Cytonn INVESTMENTS

NCBA Group– H1'2024
22nd August, 2024

Below is a summary of NCBA Group's H1'2024 performance:

Balance Sheet	H1'2023 (Kshs bn)	H1'2024 (Kshs bn)	y/y change
Net Loans and Advances	292.4	309.7	5.9%
Kenya Government Securities	202.3	182.6	(9.8%)
Total Assets	**660.3**	**689.1**	**4.4%**
Customer Deposits	516.6	528.9	2.4%
Deposits Per Branch	4.8	4.6	(5.6%)
Total Liabilities	572.0	587.7	2.7%
Shareholders' Funds	**88.3**	**101.4**	**14.8%**

Key Ratios	H1'2023	H1'2024	% point change
Loan to Deposit ratio	56.6%	58.6%	2.0%
Government Securities to Deposits ratio	39.2%	34.5%	(4.6%)
Return on Average Equity	18.2%	23.1%	4.9%
Return on Average Assets	2.4%	3.2%	0.8%

Income Statement	H1'2023 (Kshs bn)	H1'2024 (Kshs bn)	y/y change
Net interest Income	17.2	16.5	(4.4%)
Net non-interest income	13.8	14.9	7.9%
Total Operating income	**31.0**	**31.4**	**1.1%**
Loan loss provision	4.4	2.7	(38.3%)
Total Operating expenses	**18.7**	**19.2**	**2.8%**
Profit before tax	12.4	12.2	(1.6%)
Profit after tax	**9.3**	**9.8**	**5.0%**
Core EPS	**5.7**	**6.0**	**5.0%**
Dividend Per Share	**1.75**	**2.25**	**28.6%**
Dividend Payout ratio	**30.8%**	**37.8%**	**7.0%**
Dividend Yield (Annualized)	**9.2%**	**10.8%**	**1.6%**

Income Statement Ratios	H1'2023	H1'2024	y/y change
Yield from interest-earning assets	10.5%	12.5%	2.0%
Cost of funding	4.7%	7.1%	2.3%
Net Interest Margin	6.0%	5.8%	(0.2%)
Net Interest Income as % of operating income	55.5%	52.5%	(3.0%)
Non-Funded Income as a % of operating income	44.5%	47.5%	3.0%
Cost to Income Ratio	60.2%	61.2%	1.0%
Cost to Income without LLP	46.0%	52.6%	6.6%

Capital Adequacy Ratios	H1'2023	H1'2024	% points change
Core Capital/Total Liabilities	16.7%	18.8%	2.1%
Minimum Statutory ratio	8.0%	8.0%	
Excess	**8.7%**	**10.8%**	**2.1%**
Core Capital/Total Risk Weighted Assets	17.9%	19.9%	2.0%
Minimum Statutory ratio	10.5%	10.5%	
Excess	**7.4%**	**9.4%**	**2.0%**
Total Capital/Total Risk Weighted Assets	18.0%	19.9%	2.0%
Minimum Statutory ratio	14.5%	14.5%	
Excess	**3.5%**	**5.4%**	**2.0%**
Liquidity Ratio	54.7%	53.6%	(1.1%)
Minimum Statutory ratio	20.0%	20.0%	

Excess	**33.1%**	**31.6%**	**(1.5%)**

Income Statement

- Core earnings per share grew by 5.0% to Kshs 6.0, from Kshs 5.7 in H1’2023, driven by the 1.1% increase in total operating income to Kshs 31.4 bn, from Kshs 31.0 bn in H1’2023. However, the performance was weighed down by a 2.8% increase in total operating expenses to Kshs 19.2 bn from Kshs 18.7 bn in H1’2023,
- The 1.1% increase in total operating income was mainly driven by a 7.9% increase in Non Interest Income (NFI) to Kshs 14.9 bn from Kshs 13.8 bn in H1’2023, which outpaced the 4.4% decline in Net Interest Income (NII) to Kshs 16.5 bn, from Kshs 17.2 bn in H1’2023,
- Interest income grew by 25.4% to Kshs 38.1 bn from Kshs 30.3 bn in H1’2023, mainly driven by a 41.4% growth in interest income from loans and advances to Kshs 23.3 bn from Kshs 16.5 bn in H1’2023, coupled with a 211.7% increase in interest income from deposits and placements to Kshs 1.7 bn, from Kshs 0.5 bn in H1’2023. As such, the Yield on Interest-Earning Assets (YIEA) increased to 12.5% from 10.5% recorded in H1’2023, mainly attributable to the faster 26.2% growth in Trailing interest income compared to a 5.9% increase in average interest earning assets to Kshs 584.8 bn, from Kshs 552.0 bn in H1’2023,
- Interest expenses rose by 64.5% to Kshs 21.6 bn from Kshs 13.1 bn in H1’2023, mainly driven by a 67.2% increase in interest expense on customer deposits to Kshs 20.3 bn from Kshs 12.1 bn in H1’2023, coupled with a 34.9% increase in interest expense from placements to Kshs 0.9 bn, from Kshs 0.7 bn in H1’2023. Consequently, Cost of funds (COF) increased by 2.4% points to 7.1% from 4.7% recorded in H1’2023, owing to a faster 58.1% increase in Trailing interest expense to Kshs 39.1 bn from Kshs 24.7 bn recorded in H1’2023, compared to a 5.7% increase in average interest bearing liabilities to Kshs 552.1 bn from Kshs 522.1 bn in H1’2023.Trailing interest expense refers to the performance of the interest expense for the past 12 consecutive months. Net Interest Margin (NIM) decreased by 0.2% points to 5.8% in H1’2024, from 6.0% in H1’2023, attributable to a slower 2.3% increase in trailing net interest income to Kshs 33.8 bn from Kshs 33.1 bn recorded in H1’2023, which was outpaced the 5.9% growth in average interest earning assets,
- Non-Funded Income (NFI) increased by 7.9% to Kshs 14.9 bn from Kshs 13.8 bn in H1’2023, mainly driven by a 11.5% increase in total fees income to Kshs 9.3 bn, from Kshs 8.3 bn in H1’2023, which outpaced the 14.6% decline in forex trading income to Kshs 3.7 bn , from Kshs 4.3 bn in H1’2023, highlighting the bank’s decreased foreign exchange margins. The revenue mix shifted to 52:48 from 55:45 in H1’2023, for the funded to Non-funded income owing to the 7.9% growth in Non Funded Income compared to a 4.4% decrease in the Funded Income,
- Total operating expenses increased by 2.8% to Kshs 19.2 bn from Kshs 18.7 bn in H1’2023, driven by 17.7% increase in staff costs to Kshs 6.9 bn from Kshs 5.8 bn recorded in Q1’2023, coupled with a 14.0% increase in other operating expenses to Kshs 9.6 bn, from Kshs 8.4 bn recorded in H1’2023, which outpaced the 38.3% decrease in loan loss provisions to Kshs 2.7 bn, from Kshs 4.4 bn recorded in H1’2023. The decrease in provisioning is partly attributable to reducing credit risk as a result improved economic environment as evidenced by the average H1’2024 Purchasing Managers Index (PMI) of 50.0, up from an average of 48.7 in H1’2023,
- Cost to Income Ratio (CIR) increased by 1.0% points to 61.2% from 60.2% in H1’2023, owing to the faster 2.8% growth in total operating expenses, which outpaced the 1.1% growth in total operating income. Notably, CIR without LLP increased by 6.6% points to 52.6% from 46.0% recorded in H1’2023, and,
- Profit before tax decreased by 1.6% to Kshs 12.2 bn in H1’2024, from Kshs 12.4 bn in H1’2023, with effective tax rate decreasing to 19.3% in H1’2024, from 24.4% in H1’2023, leading to a 5.0% increase in profit after tax to Kshs 9.8 bn in H1’2024, from Kshs 9.3 bn in H1’2023.

Balance Sheet

- The balance sheet recorded an expansion as total assets grew by 4.4% to Kshs 689.1 bn, from Kshs 660.3 bn in

H1’2024, mainly driven by a 5.9% growth in net loans and advances to Kshs 309.7 bn, from 292.4 bn in H1’2023, coupled with a 23.6% increase in financial investments Kshs 36.3 bn, from Kshs 29.3 bn in H1’2023, which outpaced the 9.8% decline in investment in government securities to Kshs 182.6 bn, from Kshs 202.3 bn in H1’2023,

- Total liabilities rose by 2.7% to Kshs 587.7 bn from Kshs 572.0 bn in H1’2024, driven by a 2.4% growth in customer deposits to Kshs 528.9 bn, from Kshs 516.6 bn in H1’2023, coupled with a 139.6% increase in borrowings to 9.5 bn from Kshs 4.0 bn recorded in H1’2023, which outpaced the 19.5% decrease in placements to Kshs 20.2 bn, from Kshs 25.0 bn in H1’2023. With 116 branches countrywide, compared to 107 branches in H1’2023, deposits per branch decreased by 5.6% to Kshs 4.6 bn, from Kshs 4.8 bn in H1’2023,
- The faster 5.9% growth in loans as compared to the 2.4% growth in customer deposits led to an increase in the loan to deposits ratio to 58.6%, from 56.6% in H1’2023,
- The bank’s Asset Quality improved, with Gross NPL ratio decreasing to 12.2% in H1’2024, from 13.4% in H1’2023, attributable to the 4.1% decrease in Gross non-performing loans to Kshs 40.9 bn, from Kshs 42.6 bn in H1’2023, compared to the 5.4% increase in gross loans to Kshs 334.1 bn, from Kshs 317.0 bn recorded in H1’2023,
- General Provisions (LLP) decreased by 14.1% to Kshs 13.5 bn in H1’2024 from Kshs 15.7 bn in H1’2023. The NPL coverage increased to 59.8% in H1’2024, from 57.8% in H1’2023, attributable to the 4.1% decrease in gross non-performing loans, which outpaced the 22.2% increase in interest in suspense to Kshs 11.0 bn, from Kshs 9.0 bn in H1’2023,
- Shareholders’ funds increased by 14.8% to Kshs 101.4 bn in H1’2024, from Kshs 88.3 bn in H1’2023, supported by a 23.3% increase in retained earnings to Kshs 74.7 bn, from Kshs 60.6 bn in H1’2023,
- NCBA Bank remains capitalized with a core capital to risk-weighted assets ratio of 19.9%, 9.4% points above the statutory requirement of 10.5%. In addition, the total capital to risk-weighted assets ratio came in at 19.9%, exceeding the statutory requirement of 14.5% by 5.4% points, and,
- The bank currently has a Return on Average Assets (ROaA) of 3.2%, and a Return on Average Equity (ROaE) of 23.1%.

Key Take-Outs:

1. **Increased earnings -** Core earnings per share (EPS) grew by 5.0% to Kshs 6.0, from Kshs 5.7 in H1’2023, driven by the 1.1% growth in total operating income to Kshs 31.4 bn, from Kshs 31.0 bn in H1’2023.
2. **Improved asset quality –** The bank’s gross NPL ratio decreased to 12.2% in H1’2024, from 13.4% in H1’2023, attributable to the 4.1% decrease in Gross non-performing loans to Kshs 40.9 bn, from Kshs 42.6 bn in H1’2023, compared to the 5.4% increase in gross loans to Kshs 334.1 bn, from Kshs 317.0 bn recorded in H1’2023,
3. **Reduced Provisioning** - On the back of reduced credit risk occassioned by improving business environment, the bank decreased its provisions holdings meant to cover for anticipated losses in the future, with its general provisions decreasing by 14.1% to Kshs 13.5 bn, from Kshs 15.7 bn recorded in H1’2023. Further, loan loss provisions expense reduced by 38.3% to Kshs 2.7 bn, from Kshs 4.4 bn recorded in H1’2023.
4. **Increased dividends-** Dividends per share increased by 28.6% to Kshs 2.25 in H1’2024, from Kshs 1.75 in H1’2023 translating to an annualized dividend yield of 10.8% and a dividend payout ratio of 37.8% in H1’2024 compared to a dividend yield of 9.2% and a dividend payout ratio of 30.8% in H1’2023.

Going forward, the factors that would drive the bank’s growth would be:

- **Digital transformation**. The lender has capitalized on digital innovation for service delivery over the past years to improve its operational efficiency, which has been a key factor in its financial performance. In March 2024, the lender disclosed that they had disbursed a total of Kshs 930.0 bn via digital banking avenues, including Fuliza, Mshwari and Loop, remaining a market leader in digital lending.

- **Revenue diversification**. The lender has also capitalized on revenue diversification and increasing the bottom line contribution of all the business lines. Notably, subsidiary contribution to group’s profitability has increased over the period, standing at Kshs 4.0 bn in FY’2023. Further, the planned 100.0% acquisition of AIG Kenya Insurance is set to increase the non-funded revenue base more.

Valuation Summary

- We are of the view that NCBA Group is a “buy” with a target price of Kshs 52.7 representing an upside of 25.5%, from the current price of 42.0 as of 23rd August 2024, inclusive of a dividend yield of 10.8%.

- NCBA group is currently trading at a P/TBV of 0.8x and a P/E of 3.2x vs an industry average of 0.8x and 3.7x respectively