1’2022 from Kshs 0.4 bn in Q1’2021. Total assets in the bank’s regional subsidiaries, excluding Equity Bank Kenya Ltd, grew by 22.7% to Kshs 427.5 bn in Q1’2022, from Kshs 348.5 bn in Q1’2021, largely driven by the 33.8% growth of the subsidiaries’ loan book to Kshs 221.0 bn, from Kshs 165.2 bn recorded in Q1’2021,
2. Increased innovation and digitization have seen 97.1% of all transactions of the bank being done on alternative channels, with mobile and internet transactions taking up 84.6% 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 68.9%, 28.2% and 2.9%, respectively. This highlights the transformation of branches to handle high-value transactions. This transformation aids the bank by offering its ecosystem banking products to retail and SME clients, and,
3. The bank’s asset quality improved y/y, as evidenced by the 3.2% points decline in the NPL ratio to 9.0% in Q1’2022, from 12.1% in Q1’2021. The main sectors that contributed to the Non-Performing Loans were SMEs and Agriculture, which contributed 12.7% and 7.6%, respectively. The group’s Tanzanian subsidiary recorded the highest NPL ratio, coming in at 24.7% in Q1’2022, with Equity Bank Kenya recording an NPL ratio of 8.4% in Q1’2022. However, the group’s asset quality deteriorated q/q by 0.4% points to 9.0%, from 8.6% in FY’2021, partly attributable to the loan book’s highest exposure to the trade services sector which has continued to be constrained by increased input costs following the increased inflationary pressures in the East African Region. Should they persist, we expect impair the group’s asset quality to be impaired in the medium term.

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 56.9%, an improving loan to deposit ratio of 69.2% and a core capital to risk-weighted asset ratio of 13.9%, 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 "***Accumulate***" with a target price of Kshs 51.2 representing an upside of 12.6%, from the current price of Kshs 45.5 as of 13th May 2022, and,
- Equity Group is currently trading at a P/TBV of 0.9x and a P/E of 4.0x vs an industry average of 0.8x and 4.4x, respectively.