

Below is a summary of HF Group's Q1'2025 performance:

Balance Sheet Items	Q1'2024	Q1'2025	y/y change
Government Securities	38.1	38.9	2.0%
Net Loans and Advances	10.1	20.4	102.2%
Total Assets	62.3	73.4	17.9%
Customer Deposits	43.8	50.1	14.5%
Deposits/Branch	2.0	2.3	14.5%
Total Liabilities	53.3	57.2	7.4%
Shareholders' Funds	9.0	16.2	79.6%

Balance Sheet Ratios	Q1'2024	Q1'2025	% y/y change
Loan to Deposit Ratio	87.1%	77.6%	(9.6%)
Government Securities to Deposit Ratio	23.1%	40.7%	17.7%
Return on average equity	5.1%	5.6%	0.5%
Return on average assets	0.8%	1.0%	0.3%

Income Statement (Kshs Bn)	Q1'2024	Q1'2025	y/y change
Net Interest Income	0.7	1.0	46.1%
Net non-Interest Income	0.39	0.42	9.9%
Total Operating income	1.1	1.4	33.0%
Loan Loss provision	(0.1)	(0.1)	(7.9%)
Total Operating expenses	(0.9)	(1.1)	19.1%
Profit before tax	0.2	0.3	112.1%
Profit after tax	0.2	0.3	118.1%
Core EPS	1.3	0.1	(89.3%)

Income Statement Ratios	Q1'2024	Q1'2025	y/y change
Yield from interest-earning assets	11.4%	12.2%	0.8%
Cost of funding	6.1%	7.1%	1.0%
Net Interest Spread	5.3%	5.1%	(0.3%)
Net Interest Margin	5.4%	5.4%	0.1%
Cost of Risk	10.3%	7.1%	(3.2%)
Net Interest Income as % of operating income	63.7%	70.0%	6.3%
Non-Funded Income as a % of operating income	36.3%	30.0%	(6.3%)
Cost to Income Ratio	85.1%	76.2%	(8.9%)
Cost to Income Ratio (without LLP)	74.8%	69.1%	(5.7%)

Capital Adequacy Ratios	Q1'2024	Q1'2025	% points change
Core Capital/Total Liabilities	4.5%	17.6%	13.1%
Minimum Statutory ratio	8.0%	8.0%	0.0%
Excess	(3.5%)	9.6%	13.1%
Core Capital/Total Risk Weighted Assets	5.2%	21.3%	16.1%
Minimum Statutory ratio	10.5%	10.5%	0.0%
Excess	(5.3%)	10.8%	16.1%
Total Capital/Total Risk Weighted Assets	8.8%	24.3%	15.5%
Minimum Statutory ratio	14.5%	14.5%	0.0%
Excess	(5.7%)	9.8%	15.5%
Liquidity Ratio	24.9%	45.1%	20.2%
Minimum Statutory ratio	20.0%	20.0%	0.0%
Excess	4.9%	25.1%	20.2%

Income Statement

- Core earnings per share declined by 89.3% to Kshs 0.1, from Kshs 1.3 in Q1'2024, mainly driven by a 33.0% increase in Total Operating Income to Kshs 1.4 bn from Kshs 1.1 bn in Q1'2024, which outpaced a 19.1% increase in total operating expenses to Kshs 1.1 bn from Kshs 0.9 bn in Q1'2024,
- The total operating income increased by 33.0% to Kshs 1.4 bn from Kshs 1.1 bn in Q1'2024, mainly driven by a 46.1% growth in Net Interest Income (NII) to Kshs 1.0 bn, from Kshs 0.7 bn in Q1'2024, coupled with the 9.9% increase in Non- Interest Income (NFI) to Kshs 0.42 bn from Kshs 0.39 bn in Q1'2024,
- Interest income grew by 18.6% to Kshs 1.8 bn from Kshs 1.5 bn in Q1'2024, mainly driven by an 87.4% growth in interest income from government securities to Kshs 0.6 bn, from Kshs 0.3 bn in Q1'2024, coupled with a 2.3% increase in interest income from loans and advances to Kshs 1.19 bn, from Kshs 1.16 bn in Q1'2024. As such, the Yield on Interest-Earning Assets (YIEA) increased by 0.8% points to 12.2% from 11.4% recorded in Q1'2024, attributable to a faster 20.7% Increase in trailing interest income to Kshs 6.7 bn, from Kshs 5.5 bn in Q1'2024 compared to the slower 13.1% growth in average interest earning assets to Kshs 54.8 bn, from Kshs 48.4 bn in Q1'2024,
- Interest expenses declined by 3.7% to Kshs 0.80 bn from Kshs 0.84 bn in Q1'2024, mainly driven by a 65.2% decrease in interest expense from placements to Kshs 0.03 bn, from Kshs 0.09 bn recorded in Q1'2024 coupled with a 18.2% decrease in other interest expenses to Kshs 0.07 bn from Kshs 0.09 bn in Q1'2024. Cost of funds (COF) increased by 1.0% points to 7.1% from 6.1% recorded in Q1'2024, owing to a faster 26.2% increase in Trailing interest expense to Kshs 3.7 bn from Kshs 2.9 bn recorded in Q1'2024, compared to an 8.0% increase in average interest-bearing liabilities to Kshs 52.0 bn from Kshs 48.2 bn in Q1'2024. Trailing interest expense refers to the performance of the interest expense for the past 12 consecutive months. Net Interest Margin (NIM) increased by 0.1% points to 5.43% from 5.36% in Q1'2024, attributable to a 14.5% decrease in trailing net interest income to Kshs 3.0 bn from Kshs 2.6 bn recorded in Q1'2024, compared to the 13.1% growth in average interest earning assets,
- Non-Funded Income (NFI) increased by 9.9% to Kshs 0.42 bn from Kshs 0.39 bn in Q1'2024, mainly driven by a 51.5% increase in other fees income to Kshs 0.09 bn, from Kshs 0.06 bn in Q1'2024, coupled with a 12.7% increase in other income to 0.24 bn from the Kshs 0.22 bn recorded in Q1'2024. Total fees and commissions

increased by 20.1% to 0.15 bn from the Kshs 0.12 bn recorded in in Q1'2024. The revenue mix shifted to 70:30, from 64:36 for the funded to Non-funded income owing to the faster 46.1% growth in Funded Income compared to a 9.9% increase in the Non-Funded Income,

- Total operating expense increased by 19.1% to Kshs 1.1 bn in Q1'2025, from Kshs 0.9 bn in Q1'2024, mainly attributable to 16.9% increase in staff cost to Kshs 0.5 bn, from Kshs 0.4 bn in Q1'2024. Notably, loan loss provisions expense decreased by 7.9% to remain relatively unchanged from the 0.1 bn recorded in Q1'2024,
- Cost to Income Ratio (CIR) decreased by 8.9% points to 76.2% from 85.1% in Q1'2024, owing to the slower 19.1% increase in total operating expenses, which was outpaced by the 33.0% increase in total operating income. CIR without LLP decreased by 5.7% points to 69.1% from 74.8% in Q1'2024.
- Profit before tax increased by 112.1% to Kshs 0.3 bn, from Kshs 0.2 bn recorded in Q1'2024, with effective tax rate decreasing to 2.5% in Q1'2025, from 5.2% in Q1'2024, leading to a 118.1% increase in profit after tax to Kshs 0.3 bn in Q1'2025, from Kshs 0.2 bn in Q1'2024.

Balance Sheet

- The balance sheet recorded an expansion as total assets increased by 17.9% to Kshs 73.4 bn, from Kshs 62.3 bn in Q1'2024, mainly driven by a 102.2% increase in governments securities holdings to Kshs 20.4 bn, from 10.1 bn in Q1'2024, coupled with a 2.0% increase in net loans and advances to Kshs 38.9 bn, from Kshs 38.1 bn in Q1'2024. Total liabilities increased by 7.4% to Kshs 57.2 bn from Kshs 53.3 bn in Q1'2024, mainly driven by 14.5% increase in customer deposits to Kshs 50.1 bn, from Kshs 43.8 bn in Q1'2024, however weighed down by the 22.5% decline in borrowings to Kshs 2.6 bn, from Kshs 3.4 bn in Q1'2024. With 22 branches, similar to Q1'2024, deposits per branch increased by 14.5% to Kshs 2.3 bn, from Kshs 2.2 bn in Q1'2024,
- The 14.5% increased growth in customer deposits, which outpaced the 2.0% increase in net loans led to a decrease in the loan to deposits ratio to 77.6%, from 87.1% in Q1'2024,
- The bank's Asset Quality deteriorated, with Gross NPL ratio increasing to 25.2% in Q1'2024, from 24.1% in Q1'2024, attributable to a 6.8% increase in Gross non-performing loans to Kshs 12.0 bn, from Kshs 11.2 bn in Q1'2024, which outpaced the 2.2% decrease in gross loans to Kshs 47.5 bn, from Kshs 46.5 bn recorded in Q1'2024,
- General Provisions (LLP) increased by 7.4% to Kshs 5.3 bn in Q1'2025 from Kshs 4.9 bn in Q1'2024. The NPL coverage decreased to 72.1% in Q1'2025, from 74.4% in Q1'2024, attributable to the 7.4% increase in general provisions, coupled with a 2.3% decrease in interest in suspense to Kshs 3.3 bn from 3.4 bn in Q1'2024 compared to a 6.8% increase in Gross Non-performing Loans to Kshs 12.0 bn, from Kshs 11.2 bn in Q1'2024.
- Shareholders' funds increased by 79.6% to Kshs 16.2 bn in Q1'2024, from Kshs 9.0 bn in Q1'2024, however weighed down by a 23.8% decline in retained earnings to Kshs 2.5 bn, from Kshs 3.2 bn in Q1'2024,
- HF Group remains capitalized with a core capital to risk-weighted assets ratio of 21.3%, 10.8% points above the statutory requirement of 10.5%. In addition, the total capital to risk-weighted assets ratio came in at 24.3%, exceeding the statutory requirement of 14.5% by 9.8% points, and,
- The bank currently has a Return on Average Assets (ROaA) of 1.0%, and a Return on Average Equity (ROaE) of 5.6%.

Key Take-Outs:

1. **Decreased earnings** - Core earnings per share declined by 89.3% to Kshs 0.1, from Kshs 1.3 in Q1'2024, mainly driven by a 33.0% increase in Total Operating Income to Kshs 1.4 bn from Kshs 1.1 bn in Q1'2024, which outpaced a 19.1% increase in total operating expenses to Kshs 1.1 bn from Kshs 0.9 bn in Q1'2024,

2. **Deteriorated asset quality** – The bank's Asset Quality deteriorated, with Gross NPL ratio increasing to 25.2% in Q1'2024, from 24.1% in Q1'2024, attributable to a 6.8% increase in Gross non-performing loans to Kshs 12.0 bn, from Kshs 11.2 bn in Q1'2024, which outpaced the 2.2% decrease in gross loans to Kshs 47.5 bn, from Kshs 46.5 bn recorded in Q1'2024,
3. **Expanded Balanced sheet** - The balance sheet recorded an expansion as total assets increased by 17.9% to Kshs 73.4 bn, from Kshs 62.3 bn in Q1'2024, mainly driven by a 102.2% increase in governments securities holdings to Kshs 20.4 bn, from 10.1 bn in Q1'2024, coupled with a 2.0% increase in net loans and advances to Kshs 38.9 bn, from Kshs 38.1 bn in Q1'2024,
4. **Increased lending**- Customer net loans and advances increased by 2.0% to Kshs 38.9 bn in Q1'2025, from Kshs 38.1 bn in Q1'2024.

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

- **Capital injection through rights issue** - The Group successfully raised Kshs 6.0 bn in 2024 via a rights issue. This capital boosted HF Group's financial position, enabling further investment in growth initiatives. The capital raised was for product expansion, technological advancements and for regulatory compliance requiring banks to increase their capital base to Kshs 10.0 bn by 2028. The successful completion of the rights issue positioned HF Group to implement its growth strategies effectively and navigate the evolving financial landscape.

Valuation Summary

- We are of the view that HF Group is a "buy" with a target price of Kshs 7.5 representing a upside of 11.6%, from the current price of 6.7 as of 29th May 2025
- HF Group is currently trading at a P/TBV of 0.2x and a P/E of 7.0x vs an industry average of 0.9x and 3.8x respectively.