

KINGDOM SECURITIES

KCB Group Profits Decline on Higher Expenses

KCB Group posted KES 13.58Bn profit before tax (PBT) for Q1 2023, a 1.3% drop from that of KES 14.03Bn reported in Q1 2022, being depressed by a higher interest and operating expenses that soared 67.7% and 53.3% year on year (y-y) to KES 11.55Bn and KES 23.00Bn respectively. Profits after (PAT) was 1.1% y-y down to KES 9.75Bn in Q1 2023 compared to KES 9.86Bn recorded in Q1 2022.

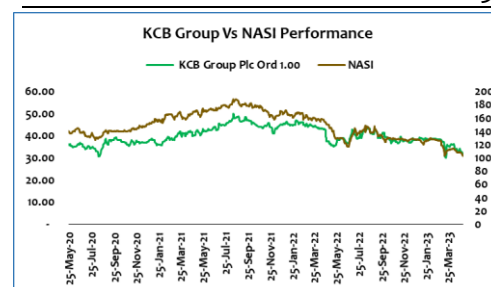
KCB Group's earnings per share (EPS) stands at 12.14, a 0.3% drop from that of 12.18 same time 2022.

We retain a BUY recommendation on the Group with a revised valuation price of KES 36.60, an 18.1% upside from the current price KES 31.00 as of 25th May 2023. The company remains strong with its subsidiary contribution of 35.0% in Q1 2023 up from 17.2% in Q1 2022.

- The performance remained supported interest income and non-funded incomes. Net interest income (NII) contribution to total income dropped from 68.0% in Q1 2022 to 59.9% in Q1 2023 on a faster growth in NFIs on what appears to be a better utilization of technology in the lending business by the bank.
- Interest income spiked 26.2% from KES 26.63Bn to KES 33.61Bn riding on interest income growths from both loans and advances and government securities.
- Interest from loans and advances went 31.4% up to KES 34.69Bn riding on a faster loan book growth of 32.6% from KES 675.48Bn to KES 928.82Bn. Yield on loans and advances were improved from 10.9% to 11.0% on what we attribute to the lifting of the interest rate capping.
- Interest from government securities moved 14.6% y-y up from KES 7.66Bn to KES 8.78Bn benefiting from an 8.5% growth on government securities book which enlarged by KES 23.28Bn from KES 274.44Bn to KES 297.72Bn. Yield on Government on Securities government securities rose from 11.2% in Q1 2022 to 12.2% taking advantage of the rate hikes that continue to affect government borrowing rates.
- Interest expense jumped 67.7% y-y to KES 11.55Bn from KES 6.89Bn in Q1 2022, being affected by a 65.5% growth on borrowings and expensive deposits especially from banking institutions whose expenses quadrupled to KES 3.65Bn in. Customer deposits became expensive rising by 36.0% y-y to KES 7.80Bn.
- Non-funded income climbed 59.2% y-y from KES 6.89Bn to KES 11.55Bn on account of a double growth in other fees and commissions especially from mobile loans and other digital transactions all of which totaled to 99.0% of all transactions.
- Operating expenses accelerated at 53.3% y-y from KES 15.0Bn in Q1 2022 to KES 23.00Bn pushed by loan loss provisions, staff costs and other operating expenses which the lender partly attributes to its regional growth.
- Loan loss provisions nearly doubled at 98.4% from KES 2.08Bn to KES 4.12Bn driven by credit risk growth and forex devaluation in Kenya at the backdrop of a challenging economic environment.

KCB Group plc Earnings Update – Q1 2023

Bloomberg Ticker	KNCB KE
Recommendation	BUY
Share Statistics	
Implied Fair Value	36.60
Current Price (KES)	31.00
Upside/Downside	18.1%
3 Months Avr	33.92
6 Months Avr	35.80
12 Months Avr	37.84
52 Week High - Low	43.50 - 28.50
Issued shares (Mn)	3,213.46
Market Cap (KES Mn)	99,617.35
Market Cap (USD Mn)	871.65
EPS	12.14
PE	2.6
Bvps	57.2
PB	0.5



NNI + 11.8% Y/Y

Provisions + 98.4% Y/Y

Opex. +53.3% Y/Y

Opex Exc. Loan loss prov. + 46.1% y-y

PBT - 1.3% Y/Y

PAT -1.1% Y/Y

Govt. Securities + 8.5% Y/Y

Loans + 31.9% Y/Y

Deposits + 4.5% Y/Y

Shareholder's Funds +16.9% Y/Y

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- Staff costs increased by 39.3% from KES 6.72Bn to KES 9.36Bn on impact of the acquisition of the TMB bank in DRC as well as salary increments and staff bonus.
- Other operating expenses ballooned from KES 4.30Bn in Q1 2022 to KES 7.43Bn as the to cater for the general expansion of the Group.

Balance sheet

- Total assets expanded by 39.7% y-y from KES 1,166.91Bn in Q1 2022 to KES 1,630.60Bn in Q1 2023 on accelerated growths in loans and advances plus government securities. Loans and advances were 31.9% y-y up from KES 704.35Bn to KES 928.82Bn in Q1 2023.
- Shareholders' funds rose 16.9% y-y from KES 183.72Bn to KES 214.85Bn on growths from retained earnings which statutory reserves which improved to KES 24.85Bn in Q1 2023 from that of KES 7.37Bn. We view the statutory reserve growth as a deliberate move to grow the Group's capital ratio buffers far above the regulatory requirements.
- The Group's borrowings almost doubled from KES 37.84Bn in Q1 2022 to KES 62.64Bn in Q1 2023 to support the growing loan book.

Key Ratios

- Growth in borrowings and expensive deposits depressed the net interest margin from 7.6% in Q1 2022 down to 6.2% by closure of Q1 2023. This also saw the cost of funds move from 3.0% in Q1 2022 to 3.6% in Q1 2023.
- Capital reallocation saw liquidity ratio improve from 36.9% in Q1 2022 to 43.7% in Q1 2023.
- Return on average assets (ROaA) receded on being affected by a faster growth in assets in relation to overall net revenue. Return on average equity (ROaE) dropped to 2.5% in Q1 2023 in comparison to 3.4% for Q1 2022 on account of a faster growth in average equity compared to net revenue.
- Non-performing loans (NPLs) remained high escalating to 17.5% in Q1 2023 from that of 17.5%, still above the market average of 14.0% as of February 2023. NPLs was affected by loans under manufacturing, transport and communication from its Kenyan unit.

P&L (KES Mn)	Q1-2021	Q1-2022	Q1-2023	%Δ Y-Y
Interest Income	21,970	26,628	33,613	26.2%
Interest Expense	5,243	6,888	11,553	67.7%
NII	16,726	19,740	22,060	11.8%
NFI	6,314	9,292	14,790	59.2%
Total Income	23,040	29,031	36,850	26.9%
Loan Loss Provisions	2,861	2,075	4,118	98.4%
Operating Expense	13,922	14,999	22,996	53.3%
Opex Excl Provisions	11,061	12,924	18,878	46.1%
PBT	9,118	14,032	13,854	-1.3%
PAT	6,376	9,856	9,753	-1.1%
EPS	7.02	12.18	12.14	-0.3%

Balance Sheet (KES Mn)	Q1-2021	Q1-2022	Q1-2023	%Δ Y-Y
Investments	212,127	274,443	297,719	8.5%
Loans and Advances	597,110	704,366	928,824	31.9%
Total Asset	977,523	1,166,908	1,630,604	39.7%
Customer Deposit	749,414	845,817	1,196,587	41.5%
Shareholders' Fund	147,508	183,723	214,846	16.9%

Ratios	Q1-2021	Q1-2022	Q1-2023
NII % of Total Income	72.6%	68.0%	59.9%
NFI % of Total Income	27.4%	32.0%	40.1%
CTI	60.4%	51.7%	62.4%
CTI exc Provision	48.0%	44.5%	51.2%
Yield on Advances	10.6%	10.9%	11.0%
Yield on Government Securities	11.3%	11.2%	12.2%
Cost of Funds	2.6%	3.0%	3.6%
Net Interest Margins	7.8%	7.6%	6.2%
ROaA	2.6%	3.4%	3.0%
ROaE	17.6%	21.9%	19.0%
Gross NPL to Net Loans	14.7%	16.7%	16.7%
AD Ratio	79.7%	83.3%	77.6%
Investments Securities to Assets	21.7%	23.5%	18.3%
Advances to Assets	61.1%	60.4%	57.0%

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Recommendation Guide:

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 of both capital appreciation and the dividend yield.

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