ABSA Bank Kenya Plc – H1’2022
26th August 2022

Below is a summary of ABSA Bank’s H1’2022 performance;

Balance Sheet Items	H1’2021	H1’2022	y/y change
Government Securities	121.3	120.8	(0.4%)
Net Loans and Advances	218.9	261.5	19.5%
Total Assets	**398.2**	**445.3**	**11.8%**
Customer Deposits	263.9	281.7	6.7%
Deposits per Branch	3.1	3.4	8.0%
Total Liabilities	346.2	389.0	12.4%
Shareholder's Funds	**52.0**	**56.2**	**8.2%**

Balance sheet ratios	H1’2021	H1’2022	% point change
Loan to Deposit Ratio	82.9%	92.9%	10.0%
Return on average equity	19.3%	21.4%	2.1%
Return on average assets	2.3%	2.7%	0.4%

Income Statement Items	H1’2021	H1’2022	y/y change
Net Interest Income	12.0	14.4	20.3%
Net non-Interest Income	5.8	6.5	10.8%
Total Operating income	**17.8**	**20.9**	**17.2%**
Loan Loss provision	(1.9)	(3.0)	52.2%
Total Operating expenses	(9.9)	(11.8)	19.2%
Profit before tax	**7.9**	**9.1**	14.7%
Profit after tax	**5.6**	**6.3**	13.0%
Core EPS	**1.0**	**1.2**	**13.0%**

Income statement ratios	H1’2021	H1’2022	% point change
Yield from interest-earning assets	9.2%	9.7%	0.5%
Cost of funding	2.8%	2.7%	(0.1%)
Net Interest Margin	7.0%	7.6%	0.6%
Cost to Income	55.5%	56.4%	0.9%
Cost to Assets	2.0%	2.0%	0.0%
Net Interest Income as % of operating income	67.2%	69.0%	1.8%
Non-Funded Income as a % of operating income	32.8%	31.0%	(1.8%)

Capital Adequacy Ratios	H1’2021	H1’2022	% Points change
Core Capital/Total Liabilities	17.7%	18.1%	0.4%
Minimum Statutory ratio	8.0%	8.0%	0.0%
Excess	**9.7%**	**10.1%**	**0.4%**
Core Capital/Total Risk Weighted Assets	14.7%	14.0%	(0.7%)
Minimum Statutory ratio	10.5%	10.5%	0.0%
Excess	**4.2%**	**3.5%**	**(0.7%)**
Total Capital/Total Risk Weighted Assets	17.3%	16.4%	(0.9%)
Minimum Statutory ratio	14.5%	14.5%	0.0%
Excess	**2.8%**	**1.9%**	**(0.9%)**
Liquidity Ratio	38.1%	30.3%	(7.8%)
Minimum Statutory ratio	20.0%	20.0%	0.0%

Excess	**18.1%**	**10.3%**	**(7.8%)**
Adjusted Core Capital/Total Liabilities	**17.8%**	**18.2%**	**0.4%**
Adjusted Core Capital/Total RWA	**14.8%**	**14.0%**	**(0.8%)**
Adjusted Total Capital/Total RWA	**17.4%**	**16.5%**	**(0.9%)**

Income Statement

- Core earnings per share increased by 13.0% to Kshs 1.2 in H1’2022, from Kshs 1.0 in H1’2021, driven by a 17.2% increase in total operating income to Kshs 20.9 bn, from Kshs 17.8 bn recorded in H1’2021. However, the growth was weighed down by the 19.2% increase in total operating expenses, to Kshs 11.8 bn, from Kshs 9.9 bn recorded in H1’2021,
- Total operating income rose by 17.2% to Kshs 20.9 bn, from Kshs 17.8 bn recorded in H1’2021 driven by a 20.3% increase in Net Interest Income (NII) to Kshs 14.4 bn, from Kshs 12.0 bn in H1’2021, coupled with a 10.8% gain in Non-Funded Income (NFI) to Kshs 6.5 bn, from Kshs 5.8 bn in H1’2021,
- Interest income grew by 21.3% to Kshs 18.4 bn in H1’2022, from Kshs 15.2 bn in H1’2021, mainly driven by a 21.2% increase in interest income from loans and advances to Kshs 13.3 bn, from Kshs 11.0 bn in H1’2021, coupled with a 11.1% increase in interest income from Government securities to Kshs 4.6 bn, from Kshs 4.1 bn in H1’2021. The Yield on Interest-Earning Assets (YIEA) increased to 9.7%, from 9.2% recorded in H1’2021, attributable to the faster 12.7% growth in trailing interest income which outpaced the 6.8% growth in the average Interest-Earning Assets (IEA). Trailing Interest Income refers to the performance of the interest income for the past 12 consecutive months,
- Interest expenses increased by 25.1% to Kshs 4.0 bn, from Kshs 3.2 bn in H1’2021, following a 12.4% increase in interest expense on customer deposits to Kshs 3.3 bn, from Kshs 2.9 bn in H1’2021. The bank was able to mobilize cheaper deposits with the Cost of funds (COF) marginally declining by 0.1% points to 2.7%, from 2.8% in H1’2021, owing to the slower 4.7% increase in the trailing interest expenses compared to the 6.4% growth in 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) increased to 7.6% from 7.0% in H1’2021, attributable to the faster 15.4% increase in trailing net interest income, which outpaced the 11.7% growth in interest earning assets,
- Non-Funded Income (NFI) increased by 10.8% to Kshs 6.5 bn, from Kshs 5.8 bn in H1’2021, mainly driven by a 44.2% increase in Foreign Exchange trading income to Kshs 3.0 bn, from Kshs 2.1 bn in H1’2021, coupled with a 4.5% increase in other fees and income to Kshs 2.3 bn, from Kshs 2.2 bn in H1’2021. Notably, the bank’s total fees and commissions declined by 2.4% to Kshs 3.0 bn, from Kshs 3.1 bn in H1’2021. The revenue mix shifted to 69:31, funded to non-funded income, from 67:33, funded to non-funded income recorded in H1’2021, attributable to the faster 20.3% increase in NII compared to the 10.8% increase in NFI,
- Total operating expenses increased by 19.2% to Kshs 11.8 bn in H1’2022, from Kshs 9.9 bn in H1’2021, mainly attributable to a 52.2% increase in Loan Loss Provisions (LLPs) to Kshs 3.0 bn, from Kshs 2.0 bn in H1’2021, coupled with an 8.9% increase in staff costs to Kshs 4.8 bn from Kshs 4.4 bn in H1’2021. The increased provisioning level was due to the slowdown in business activity in H1’2022 on the back of the elevated inflationary pressures,
- Cost to Income Ratio (CIR) deteriorated to 56.4%, from 55.5% in H1’2021, owing to the 19.2% growth in total operating expenses, which outpaced the 17.2% increase in total operating income. Without LLP, the cost to income ratio improved to 42.3%, from 44.6% in H1’2021, an indication of improved efficiency,
- Profit before tax and exceptional items increased by 14.7% to Kshs 9.1 bn in H1’2022, from Kshs 7.9 bn in H1’2021. Similarly, profit after tax increased by 13.0% to Kshs 6.3 bn in H1’2022, from Kshs 5.6 bn in H1’2021 with the effective tax rate increasing to 30.9%, from 29.9% in H1’2021, and,

- The Board of Directors recommended an interim Dividend Per Share (DPS) of Kshs 0.2, translating to a total dividend payout of Kshs 1.1 bn. At the current price of Kshs 11.7, this translates to a dividend yield of 1.7%.

Balance Sheet

- The balance sheet recorded an expansion as total assets grew by 11.8% to Kshs 445.3 bn in H1’2022, from Kshs 398.2 bn in H1’2021. This growth was largely driven by a 19.5% growth in the loan book to Kshs 261.5 bn, from Kshs 218.9 bn in H1’2021. However, investments in government and other securities decreased by 0.4% to Kshs 120.8 bn, from Kshs 121.3 bn in H1’2021, weighing on the growth. Placements in other banks also declined by 33.9% to Kshs 3.4 bn, from Kshs 5.1 bn recorded in H1’2021,
- Total liabilities rose by 12.4% to Kshs 389.0 bn, from Kshs 346.2 bn in H1’2021, driven by a 6.7% increase in customer deposits to Kshs 281.7 bn, from Kshs 263.9 bn in H1’2021. Placements by other banking institutions also increased by 1.3% increase to Kshs 6.8 bn, from Kshs 6.7 bn in H1’2021. Deposits per branch rose by 8.0% to Kshs 3.4 bn, from Kshs 3.1 bn in H1’2021 with the number of branches decreasing by 1 to 83 from 84 in H1’2021,
- The faster 19.5% growth in loans compared to the 6.7% increase in customer deposits led to an increase in the loans to deposit ratio to 92.9%, from 82.9% recorded in H1’2021. Key to note, this is the highest loan to deposit ratio the bank has recorded since Q1’2017, when the loan to deposit ratio came in at 92.8%, an indication that the bank has resumed lending in a recovering economy,
- Gross Non-Performing Loans (NPLs) increased by 7.9% to Kshs 19.8 bn in H1’2022, from Kshs 18.3 bn recorded in H1’2021. However, the NPL ratio declined to 7.1%, from 7.9% recorded in H1’2021. The asset quality improvement is attributable to the faster 19.5% growth in Gross loans, compared to the relatively slower 7.9% increase in Gross Non-Performing Loans (NPLs). overall, the improved asset quality was attributable to the continued economic improvement. On the other hand, the NPL coverage increased to 78.5% in H1’2022, from 70.9% in H1’2021, owing to the faster 23.8% increase in General Loan Loss Provisions, which outpaced the 7.9% growth in Gross Non-Performing Loans (NPLs), an indication of modest provisioning,
- Shareholders’ funds increased by 8.2% to Kshs 56.2 bn, from Kshs 52.0 bn recorded in H1’2021. The increase is attributable to the 12.1% increase in Retained earnings to Kshs 54.0 bn, from Kshs 48.1 bn in H1’2021,
- ABSA Bank Kenya is currently sufficiently capitalized with a core capital to risk-weighted assets ratio of 14.0%, 3.5% points above the 10.5% statutory requirement. In addition, the total capital to risk-weighted assets ratio was 16.4%, exceeding the 14.5% statutory requirement by 1.9% points. Adjusting for IFRS 9, the core capital to risk-weighted assets stood at 14.0% while total capital to risk-weighted assets came in at 16.5%, and,
- The bank currently has a Return on Average Assets (ROaA) of 2.7%, and a Return on Average Equity (ROaE) of 21.4%.

Key Take-Outs:

1. **Improvement in Asset Quality** - The bank’s asset quality improved, with the NPL ratio decreasing to 7.1% in H1’2022, from 7.9% in H1’2021, owing to the faster 19.5% growth in Gross Loans, compared to the relatively slower 7.9% increase in Gross Non-Performing Loans (NPLs). We note that the NPL ratio has continued to decline having reduced by 0.5% points from 7.6% recorded in Q1’2022 mainly attributable to the improving business environment, and,
2. **Modest Provisioning –** As the NPLs increase, the group has continued to increase its provisioning levels with the NPL coverage coming in at 78.5% in H1’2022, an increase from the 76.2% and 70.9% recorded in

in Q1’H1’2021, respectively. This points towards modest provisioning by the bank amidst the tough operating environment on the back of the elevated cost of living.

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

I. **Diversification** - This is expected to reduce the bank’s reliance on interest income as well as increasing the bottom line. It has continued to grow its product offerings to include business lines such as to Banc-assurance, Investment banking advisory and Asset Management which will continue growing the Non-Funded Income (NFI). The bank has also diversified in its digital offerings especially after the COVID-19 leading to 90.0% of all transactions happening outside. The uptake of “Timiza” which is a digital banking App, has also accelerated leading to higher Non-Interest Income.

Valuation Summary

- We are of the view that ABSA Bank Kenya is an “***BUY***” with a target price of Kshs 17.2, representing an upside of 46.6%, from the current price of Kshs 11.7 as of 26th August 2022, inclusive of a dividend yield of 10.7%,
- ABSA Bank Kenya is currently trading at a P/TBV of 1.0x and a P/E of 5.5x vs an industry average of 0.9x and 3.8x, respectively.