

The Co-operative Bank of Kenya Limited – Strong Organic Growth

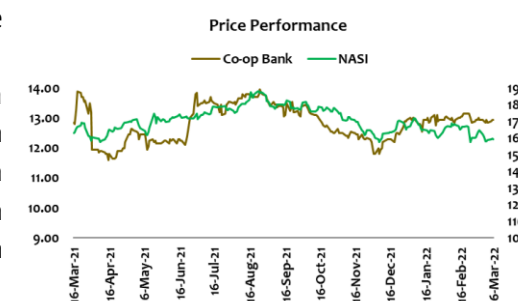
The Co-operative Bank of Kenya Limited (CBKL) reported KES 22.65Bn in profits before tax, a 58.6% y-y increase from KES 14.28Bn in FY-20. Profits after tax (PAT) surged 53.0% y-y to KES 16.54Bn from KES 10.81Bn. Growth was supported by a 12.9% improvement in net interest income (NII) and a 3.3% y-y decline in expenses. The board retained per share dividend of KES 1.00, a 35.1% payout on an EPS of 2.85. The bottom-line strong performance is pillared by the top line growth as the bank did not benefit much from decline in loan loss provisions.

We retain BUY recommendation on the counter at a value of KES 17.21, 31.9% upside compared to a volume weighted average price (VWAP) of KES 13.05 as of March 17th, 2022. The dividend yield of 7.7% pushes total return to 35.1%.

- Net interest income (NII) increased by 12.9% y-y to KES 41.04Bn from KES 36.35Bn in FY-20. The bank saw a strong Q4-21 with NII q-q growth of 25.8%. NII contribution to income improved marginally to 67.9% from 67.5% in FY-20
- Interest income was up 13.9% y-y to KES 55.65Bn from KES 48.84Bn. Income from loans and advances was KES 36.51Bn, a 9.0% y-y improvement from KES 33.50Bn driven by aggressive collection and a 8.2% growth in loan book as yields from advances remained stable at 12.2%. Returns from investments in government securities were up 26.4% y-y supported by a 14.0% growth in investment in securities while yields stabilized at 10.7%.
- Interest expenses were up 17.0% y-y to KES 14.61Bn from KES 12.49Bn. This was driven by a 21.9% jump on cost of customer deposits as customer liabilities expanded by 7.7% y-y while cost of customer deposit increased to 3.4% from 3.1% in FY-20. A 6.8% y-y thinning of borrowed funds saw other interest decline by 19.6% y-y with cost of borrowed fund constituting a large proportion of the expense line.
- Non-funded income (NFI) were up 11.0% y-y to KES 19.40Bn from KES 17.498Bn buoyed by a 18.1% y-y increase in net fees and commission income to KES 15.23Bn from KES 12.90Bn. The income line growth was supported by revenues from digital lending with the bank boasting +5.3Mn registered clients and loans worth KES 6.0Bn disbursed per month. NFI contributions marginally eased to 32.1% from 32.5%.
- Overall expenses declined by 3.3% to 38.09Bn from KES 39.40Bn with cost to income (CTI) coming down to 63.0% from 73.2% in FY-20. Loans loss provision eased 2.3% to 7.93Bn from KES 8.11Bn.
- A 3.8% decline in other operating expense saw expenses excluding provisions declined by 3.6% y-y to KES 30.16Bn from KES 31.29Bn. The dip saw CTI ex provisions ease to 49.9% from 58.1% in FY-20.
- The lender's effective tax rate (ETR) was 27.0%, up 266.5bps higher compared to an ETR of 24.7% in FY-20.

Recommendation:	BUY
Bloomberg Ticker:	COOP KN
Share Stats	
Valuation	17.21
Current Price	13.05
Upside / Downside	31.9%
3-Months Av	12.91
6-Months Av	12.77
52-Week Av	12.84
52 Week High - Low	13.95 - 11.50
Issued shares Mn	5,867.17
Free Float	35.4%
Market Cap (KES Mn)	76,566.63
Market Cap (USD Mn)	669.79
EPS (annualized)	2.85
PE	4.6x
PB	0.8x
DPS	1.00
DPS Yield	7.7%
Payout	35.1%
Total Return	39.5%

Return Performance		
Period	Co-op Bank	NASI
3-Months	6.1%	-3.6%
6-Months	-3.3%	-13.7%
Y-T-D	0.8%	-6.8%
Y-Y	2.0%	-3.5%



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Earnings Update – FY-2021

Subsidiaries Performance

- Balance sheet saw total assets increase by 8.0% y-y to KES 579.77Bn from KES 536.95Bn in FY-20. Investment in securities increase to KES 185.76Bn, a 14.0%y-y jump from KES 163.02Bn. Investments in securities shrunk by KES 8.99Bn in Q4-21 which is seen to be a shift in cash management towards growing loan book and liquidation of debt. This was supported by decline in borrowing and a drop in deposits in Q4-21 compared to Q3-21. The proportion of investments in securities to asset book increased by 32.0% from 30.4%.
 - Net loan book expanded by 8.25 y-y to KES 310.20Bn from KES 286.63Bn on growth on digital lending and improved lending to micro small and medium enterprises (MSME). Net loan book to total assets remained flat at 53.5% from 53.4% during the period.
 - Customer deposits improved to KES 407.73Bn, a 7.7% jump from KES 378.63Bn leaving advance to deposit AD ration up to 76.1% from 75.7% in FY-20.
 - The lender saw its borrowing thin by 6.8% y-y to KES 42.92Bn from KES 46.03Bn improving the debt to equity ratio to 42.6% from 50.0% in FY-20.
 - A 12.9% increase in retained earnings pushed shareholders' funds up by 9.4% to KES 100.76Bn from KES 92.05Bn in FY-20.
- Co-op Consultancy and Insurance Agency KES 803.9Mn PBT
 - Co-op Trust Investment – KES 140.4Mn PBT with AUM of KES 189.2Bn in Dec-21 vs KES 127.5Bn in Dec-20.
 - Kingdom Bank – KES 512.4Mn PBT
 - Co-op Bank South Sudan – KES 421.7Mn loss attributed to hyperinflation accounting due to currency devaluation of the South Sudan Pound.

Key ratios

- Despite improvement in asset yield, net interest margin (NIM) were flat at 8.1% as cost of funds increased to 3.3% from 3.2% in FY20.
- The reversal of profitability projections saw return on equity averaged at 17.2% in FY-21 improving from 12.5% in FY-20. Return on assets was 3.0% up from 2.2% in FY-20.
- A 15.9% y-y decline in gross non-performing loans (NPLs) aided NPL ratio down to 14.0% from a high of 18.1% in FY-20.

Outlook

- The bank remains resilient as it continues to maximize in organic growth. We expect the lender to retain its generous levels of provisions which saw them not affected by the heavy provisions seen in tier one banks in 2020.
- Digital drive will remain a key factor on growing NFI as NFI contributions remain low compared to its peers.
- The lender will remain skeptical in risk acceptance opting to invest further in investment securities while growing MSME and consumer lending through digital channels.

Income Statement (KES Mn)	FY-2020	FY-2021	%Δ Y-Y	Q3-2021	Q4-2021	%Δ Q-Q
Interest Income	48,841	55,648	13.9%	13,612	16,077	18.1%
Interest Expense	12,492	14,611	17.0%	3,778	3,705	-1.9%
NII	36,349	41,037	12.9%	9,834	12,371	25.8%
NFI	17,481	19,396	11.0%	5,407	3,666	-32.2%
Total Income	53,830	60,433	12.3%	15,240	16,037	5.2%
Provisions	8,112	7,929	-2.3%	1,887	1,884	-0.1%
Expenses	39,398	38,090	-3.3%	9,261	10,133	9.4%
Expense excl Provisions	31,286	30,161	-3.6%	7,374	8,249	11.9%
PBT	14,282	22,649	58.6%	5,957	6,168	3.5%
PAT	10,813	16,544	53.0%	4,258	4,920	15.5%
EPS	1.98	2.85	43.9%	0.72	0.87	20.8%

Balance Sheet (KES Mn)	FY-2020	FY-2021	%Δ Y-Y	Q3-2021	Q4-2021	%Δ Q-Q
Investment Securities	163,018	185,763	14.0%	11,375	(8,988)	-179.0%
Loans and Advances	286,634	310,195	8.2%	5,126	3,879	-24.3%
Total Assets	536,945	579,772	8.0%	19,879	(13,115)	-166.0%
Customer Deposit	378,630	407,726	7.7%	12,752	(12,712)	-199.7%
Borrowings	46,026	42,915	-6.8%	(589)	(925)	56.9%
Shareholders' Equity	92,048	100,746	9.4%	2,792	5,355	91.8%

NPLs KES Mn	FY-2020	FY-2021	%Δ Y-Y	Q3-2021	Q4-2021	%Δ Q-Q
Gross NPLs	59,134	49,731	-15.9%	(1,366)	250	118.3%
Total NPL	51,889	43,392	-16.4%	(1,386)	737	153.2%

Key Ratios	FY-2020	FY-2021
NII Contribution	67.5%	67.9%
NFI Contribution	32.5%	32.1%
CTI	73.2%	63.0%
CTI ex Provisions	58.1%	49.9%
Cost of Funds	3.2%	3.3%
Net Interest Margin	8.1%	8.2%
ROaA	2.2%	3.0%
ROaE	12.5%	17.2%
Gross NPL to Net Loans	18.1%	14.0%
Advance to Deposit	75.7%	76.1%
Investment to Assets	30.4%	32.0%
Loans to Assets	53.4%	53.5%
Debt to Equity	50.0%	42.6%

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Analysts' stock ratings are defined as follows:

- **Buy** – A buy rating reflects 1) An analyst has a bullish conviction on a stock 2) A 30% or greater expected return.
- **Accumulate** – An accumulate rating reflects 1) An analyst has a lesser bullish conviction on a stock 2) Expected return falls between 10% and 30%.
- **Hold** – A hold rating reflects 1) An analyst has a neutral conviction (lack of bullish or bearish conviction) on a stock 2) Expected return falls within the range of 5% to 10%.
- **Speculative Buy** – A speculative buy rating reflects 1) An analyst has a bullish conviction accompanied by a substantially higher than normal risk 2) Expected return falls above 10%.
- **Sell** – A sell rating reflects 1) An analyst has a bearish conviction on a stock 2) Expected return falls below 5%.

*Expected Return (ER) represents the sum total of both capital appreciation and the dividend yield.

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