Equity Group Holdings Plc – FY’2020
1st April, 2021

Below is a summary of the bank’s performance:

Balance Sheet Items	FY'2019	FY'2020	y/y change
Government Securities	138.6	175.7	26.8%
Net Loans and Advances	366.4	477.8	30.4%
Total Assets	**673.7**	**1015.1**	**50.7%**
Customer Deposits	482.8	740.8	53.5%
Total Liabilities	561.9	876.5	56.0%
Shareholders’ Funds	**110.7**	**132.2**	**19.4%**

Balance Sheet Ratios	FY'2019	FY'2020	% point change
Loan to Deposit Ratio	75.9%	64.5%	(11.4%)
Return on average equity	22.0%	16.5%	(5.5%)
Return on average assets	3.6%	2.4%	(1.2%)

Income Statement	FY'2019	FY'2020	y/y change
Net Interest Income	45.0	55.1	22.6%
Net non-Interest Income	30.8	38.5	25.1%
Total Operating income	**75.8**	**93.7**	**23.6%**
Loan Loss provision	(5.3)	(26.6)	402.2%
Total Operating expenses	(44.3)	(72.7)	64.1%
Profit before tax	31.5	22.2	(29.6%)
Profit after tax	**22.6**	**20.1**	(10.9%)
Core EPS	**6.0**	**5.3**	(10.9%)

Income Statement Ratios	FY'2019	FY'2020
Yield from interest-earning assets	11.2%	10.1%
Cost of funding	2.9%	2.7%
Cost of risk	7.0%	28.4%
Net Interest Margin	8.4%	7.6%
Net Interest Income as % of operating income	59.4%	58.9%
Non-Funded Income as a % of operating income	40.6%	41.1%
Cost to Income Ratio	58.5%	77.6%
CIR without LLP	51.5%	49.2%
Cost to Assets	6.3%	5.5%

Capital Adequacy Ratios	FY'2019	FY'2020
Core Capital/Total Liabilities	22.3%	16.2%
Minimum Statutory ratio	8.0%	8.0%
Excess	**14.3%**	**8.2%**
Core Capital/Total Risk Weighted Assets	17.9%	14.8%
Minimum Statutory ratio	10.5%	10.5%
Excess	**7.4%**	**4.3%**
Total Capital/Total Risk Weighted Assets	21.4%	18.9%
Minimum Statutory ratio	14.5%	14.5%
Excess	**6.9%**	**4.4%**

Liquidity Ratio	52.1%	59.3%
Minimum Statutory ratio	20.0%	20.0%
Excess	**32.1%**	**39.3%**
Adjusted core capital/ total deposit liabilities	22.7%	16.2%
Adjusted core capital/ total risk weighted assets	18.2%	14.8%
Adjusted total capital/ total risk weighted assets	21.7%	19.0%

**Note that the figures are extracts from the books of NCBA Group PLC.*

Key Highlights

- During the year, Equity Group restructured loans worth Kshs 171.0 bn to its customers, equivalent to 35.8% of its net loans which stood at Kshs 477.8 bn in FY'2020. Additionally, the Group announced that as at the end of the year, 23.4% of the restructured loans (Kshs 40.0 bn) had resumed repayment and 5.3% of the total restructured loans (Kshs 9.0 bn) had been downgraded to Non-Performing loans. Kshs 122.0 bn, therefore, remains under moratorium constituting 71.3% of the total restructured loan amount and 25.5% of the loan book,
- Equity Group Holdings completed the 66.5% stake acquisition of the Banque Commerciale Du Congo (BCDC) at a cost of USD 95.0 mn (Kshs 10.3 bn). Initially, the deal was to cost USD 105.0 mn (Kshs 11.4 bn), however factoring in the adverse effects of the COVID-19 pandemic on the two economies, the two parties agreed to reduce the amount to USD 95.0 mn (Kshs 10.3 bn), and,
- Equity Group Holdings disbursed an additional Kshs 111.4 bn in FY'2020 to help support the economies it serves as the Group's net loans and advances increased by 30.4% to Kshs 477.8 from Kshs 366.4 bn recorded in FY'2019. A total of Kshs 57.5 bn was disbursed in the period to 141,106.0 MSMEs under the Group's Young Africa Works Program.

Income Statement

- Core earnings per share declined by 10.9% to Kshs 5.3, from Kshs 6.0 recorded in FY'2019, better than our projections of a 22.6% decline to Kshs 4.6. The performance was driven by a 64.1% growth in total operating expenses to Kshs 72.7 bn, outpacing the 23.6% growth in total operating income. The variance in core earnings per share growth against our expectations was due to the total operating income increasing by 23.6% against our expectation of a 14.4% growth in FY'2020, despite the total operating expenses growing faster by 64.1% against our expectations of a 41.5% increase in FY'2020,
- Total operating income rose by 23.6% to Kshs 93.7 bn, from Kshs 75.8 bn recorded in FY'2019. This was driven by a 25.1% increase in Non-Funded Income (NFI) to Kshs 38.5 bn, from Kshs 30.8 bn in FY'2019, coupled with a 22.6% increase in Net Interest Income (NII) to Kshs 55.1 bn, from Kshs 45.0 bn in FY'2019,
- Interest income increased by 23.5% to Kshs 73.8 bn, from Kshs 59.7 bn in FY'2019. This was driven by a 25.5% increase in interest income on loans and advances to Kshs 52.0 bn, from Kshs 41.5 bn in FY'2019, coupled with a 24.1% increase in interest income from government securities to Kshs 20.9 bn, from Kshs 16.9 bn in FY'2019. The increase in interest income was however weighed down by a 54.4% decline in interest income from deposits and placements with banking institutions to Kshs 0.5 bn, from Kshs 1.2 bn in FY'2019. The Yield on Interest-Earning Assets declined to 10.1%, from 11.2% in FY'2019, as the average interest-earning assets grew faster by 36.7% to Kshs 729.3 bn, from Kshs 533.5 bn in FY'2019 compared to the 23.5% trailing interest income. Trailing Interest Income refers to the performance of the interest income for the past 12 consecutive months,
- Interest expense increased by 26.3% to Kshs 18.6 bn, from Kshs 14.7 bn in FY'2019, following a 23.9% increase in interest expense on customer deposits to Kshs 13.7 bn, from Kshs 11.1 bn in FY'2019, coupled

with an 89.7% increase in interest expense on deposits and placements from banking institutions to Kshs 1.3 bn, from Kshs 0.7 bn in FY'2019. Cost of funds, on the other hand, decreased marginally by 0.2% points to 2.7%, from 2.9% in FY'2019, owing to the faster 36.7% growth in average interest-bearing liabilities, which outpaced the 26.3% growth in the trailing interest expense. Trailing interest expense refers to the performance of the interest expense for the past 12 consecutive months. Net Interest Margin (NIM) declined to 7.6% from 8.4% in FY'2019, attributable to the 36.7% growth in average interest-earning assets, which outpaced the 22.6% growth of Net Interest Income (NII),

- Non-Funded Income (NFI) rose by 25.1% to Kshs 38.5 bn, from Kshs 30.8 bn in FY'2019. The increase was mainly driven by an 18.3% increase in Fees and commissions on loans and advances to Kshs 6.6 bn, from Kshs 5.6 bn in FY'2019, coupled with the 77.2% growth in Foreign Exchange Trading income to Kshs 6.2 bn, from Kshs 3.5 bn in FY'2019. Despite the waiver on mobile banking fees seen during the year in Kenya, Equity Group's total fees and commission increased by 6.9% to Kshs 22.7 bn, from Kshs 21.2 bn in FY'2019 boosted by fees and commissions growth recorded in the Group's subsidiaries. Equity Bank Kenya's total fees and commissions declined by 8.0% to Kshs 14.2 bn in FY'2020, from Kshs 15.4 bn recorded in FY'2019, while the subsidiaries' total fees and commissions increased by 46.6% to Kshs 8.5 bn from Kshs 5.8 bn recorded in FY'2019. Notably, the revenue mix remained unchanged at 59:41, funded to non-funded income, same as was recorded in FY'2019,
- Total operating expenses grew by 64.1% to Kshs 20.0 bn in FY'2020, from Kshs 16.5 bn recorded in FY'2019, mainly driven by the 402.2% increase in Loans Loss Provision to Kshs 26.6 bn, from Kshs 5.3 bn recorded in FY'2019. The increased provision level was on the back of the subdued operating environment seen during the year. Additionally, Staff Costs increased by 20.4% to Kshs 15.4 bn in FY'2020, from Kshs 12.8 bn recorded in FY'2019,
- As a result of the 402.2% increase in Loans Loss Provision, Cost to Income Ratio (CIR) deteriorated to 77.6%, from 58.5% in FY'2019. Without LLP, cost to income ratio improved by 2.3% points to 49.2%, from 51.5% in FY'2019, an indication of an indication of an improvement in the Banks efficiency levels,
- Profit before tax declined by 29.6% to Kshs 22.2 bn, from Kshs 31.5 bn in FY'2019. Profit after tax declined by 10.9% to Kshs 20.1 bn in FY'2020, from Kshs 22.6 bn recorded in FY'2019 with the effective tax rate decreasing to 9.3% from 28.3% in FY'2019, on the back of the reduced Corporate Tax during most of 2020, and,
- The Board of Directors did not recommend a dividend for the Financial Year 2020, and for the second year running due to the need to preserve cash in the Covid-19 business environment and to enhance the bank's core capital.

Balance Sheet

- The balance sheet recorded an expansion as Total Assets increased by 50.7% to Kshs 1,015.1 bn, from Kshs 673.7 bn recorded in FY'2019. This growth was largely driven by a 30.4% increase in the loan book to Kshs 477.8 bn, from Kshs 366.4 bn recorded in FY'2019, coupled with the 26.8% growth in investment in government securities to Kshs 175.7 bn, from Kshs 138.6 bn recorded in FY'2019. The remarkable expansion in the balance is partly attributable to the 66.5% stake acquisition of Congolese lender, Banque Commerciale Du Congo (BCDC),
- Total liabilities rose by 56.0% to Kshs 876.5 bn, from Kshs 561.9 bn in FY'2019, driven by a 53.5% increase in customer deposits to Kshs 740.8 bn, from Kshs 482.8 bn in FY'2019. Key to note, the strong growth in customer deposits is mainly attributable to the acquisition of BCDC, with the subsidiary contributing Kshs 234.0 bn to the total deposits. Deposits per branch increased by 34.3% to Kshs 2.2 bn, from Kshs 1.6 bn in FY'2019, with the number of branches increasing by 42 to 336 branches in FY'2020, from 294 in FY'2019, with Equity BCDC contributing 26 additional branches,
- The faster 53.5% growth in customer deposits as compared to the 30.4% growth in loans, led to a decline in the Loans to deposit ratio declined to 64.5% from 75.9% in FY'2019,

- Gross Non-Performing Loans (NPLs) increased by 63.7% to Kshs 59.4 bn in FY'2020, from Kshs 36.3 bn recorded in FY'2019. The NPL ratio rose to 11.5% in FY'2020, from 9.5% recorded in FY'2019, attributable to the faster 63.7% growth in Gross Non-Performing Loans (NPLs), compared to the 34.2% increase in gross loans. The main sectors that contributed to the deterioration in asset quality were SMEs and large enterprises sectors, which contributed the largest portion of the Non-Performing loans with NPL Ratios of 15.5% and 9.1%, respectively. The group's Tanzania subsidiary also recorded a high NPL ratio of 35.4% in FY'2020, with Equity Bank Kenya recording an NPL ratio of 11.5% in FY'2020. With the general Loan Loss Provisions increasing by 118.7% to Kshs 28.3 bn, from Kshs 12.9 bn in FY'2019, higher than the 63.7% rise in the Gross Non-Performing Loans, the NPL coverage improved to 62.4%, from 47.5% in FY'2019, an indication of sufficient provisioning,
- Shareholders' funds grew by 18.6% to Kshs 121.4 bn in FY'2020, from Kshs 102.4 bn in FY'2019, mainly supported by a 19.8% growth in retained earnings to Kshs 118.8 bn, from Kshs 99.1 bn in FY'2019,
- Equity Group is currently sufficiently capitalized with a core capital to risk-weighted assets ratio of 14.8%, 4.3% points above the statutory requirement. In addition, the total capital to risk-weighted assets ratio was 18.9%, exceeding the statutory requirement by 4.4% points. Adjusting for IFRS 9, the core capital to risk-weighted assets stood at 14.8% while total capital to risk-weighted assets came in at 19.0%, and,
- The bank currently has a Return on Average Assets (ROaA) of 2.4%, and a Return on Average Equity (ROaE) of 16.5%.

Key Take-Outs:

1. The Group's geographical diversification strategy has continued to emerge as a net positive, with the bank's various subsidiaries in Uganda, DRC, Rwanda, Tanzania, and South Sudan cumulatively contributing 28.0% to the bank's total profitability and 39.0% to the group's total asset base. However, given the high NPL levels in the group's Tanzania subsidiary of 35.4%, the group will need to improve its credit assessment in the country to bring down the high NPL ratio. Cumulatively, the group's subsidiaries recorded a 59.7% growth in their Profit after Tax (PAT) to Kshs 6.1 bn, from Kshs 3.8 bn in FY'2019, with the Tanzanian branch recording a loss of Kshs 0.30 bn in FY'2020, a marginal improvement from the earlier recorded loss of Kshs 0.32 bn in FY'2019. Total assets in the bank's regional subsidiaries grew by 184.1% to Kshs 472.2 bn in FY'2020, from Kshs 166.2 bn in FY'2019, attributable to the acquisition of the Banque Commerciale Du Congo (BCDC). Improved efficiencies in the subsidiaries saw their cost structure contribution to the Group, improve to 31.8% in FY'2020, from 34.1% in FY'2019,
2. The Group's South Sudan subsidiary saw it's NPL ratio decline by 14.3% points to 1.2% in FY'2020 from 15.5% recorded in FY'2019. The improved asset quality is partly attributable to improved credit assessment,
3. Equity Group's recorded a remarkable increase in its balance sheet, as Total Assets increased by 50.7% to Kshs 1,015.1 bn, from Kshs 673.7 bn recorded in FY'2019 despite the challenging business environment. The growth makes Equity Group the first bank in East and Central Africa to cross the Kshs 1.0 tn mark and is largely attributable to the Group's 66.5% stake acquisition of Congolese lender, Banque Commerciale Du Congo (BCDC). BCDC contributed Kshs 285.1 bn worth of assets in FY'2020 to the Group. The Group's diversification into different markets will allow it to mitigate risks that are unique to Kenya such as the 2022 electioneering period as well as spread risks over economically well-placed economies,
4. Increased innovation and digitization have seen 98.0% of all transactions of the bank being done on alternative channels, with mobile and internet transactions taking up 84.4% of all transactions, and agency banking contributing 8.3% of all transactions. However, in terms of the value of transactions, branches and mobile banking each contributed 37.4% of the value of all transactions, while agency banking contributed 17.7%. This highlights the transformation of branches to handle high-value transactions. This transformation aids the bank by offering its ecosystem banking products to corporate and SME clients,

5. Despite the recent waiver of banking and mobile money transactions unveiled by the Central Bank of Kenya as a measure to cushion citizens against the effects of the COVID-19 pandemic, the group recorded an increase of 25.1% in Non-Funded Income (NFI) to Kshs 38.5 bn, from Kshs 30.8 bn in FY'2019. The increase was mainly driven by an 18.3% increase in Fees and commissions on loans and advances to Kshs 6.6 bn, from Kshs 5.6 bn in FY'2019, coupled with the 77.2% growth in Foreign Exchange Trading income to Kshs 6.2 bn, from Kshs 3.5 bn in FY'2019, and,
6. The bank's asset quality deteriorated, as evidenced by the 2.0% points rise in the NPL ratio to 11.5% in FY'2020, from 9.5% in FY'2019. The main sectors that contributed to the deterioration in asset quality were SMEs and large enterprises sectors, which contributed the largest portion of the Non-Performing loans with NPL Ratios of 15.5% and 9.1%, respectively. Key to note, the Group's Tanzania subsidiary recorded a high NPL ratio of 35.4%. The subsidiaries contributed 3.2% of the group's loan book. With the improvement in business conditions and expected economic recovery in Rwanda, Uganda, Kenya, Tanzania and DRC, we expect the group's asset quality to improve marginally in FY'2021.

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

I. Channeled diversification is likely to further improve on efficiency with emphasis on alternative channels of transactions, as the bank rides on the digital revolution wave, thereby further improving the cost to income ratio by cost rationalization and revenue expansion. This will likely propel the bank's prospects of achieving sustainable growth, as it replicates its successful business model across its various regional subsidiaries, and,
II. The bank's operating model of enhancing balance sheet agility is likely to place the bank in a prime position to take advantage of any opportunities that may arise, such as attractive inorganic growth via acquisitions or fast lending with the repeal of the interest rate cap law. The bank's balance sheet agility is seen with a liquidity ratio of 59.3%, loan deposit ratio of 64.5% and a core capital to risk-weighted asset ratio of 14.8%.

Valuation Summary

- We are of the view that Equity Group is an "***buy***" with a target price of Kshs 49.7 representing an upside of 27.3%, from the current price of Kshs 39.1 as of 1st April 2021,
- Equity Group is currently trading at a P/TBV of 1.2x and a P/E of 7.3x vs an industry average of 1.0x and 8.4x, respectively.