Kenya Listed Commercial Banks Analysis
Cytonn FY'2018 Banking Sector Report

"Growth and Recovery in a tough operating environment"

Cytonn

Saturday, 20 April 2019

I. Introduction to Cytonn

About Us

Cytonn Investments is an alternative investment manager with a primary focus on real estate investments in the high growth East African Region. In addition to real estate, Cytonn invests in educational facilities and hospitality, which are complimentary to its real estate developments. We have a unique strategy of coupling two compelling demand areas - the lack of high yielding investment products due to the large banking spread, and the lack of institutional grade real estate; by manufacturing high yielding instruments to attract funding from investors, and we deploy that funding to investment grade, well planned and comprehensive real estate developments that are largely pre-sold.

82 Over Kshs. 82 billion worth of projects under mandate

7 Seven offices across 2 continents

500 Over 500 staff members, including Cytonn Distribution

10 10 investment ready projects in real estate

A unique franchise differentiated by:

Independence & Investor Focus

Focused on serving the interest of clients, which is best done on an independent platform to minimize conflicts of interest

Alternative Investments

Specialized focus on alternative assets - Real Estate, Private Equity, and Structured Solutions

Strong Alignment

Every staff member is an owner in the firm. When clients do well, the firm does well; and when the firm does well, staff do well

Committed Partners

Strong global and local partnerships in financing, land and Cytonn Real Estate, our development affiliate

Why We Exist

Africa presents an attractive investment opportunity for investors seeking attractive and long-term returns. Despite the alternative markets in Africa having high and stable returns, only a few institutional players serve the market. Cytonn is focused on delivering higher returns in the alternative markets, while providing the best client service and always protecting our clients' interests.

WE SERVE THREE MAIN CLIENT SEGMENTS:

- High Net-worth Individuals through Cytonn Private Wealth. This is done through our captive Distribution Network
- East Africans in the Diaspora through Cytonn Diaspora
- Global and Local Institutional Clients. These clients are served from our Investment & Fundraising Team

WE INVEST OUR CLIENT FUNDS IN:

- Real Estate, and Real Estate Related Businesses
- Private Equity
- Fixed Income Structured Solutions
- Equities Structured Solutions

Our Business Structure

Cytonn Investments Management Plc

- **Cytonn Capital Partners** (Private Markets)
  - Private Offers and Real Estate Investments
  - Cytonn Hospitality
  - Cytonn Education Services
  - Superior Homes Kenya
  - Serviced Offices
- **Cytonn Asset Managers** (Regulated by Capital Markets Authority)
  - Unit Trust Funds
  - Cytonn Africa Financial Fund
  - Cytonn Advisory
  - Pension Fund Management
- **Cytonn Real Estate**
  - Research and Deal Origination
  - Project Management
  - Quality Assurance/ Control
  - Cytonn Procurement - Cymatt
  - Cytonn Real Estate Legal
  - Cytonn Properties
  - Cytonn Centre for Affordable Housing
- **Other Strategic Initiatives**
  - Cytonn Distribution
  - East African Forum for Alternative Investments

Board of Directors

To ensure that we remain focused on the clients' interests, we have put in place proper governance structures. We have a board of directors consisting of 12 members from diverse backgrounds, each bringing in unique skill-sets to the firm.

Board of Directors

Governance: Board Committees

Investments and Strategy Committee

The committee oversees and provides strategic investment direction, including the implementation and monitoring for Cytonn. The members are:

- James Maina (Chair)
- Antti-Jussi Ahveninen, MSc
- Madhav Bhalla, LLB
- Edwin H. Dande, MBA
- Elizabeth N. Nkukuu, CFA

Audit, Risk and Compliance Committee

The committee establishes and oversees finance, audit, risk and compliance, including the implementation and monitoring process. The members are:-

- Madhav Bhalla, LLB (Chair)
- Nasser Olwero, Mphil
- Madhav Bhandari, MBA
- Patricia N. Wanjama, CPS

Human Resources, Governance & Compensation Committee

The committee establishes, oversees and implements governance structure, human resource policies and firm wide compensations. The members are:-

- Rose Kimotho M.B.S (Chair)
- Antti-Jussi Ahveninen, MSc
- Prof. Daniel Mugendi Njiru, PhD
- Michael Bristow, MSc
- Edwin H. Dande, MBA

Technology and Innovation Committee

The committee establishes, oversees and implements technical expertise and innovative processes as a driver towards competitiveness. The members are:-

- Nasser Olwero, Mphil (Chair)
- Michael Bristow, MSc
- Rose Kimotho M.B.S
- Patricia N. Wanjama, CPS

Management Team

Edwin H. Dande, MBA
Managing Partner & CEO

Elizabeth N. Nkukuu, CFA
Chief Investments Officer

Patricia N. Wanjama, CPS
Partner, Head of Legal & Company Secretary

Shiv A. Arora, BSc.
Head - Private Equity Real Estate

Maurice Oduor, BBA
Principal Officer, CAML

Johnson Denge, MISK
Senior Manager Regional Markets

Martin Gitonga, BA
Senior Project Manager

Management Team Cont..

Kimathi K. Muchiri, MSc, CPA (K)
Internal Audit Manager

Daniel N. Mainye, MBA
Business Manager, Technologies

Anne Joseph, BA, CHRM
Assistant HR Manager

Grace W. Weru, BA, CPA(K)
Finance Manager, CAML

Cytonn's Business Overview

Where we Raise Money

- Local High-net-worth Investors via a captive distribution of 250 Financial Advisors and 300 Independent Financial Advisors
- Global & Local Institutions such as Taaleri of Finland
- Diaspora via our office in the Washington DC Metro Area
- Retail & Pension via Cytonn Asset Managers

Where we Invest

- **Real Estate –** 84.8%
- **Financial Services** - 4.6%
- **Education** – 0.8%
- **Hospitality -** 9.8%
- **Procurement –** Just Started

How we Exit

- **Individuals i.e. Cytonn Distribution**
- **Institutions**
- **Investment Vehicles**
  - Partnership Units (LLP)
  - REIT's Fund
  - Other Income Funds

Strategic Support Services					
	1. Finance	2. ICT	3. Legal & Compliance	4. Brand (PR & Communication)	5. CS
	6.HR	7. Risk	8. Business Admin	9. Fund Operations	10. Internal Audit

II Kenya Economic Review and Outlook

Cytonn

Kenya Economic Review

Of the 7 indicators we track, 3 are positive, 3 are neutral and 1 is negative. We maintain our positive outlook on the 2019 macroeconomic environment

Key Macro-Economic Indicators – Kenya			
Indicators	**YTD 2019 experience and outlook going forward**	**Outlook-Beginning of Year**	**Current Outlook**
GDP Growth	• GDP growth is projected to range between 5.7%-5.9% in 2019, lower than the expected growth rate of 6.0% in 2018, but higher than the 5-year historical average of 5.4%	**Positive**	**Positive**
Inflation	• Inflation has remained muted in Q1’2019 mainly supported by lower fuel and electricity. Going forward, inflation is expected to average 5.4% and remain within the government target range of 2.5% - 7.5%. However, risks abound in the near-term, including the late onset of the traditionally long rains season will disrupt food supply leading to a gradual flare in food inflation, coupled with the continued rise in global fuel prices	**Positive**	**Positive**
Interest rates	• The interest rate environment has remained stable in 2019, with the CBR having been retained at 9.0% in the 2 MPC meetings held during Q1’2019. With the heavy domestic maturities in 2019, we expect slight upward pressure on interest rates going forward, as the government tries to meet its domestic borrowing targets for the fiscal year.	**Neutral**	**Neutral**

Source – CBK

Kenya Economic Review, continued…

Of the 7 indicators we track, 3 are positive, 3 are neutral and 1 is negative. We maintain our positive outlook on the 2019 macroeconomic environment

Key Macro-Economic Indicators – Kenya			
Indicators	**YTD 2019 experience and outlook going forward**	**Outlook-Beginning of Year**	**Current Outlook**
Currency	• The Kenya Shilling has remained stable gaining by 1.1% YTD and is expected to remain resilient against the US Dollar, due to the continued narrowing of the current account thus improved balance of payments and the continued support from the CBK in the short term through its sufficient reserves of USD 8.3 bn (equivalent to 5.4-months of import cover).	**Neutral**	**Neutral**
Government Borrowing	• We still maintain our expectations of KRA not achieving their revenue targets with the National Treasury reporting ordinary revenue, as at February 2019, at Kshs 945.6 bn; 15.2% below the pro-rated target. This is expected to result in further borrowing from the domestic market to plug in the deficit, which coupled with heavy maturities might lead to pressure on domestic borrowing • On the international debt front, the government has a net external financing target of Kshs 272.0 bn to finance the budget deficit, coupled with the need to retire 3 commercial loans maturing in H1'2019. There are talks that the Government might issue another Eurobond with the targeted amount at USD 2.5 bn to refinance the USD 750 mn maturing in June but with the International Monetary Fund (IMF) having raised Kenya's debt distress risk from low to moderate on October we expect investors to demand higher yields to match the risk profile.	**Negative**	**Negative**

Source – CBK

Kenya Economic Review, continued…

Of the 7 indicators we track, 3 are positive, 3 are neutral and 1 is negative. We maintain our positive outlook on the 2019 macroeconomic environment

Key Macro-Economic Indicators – Kenya			
Indicators	**YTD 2019 experience and outlook going forward**	**Outlook Beginning of Year**	**Current Outlook**
Investor Sentiments	• Eurobond yields have been on a declining trend YTD. An improvement was also recorded in foreign inflows in the capital market to a net buying position of USD 5.6 mn in Q1'2019 from a net selling position of USD 93.4 mn in Q4'2018, an indication of improved investor sentiments. • We expect improved foreign inflows from the negative position in 2018, mainly supported by long term investors who enter the market looking to take advantage of the current cheap valuations in select sections of the market.	**Neutral**	**Neutral**
Security	• Security is expected to be upheld in 2019, given that the political climate in the country has eased. Despite the recent terror attack experienced during the quarter, Kenya was spared from travel advisories, evidence of the international community's confidence in the country's security position.	**Positive**	**Positive**

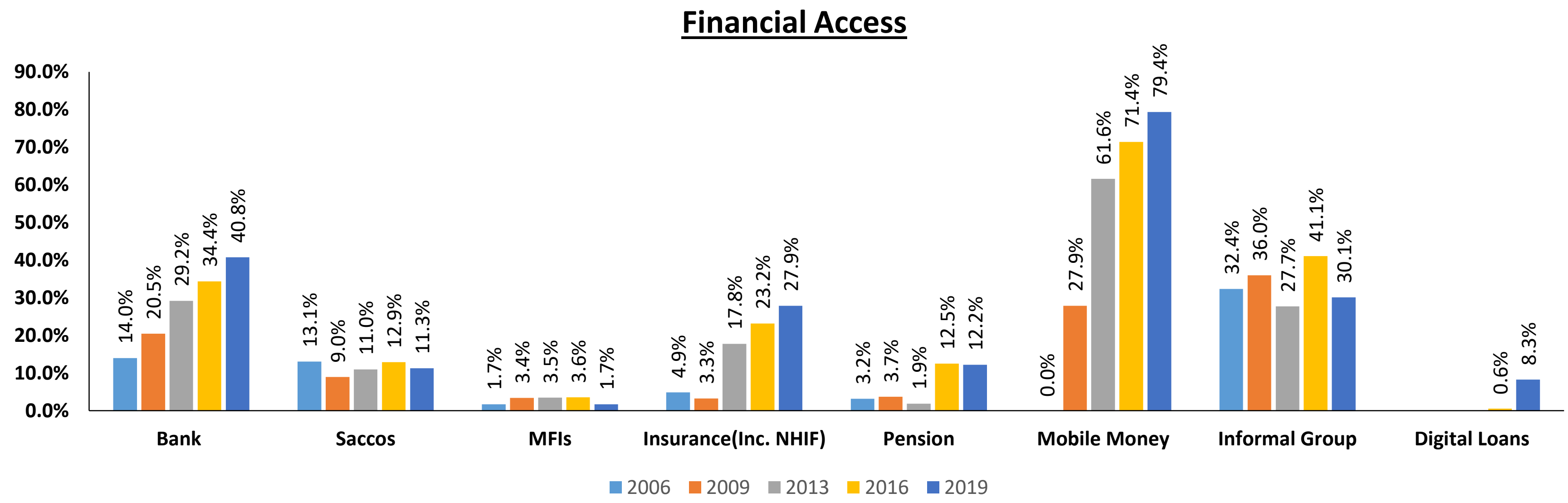
Source – CBK

III. Banking Sector Overview

Kenya Banking Sector Overview

Financial Inclusion in Kenya continues to rise, mainly driven by proliferation of mobile and digital channels

- In Kenya there are a total of 40 commercial banks, with Charterhouse Bank under statutory management and Imperial Bank under receivership, 1 mortgage finance company, 13 microfinance banks, 9 representative offices of foreign banks, 73 foreign exchange bureaus, 19 money remittance providers and 3 credit reference bureaus
- Financial inclusion in Kenya has continued to rise, with 82.9% of the adult population able to access formal financial services. This has largely been driven by digitization, with Mobile Financial Services (MFS) rising to be the preferred method to access financial services in 2019, with 79.4% of the adult population using the channel



Source: Central Bank of Kenya, FinAccess report

Recent Developments in the Kenyan Banking Sector

Consolidation continues in the banking sector, such as that of a possible merger between NIC Group and CBA Bank

1. **Consolidation:** Kenya's banking sector has witnessed heightened M&A activity over the last 4 years. In H1'2018, SBM Bank Kenya Ltd completed the acquisition of 75% of the value of all moratorium deposits at Chase Bank, with the remaining 25% to remain with Chase bank Limited. More recently, NIC Group and Commercial Bank of Africa (CBA) announced a potential merger, CBA offered to acquire Jamii Bora, and KCB had its offer to take up certain assets and Imperial Bank accepted.Below is a summary of key transactions done over the last five years and their transaction multiples. It is worth noting that transactions are happening at relatively cheaper multiples compared to historical levels

Acquirer	Bank Acquired	Book Value at Acquisition (Kshs bns)	Transaction Stake	Transaction Value (Kshs bns)	P/Bv Multiple	Date
KCB Group	National Bank of Kenya	7.0	100.0%	6.6	**0.9x**	19-Apr*
CBA Group	Jamii Bora Bank	3.4	100.0%	1.4	**0.4x**	19-Jan*
AfricInvest Azure	Prime Bank	21.2	24.2%	5.1	**1.0x**	19-Jan
NIC Group	CBA Group	30.5**	47:53***	18.0	**0.6x**	19-Jan*
KCB Group	Imperial Bank	Unknown	Undisclosed	Undisclosed	**N/A**	18-Dec
SBM Bank Kenya	Chase Bank ltd	Unknown	75.0%	Undisclosed	**N/A**	18-Aug
DTBK	Habib Bank Kenya	2.4	100.0%	1.8	**0.8x**	17-Mar
SBM Holdings	Fidelity Commercial Bank	1.8	100.0%	2.8	**1.6x**	16-Nov
M Bank	Oriental Commercial Bank	1.8	51.0%	1.3	**1.4x**	16-Jun
I&M Holdings	Giro Commercial Bank	3	100.0%	5	**1.7x**	16-Jun
Mwalimu SACCO	Equatorial Commercial Bank	1.2	75.0%	2.6	**2.3x**	15-Mar
Centum	K-Rep Bank	2.1	66.0%	2.5	**1.8x**	14-Jul
GT Bank	Fina Bank Group	3.9	70.0%	8.6	**3.2x**	13-Nov
Average			**78.3%**		**1.4x**	

** Announcement date*

*** Book Value as of the announcement date*

**** Shareholder swap ratio between NIC and CBA, respectively*

Recent Developments in the Banking Sector Cont..

The National Assembly voted to retain the 4.0% cap on loans while removing the 70% floor on deposits

2. Regulation

i. **Draft Financial Markets Conduct Bill 2018:** The National Treasury completed the Draft Financial Markets Conduct Bill, that seeks to create an effective financial consumer protection, make credit more accessible and consequently support financial innovation and competition. The bill's main objectives thus are:

   i. Ensure better conduct by banks and other lenders in terms of extending credit to retail financial customers. By categorically not defining lenders as banks, this, in our view, might be the introduction of licensing for credit companies that are not banks, mainly the non-deposit taking Microfinance Institutions (MFIs),

   ii. Provide consumer protection, mainly for retail customers by ensuring their credit contracts are clear and well understood in terms of interest, fees, charges and costs on credit facilities, thereby removing the opacity that has been existent in loan pricing

ii. **Banking Sector Charter:** The Central Bank of Kenya proposed to introduce a Banking Sector Charter that will guide service provision in the sector. The Charter aims to instill discipline in the banking sector in order to make it responsive to the needs of the banked population. It is expected to facilitate a market-driven transformation of the Kenyan banking sector, thereby considerably improving the quality of service provided, and increasing access to affordable financial services for the unbanked and under-served population. The impending implementation of the Charter possibly in 2019, will likely introduce risk-based credit scoring

Recent Developments in the Banking Sector Cont….

Regulatory policies aimed at improving stability in the sector

iii. **The National Assembly Retains 4.0% Cap on loans while scrapping the 70% floor on deposit savings:** A majority of the members of The National Assembly voted to retain the law, whose repeal proposition was included in the Finance Bill. The proposition to remove the floor of 70.0% of the Central Bank Rate (CBR) minimum interest payable on deposits was accepted in a move that will likely see banks reduce interest payable on deposits, thereby possibly alleviating the reduced Net Interest Margins (NIMs) that came with the law

iv. **IFRS 9 Implementation**: With the implementation of IFRS 9, which took effect from 1st January 2018, banks were expected to provide both for the incurred and expected credit losses. Most banks charged the one-off impairments on their equity, as allowed for in the initial year of implementation. Banks adopted more stringent lending policies, and as a consequence lending was skewed towards collateral based lending as opposed to unsecured lending. To avoid the high provisioning levels that would be required, and earn higher risk-adjusted returns, banks became unwilling to lend to the private sector and more specifically to SMEs

v. **Anti Money Laundering:** The KBA, in a circular, directed bank managers to ensure customers also provide supporting evidence for their source of cash when depositing and its use while withdrawing. Bank customers planning to withdraw or deposit Kshs 10.0 mn and above in cash will now be required to give a three-days' notice and get clearance from their respective branch managers

Recent Developments in the Banking Sector Cont….

Banks continue to seek alternative financing for onward lending to the private sector, in order to address asset-liability tenor mismatch

3. Loans to listed banks by international organizations for private sector and SME lending – Banks have been obtaining finance from international institutions mainly for onward lending to the private sector and SMEs, so as to plug a funding deficit occasioned by a mismatch in their assets and liabilities by tenor, as deposits tend to be relatively short term while loans are relatively long term. The funding issues so far have been summarized in the table below:

	Issuer	Bank	Issue Period	Amount of Loan (Kshs bn)	Term of Credit
1	IFC	Cooperative Bank	18-Feb	15.2	7-years
2	Africa Development Bank	Kenya Commercial Bank	17-Oct	10.4	Not specified
4	14 financial Institutions (syndicated)	Stanbic Bank	18-May	10.0	2,3 years
5	Africa Development Bank	Diamond Trust bank	18-Mar	7.5	7-years
6	FMO	I&M Holdings	18-Oct	4.0	Not specified
7	IFC	I&M Holdings	18-Jan	1.0	Not specified
3	SwedFund	Victoria Commercial Bank	18-Apr	0.5	Not specified
8	East African Development Bank	Sidian Bank	18-Nov	0.2	8-years
	Total			**48.9**	

Recent Developments in the Banking Sector Cont….

Banks have been driving digital innovations largely through the alternative channels as they exploit the space to generate Non Funded Income

4. Digital Innovation:

i. Housing Finance launching their own mobile banking app dubbed HF Whizz. The app aims to change the way consumers open and access their bank accounts. Users of the app will be able to open an account, access loans, and deposit and transfer cash via their mobile phones;

ii. Barclays Bank launched its own digital platform, dubbed Timiza, which allows customers to send money to their respective accounts, pay for utilities such as water and electricity, procure micro insurance, and pay for online taxi hailing services. In addition to this, the app grants customers with the access to micro loans of between Kshs 100 and Kshs 150,000 from the platform; and,

iii. Equity Group launched its FinTech subsidiary, Finserve, a technological service company, tasked to drive disruptive technology innovation in the financial services segment, which houses Equitel, Equity Eazzy app, EazzyBiz and EazzyNet

5. Barclays Kenya to Rebrand to Absa by 2020: Following the London-based Barclays Plc's exit from the African market, Barclays Africa Group Limited changed its name to Absa Group, with the Kenyan subsidiary set to complete the rebranding process by 2020. With more localized decision-making, the lender is well positioned to quickly exploit any opportunities that arise as well as build on their innovative profile that has seen the bank offer efficient services to its customers.

Growth in the Banking Sector

Listed banks' FY'2018 EPS increased by 13.8% y/y from an average decline of 1.0% witnessed in FY'2017

- Kenya's listed banks recorded a positive EPS growth of 13.8% in FY'2018, compared to a 1.0% decline in FY'2017, indicating the diversification strategies employed by banks in the wake of the interest-rate cap legislation, that was passed in September 2016, to navigate the relatively tougher operating environment, have been fruitful
- The increase was on the back of a 2.5% increase in Net Interest Income (NII) coupled with a 3.8% growth in Non-Funded Income (NFI) as banks adapted to operating under the interest rate cap regime. The Net Interest Margin (NIM) decreased to 7.9% in FY'2018 from 8.4% in FY'2017, highlighting the decline in average yields on interest earnings assets, owing to increased allocation to relatively lower yielding Government securities, and the 100 bps decline of the Central Bank Rate
- The sector had an improvement in operating efficiency as the Cost to Income Ratio (CIR) declined to 57.3% in FY'2018 from 61.1% in FY'2017, amid cost rationalization measure such as branch closures, staff layoffs in voluntary retirement plans and digitization strategies aimed at reducing operational costs
- Listed banks continued to recorded a slow growth in net loans and advances which came in at 4.3% y/y to Kshs 2.04 tn in FY'2018 from Kshs 2.0 tn in FY'2017. Deposits grew at a faster rate of 10.3% y/y to Kshs 2.7 tn in FY'2018 from Kshs 2.4 tn in FY'2017. The sector had an improved profitability y/y, as shown by the rise in the Return on Average Equity (ROaE) to 18.8% in FY'2018 from 17.6% in FY'2017

Banking Sector Growth Drivers

Alternative channels of transactions, operational efficiency and revenue diversification are the key growth drivers for banks

1) **Increased adoption of technology to improve efficiency:** Banks have been riding on the digital revolution wave to improve their operational efficiency. Increased adoption of alternative channels of transactions such as mobile, internet and agency banking, has led to increased transactions carried out via alternative channels and out of bank branches, which have been reduced to handling high value transactions and other services such as advisory. Thus banks reduced front-office operations, thereby reducing the staff required and by extension reducing operating expenses and hence improving operational efficiency
2) **Diversification to different revenue streams:** Banks have continued to diversify their revenue sources, as they adapt to operating under the interest rate cap regime. Banks increased the fees and commissions on loans and ventured into various NFI growth ventures such bancassurance. NFI was also earned from transactional income obtained as the number of transactions increased buoyed by increased adoption of alternative channels of transactions
3) **Economic recovery:** The ongoing economic recovery will lead to improved demand for credit from sectors affected by the economic slump witnessed in 2017 due to political uncertainty and severe drought. Increased credit extended to sectors such as agriculture, real estate, manufacturing and trading presents interest income growth opportunities

Growth and Recovery in a Tough Operating Environment

Focus Area	Summary	Effect on Banking Sector
Regulation	• **Banking (Amendment) Act 2015:** Put in place in the industry following the enactment of the Banking Act (Amendment) 2015, with deposit floor removed in Finance Act 2018 • **Transition to IFRS 9 from IAS 39:** IFRS 9 requires banks to adopt a forward looking approach in credit risk assessment	• Net Interest Margins declined due to the price controls, with the Net Interest Margin coming in at 7.9% from 8.4% in FY'2017, and should improve, • Banks total capital position relative to their risky assets declined on IFRS 9 implementation. Lending policies are now tighter, and skewed towards collateral based lending
Growth	• **Improved profitability:** The sector recorded improved profitability, aided by recoveries in both Funded and Non-Funded Income, on aggregate. This was also aided by reduced expenses, largely on reduced provisioning charges,	• Improved bottom line helped in improving the operational efficiency, as shown by the Cost to Income Ratio improvement to 57.3% from 61.1%. Revenue expansion by product diversification is one of the core opportunities for the banking sector to achieve sustainable growth
Consolidation	• **Various Mergers and Acquisitions happening:** With increased competition amongst players in the banking sector, coupled with tough operating environment, several consolidations have happened.	• Consolidations in the sector have resulted in (i) aiding in successful remediation of collapsed banks, (ii) leaving fewer but well capitalized players able to catalyze economic growth, thus creating a more stable banking sector
Asset Quality	• **Increase in non-performing loans:** With the Gross NPL ratio currently at 9.7%, up from 8.5% in FY'2017, and much higher than the 5-year average of 8.4%. This raises concerns around asset quality in the sector	• The increased NPLs and adoption of IFRS 9 has forced banks to adopt a more stringent risk assessment framework, to effectively reduce financial impairments and consequently the provisioning requirements required under the new reporting standard, leading to reduced credit extension

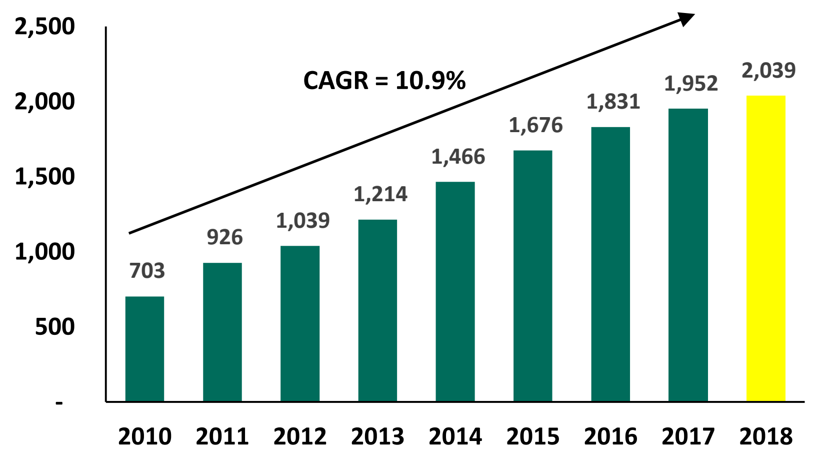
Growth in the Banking sector was realized despite the tough operating environment, characterized by the tighter regulated environment, following the capping of interest rates and compliance to the IFRS 9 standard. Increased usage of alternative channels improves operational efficiency as well as expanding Non-Funded Income. Deteriorating asset quality remains a concern, which has seen banks reduce lending to the riskier private sector and channel more funds to government securities.

III. Listed Banking Sector Metrics

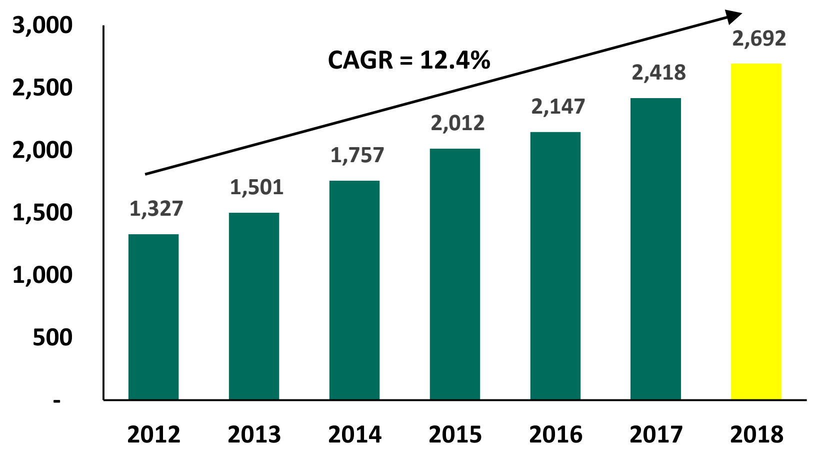
Listed Banking Sector Metrics

Deposit growth has remained strong, faster than the growth in loans and advances. The number of branches has grown slower by 8.3%, with a total of 25 branches closed in 2018

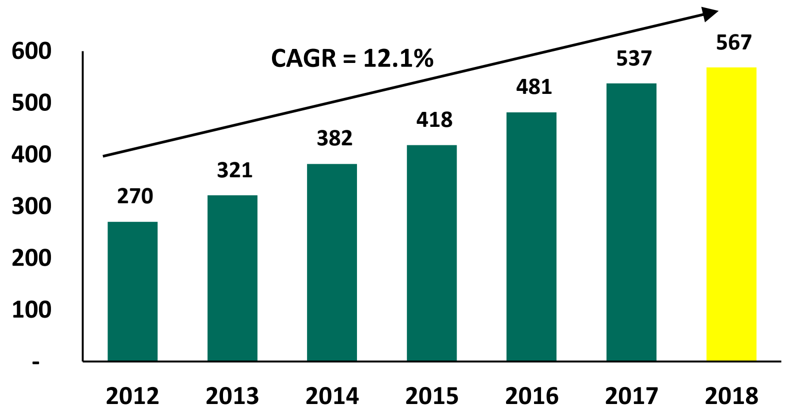
Loans and Advances (Kshs Bn)



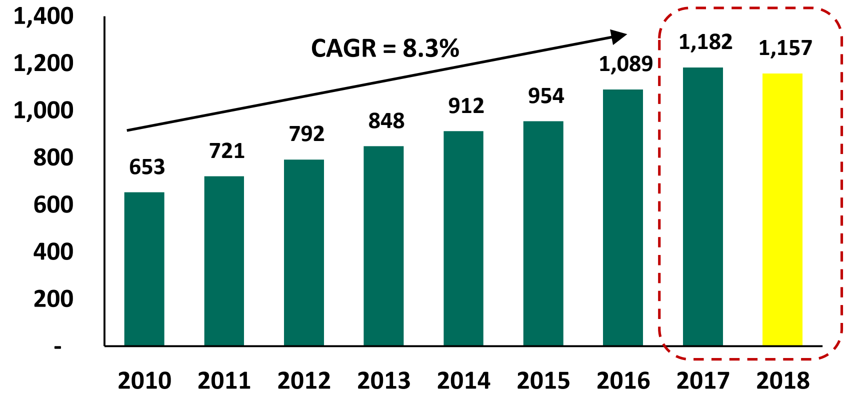
Deposits (Kshs Bn)



Shareholders Equity (Kshs Bn)



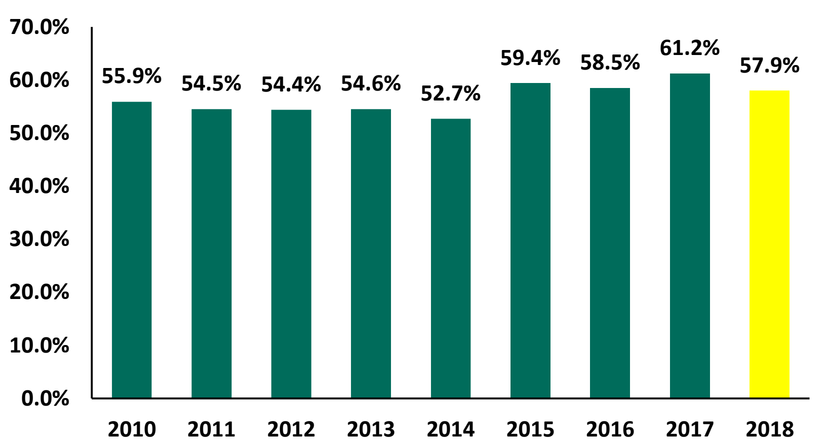
Bank Branches



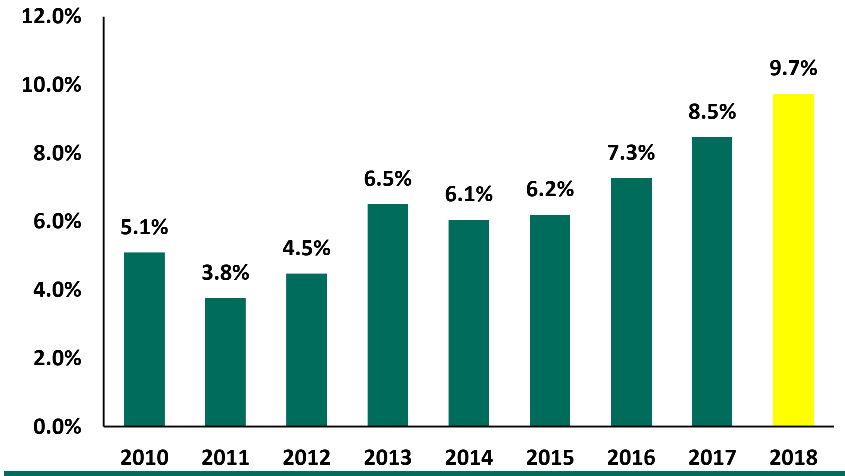
Listed Banking Sector Metrics

Under the current loan pricing framework, there has been reduced lending, leading to a lower NIM, with banks focusing on improving efficiency, amid a tough operating regime leading to asset quality deterioration

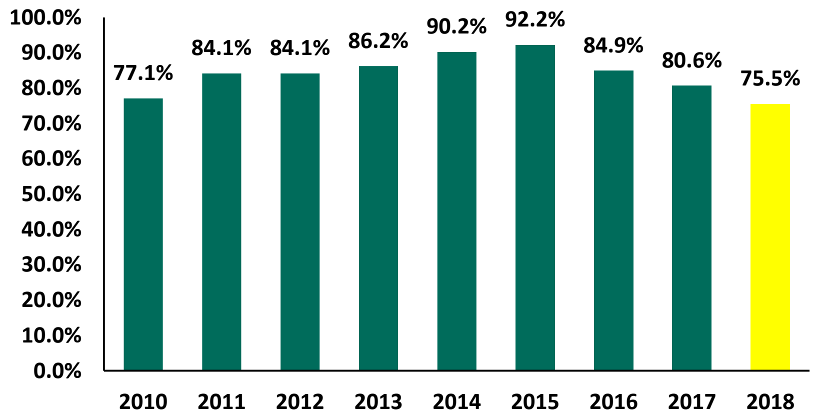
Cost to Income Ratio



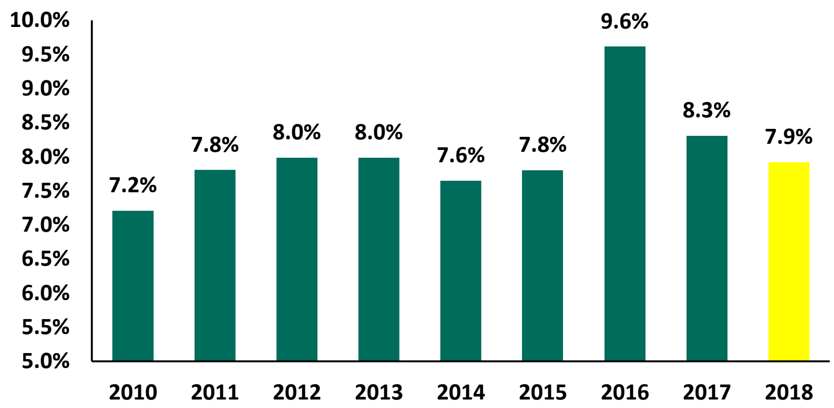
NPL Ratio



Loan to Deposit Ratio



Net Interest Margin



Listed Banks Earnings and Growth Metrics

Kenya's listed banking sector FY'2018 core EPS increased by 13.8% compared to a decline of 9.3% in FY'2017, and consequently the ROaE improved to 19.0% from 17.6% in FY'2017

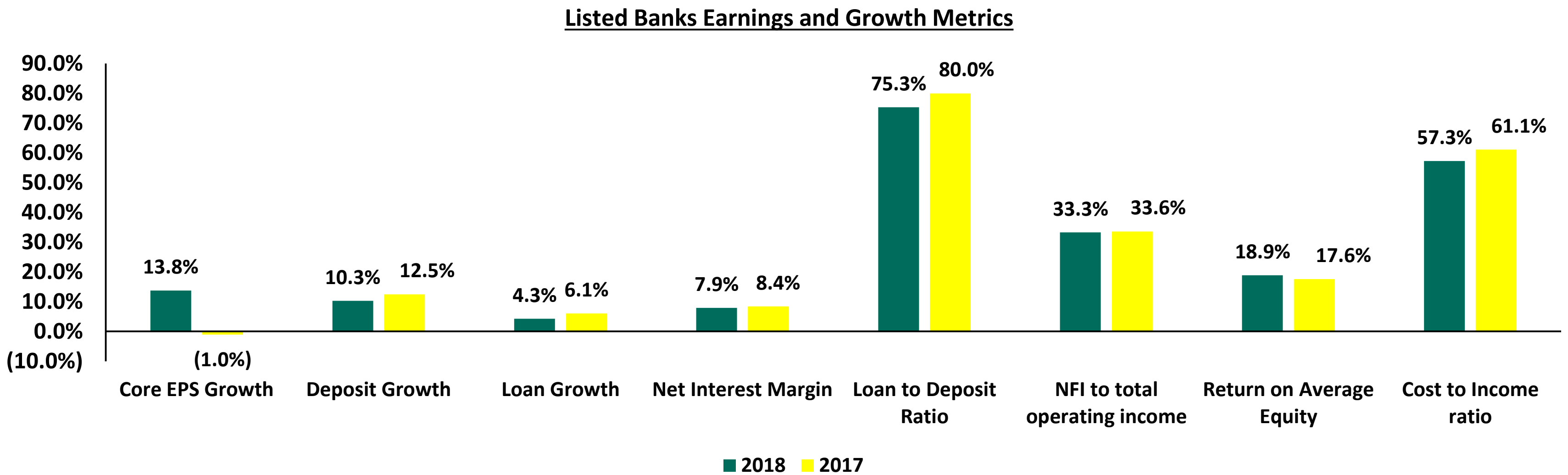
Bank	Core EPS Growth	Net Interest Margin	NFI to Total Operating Income	Deposit Growth	Growth In Govt Securities	Loan Growth	LDR	Return on Average Equity
Stanbic	45.7%	5.0%	45.1%	13.5%	3.7%	22.1%	79.7%	14.3%
NBK	33.5%	6.5%	24.8%	4.9%	29.7%	(3.0%)	66.9%	0.1%
KCB Group	21.8%	8.2%	32.0%	7.6%	9.1%	7.9%	84.8%	21.9%
SCBK	17.1%	7.5%	32.2%	5.1%	(10.7%)	(6.1%)	52.9%	17.5%
I&M	17.1%	6.7%	32.8%	25.9%	0.9%	9.0%	78.2%	17.2%
Co-op Bank	11.6%	9.5%	29.5%	6.5%	16.9%	(3.3%)	80.2%	18.3%
Barclays	7.1%	8.6%	30.6%	11.5%	58.9%	5.3%	85.5%	16.8%
Equity	4.8%	8.5%	38.4%	13.3%	1.9%	6.5%	70.3%	22.5%
DTBK	2.3%	6.2%	21.3%	6.2%	2.6%	(1.5%)	68.3%	13.9%
NIC Group	2.0%	5.7%	30.5%	4.0%	12.9%	(1.4%)	81.7%	12.1%
HF Group	N/A	4.2%	36.8%	(5.3%)	75.0%	(12.5%)	89.1%*	(5.5%)
FY'2018 Average**	**13.8%**	**7.9%**	**33.3%**	**10.3%**	**9.3%**	**4.3%**	**75.3%**	**18.9%**
FY'2017 Average	**(1.0%)**	**8.4%**	**33.6%**	**12.5%**	**22.2%**	**6.1%**	**80.0%**	**17.6%**

**Loans to Loanable funds used owing to nature of the business*

** *The weighted average is based on market capitalization as at 29th March 2019*

Listed Banks Earnings and Growth Metrics Cont…

Listed banks witnessed an improvement in operational efficiency, an improvement in total operating income, and consequently higher profitability in FY'2018 compared to FY'2017



- The improved profitability was driven by the improved operational efficiency, as the Cost to Income Ratio improved to 57.3% from 61.1% in FY'2017, as cost rationalization measures bore fruit, coupled with recovery in interest income as NII grew by 2.5% compared to a 3.8% decline in 2017
- Credit extension however remained subdued as indicated in the decline in the LDR to 75.3% from 80.0% in FY'2017, with banks now channeling funds more actively towards government securities which grew by 9.3% y/y, as loan growth came in at 4.3% a decline from a 6.1% increase in FY'2017. Deposit growth remained strong at 10.3% y/y, albeit slower than the 12.5% growth in FY'2017

Listed Banks Operating Metrics

Non-interest Income currently contributes to 33.3% of banks total operating income, slightly down from 33.6% in FY’2017, owing to the recovery in NII, and slower NFI growth y/y

Bank	Deposit/Branch (bn)	Gross NPL Ratio	NPL Coverage	Tangible Common Ratio	Non Funded Income/Revenue
DTBK	2.1	6.7%	50.6%	13.9%	21.3%
KCB Group	2.1	6.9%	68.0%	15.6%	32.0%
Barclays Bank	2.3	7.4%	69.2%	13.4%	30.6%
Equity Bank	1.5	7.8%	47.3%	15.3%	38.4%
Stanbic Holdings	8.4	9.1%	53.4%	12.1%	45.0%
Coop Bank	2.0	11.3%	48.1%	16.4%	29.5%
I&M Holdings	5.2	13.2%	56.5%	15.2%	32.8%
NIC Bank	2.9	13.4%	43.5%	16.3%	30.5%
SCBK	6.4	16.3%	67.0%	15.8%	32.2%
HF Group	1.6	27.8%	34.5%	15.7%	36.8%
NBK	1.4	47.6%	58.3%	5.0%	24.8%
Weighted Average FY'2018*	**3.1**	**9.7%**	**56.9%**	**15.1%**	**33.3%**

Listed Banks Trading Metrics

The listed banking sector is currently trading at an average P/TBv of 1.4x and average P/E of 7.0x

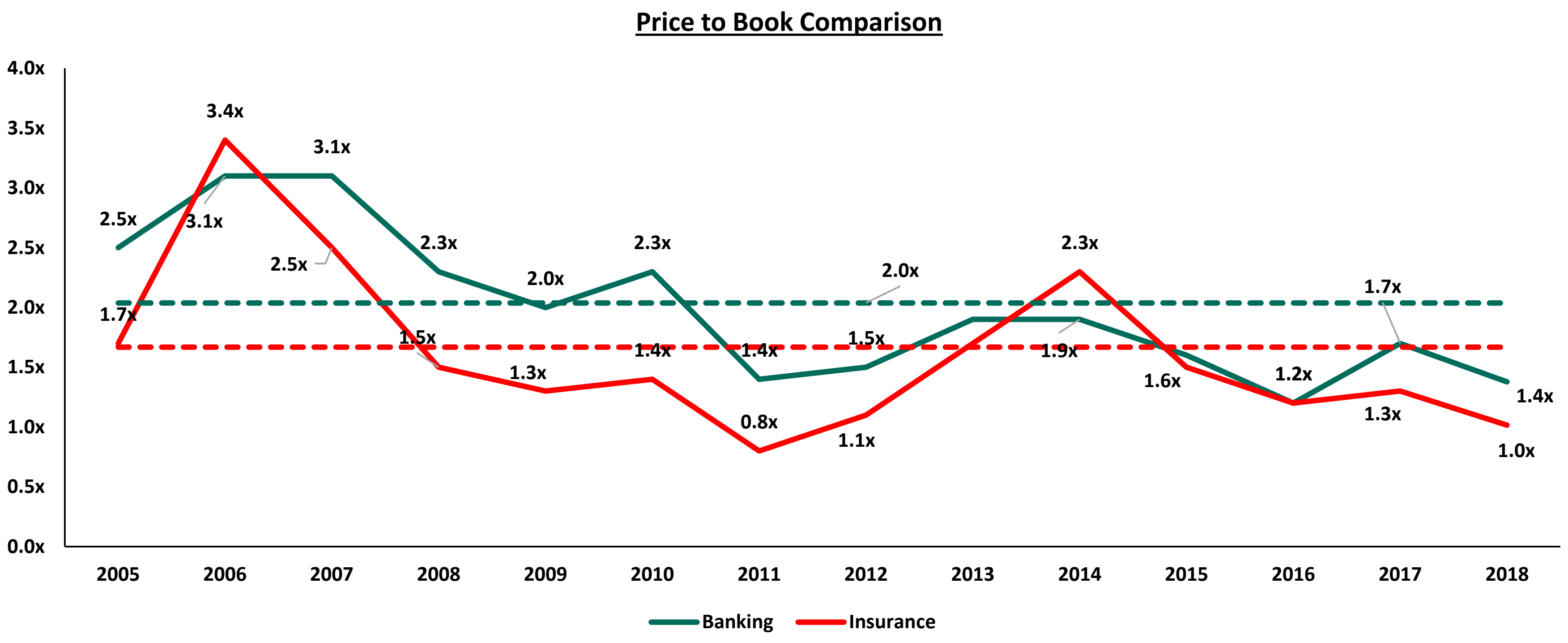
Bank	No. of shares (bn)	Market Cap (bn)	P/E	Price*	P/TBV
HF Group	0.4	1.9	**2.1x**	5.0	**0.2x**
NBK	0.3	1.7	**3.4x**	4.9	**0.3x**
DTBK	0.3	36.3	**5.4x**	130.0	**0.7x**
NIC Group	0.7	25.6	**6.1x**	36.4	**0.8x**
I&M Holdings	0.4	46.9	**5.8x**	113.5	**1.1x**
Stanbic Holdings	0.4	39.5	**6.3x**	100.0	**1.2x**
KCB Group	3.1	135.1	**5.6x**	44.1	**1.2x**
Coop Bank	5.9	87.7	**6.9x**	15.0	**1.3x**
Barclays Bank	5.4	64.1	**8.6x**	11.8	**1.5x**
SCBK	0.3	73.9	**9.1x**	215.3	**1.7x**
Equity Group	3.8	157.0	**7.9x**	41.6	**1.8x**
Weighted Average FY'2018			**7.0x**		**1.4x**

P/E calculation for HF & NBK used normalized earnings over a period of 5 years
**Prices as at 29th March 2019*

Listed Banks & Insurance Trading Metrics

Listed banks trade at an average P/B of 1.4x, higher than the insurance sector which has been priced at 1.0x. Both sectors are trading below their 13-year averages of 2.0x and 1.7x, respectively

13 year Price to Book Value: Banking and Insurance



On a price to book valuation, listed banks are currently priced at a PBV of 1.4x, higher than listed insurance companies at 1.0x, with both lower than their historical averages of 2.0x for the banking sector and 1.7x for the insurance sector

Summary of the FY'2018 Earnings

The sector achieved a higher profitability in FY'2018, as core EPS has increased by 13.8% y/y in FY'2018, compared to a 1.0% decline in 2017

1. The sector continued to have an improved performance relative to 2017, recording a market cap-weighted increase of 13.8% in core earnings per share in FY'2018 compared to a market cap weighted decline of 1.0% in FY'2017, showing that banks are adapting to the regulatory environment after the legislation capping interest rates was passed in August 2016, with the shift in business models bearing fruit, with non-funded revenue expansion and cost rationalization strategies taking effect. The performance was achieved despite the relatively tougher operating environment that was witnessed in 2018

2. The level of NPLs remains a concern within the banking sector, with the weighted average gross Non-Performing Loans (NPL) ratio for the listed banks rising to 9.7%, from 8.5% in FY'2017. Banks cited delays in government payments and spilled over effects of 2017 as the major reasons for the rise in NPLs, in real estate, personal and household, and real estate segments. We expect the level of provisioning to increase going forward as banks continue to adopt IFRS 9 that requires a forward looking approach to estimate credit losses, coupled with increased provisioning for the deteriorating financial assets

3. Deposits grew at a faster pace than loans at 10.3% compared to loans at 4.3%, and slower than 12.5% recorded in FY'2017, indicating reduced intermediation between depositors and credit consumers, with the loan to deposit ratio declining to 75.3% from 80.0% in FY'2017, as government securities investments rose by 10.3%, as banks chased higher risk-adjusted returns

IV. Banks Valuation Reports

Cytonn

Valuation Summary of Listed Banks

Diamond Trust Bank presents the highest upside with an expected total return of 87.8%

Bank	Current Price	Target Price	Upside/ (Downside)	Dividend Yield	Total Return
Diamond Trust Bank	130.0	241.5	85.8%	2.0%	**87.8%**
Equity Group	39.3	58.0	47.9%	5.1%	**53.0%**
I&M Holdings	115.0	167.7	45.8%	3.0%	**48.8%**
KCB Group	45.0	60.0	33.4%	7.8%	**41.2%**
Co-operative Bank	14.2	18.5	30.6%	7.1%	**37.7%**
NIC Group	36.8	48.8	32.6%	3.4%	**36.0%**
Stanbic Holdings	99.0	115.6	16.8%	5.9%	**22.7%**
Barclays Bank	12.0	13.1	9.9%	9.2%	**19.1%**
National Bank of Kenya	4.7	5.2	10.8%	0.0%	**10.8%**
Standard Chartered Bank Kenya	206.0	204.4	(0.8%)	8.8%	**8.1%**
HF Group	4.3	2.9	(31.8%)	0.0%	**(31.8%)**

A. Tier I Banks

Cytonn

I. Equity Group Holdings

Equity Group's Summary of Performance – FY'2018

- Equity Group recorded a Profit before tax growth of 5.9%, to Kshs 28.5 bn, up from Kshs 26.9 bn in FY'2017. Profit after tax grew by 4.8% to Kshs 19.8 bn in FY'2018, from Kshs 18.9 bn in FY'2017,
- Non-Funded Income declined by 6.3% to Kshs 25.9 bn from Kshs 27.6 bn in FY'2017, while Net Interest Income (NII) rose by 10.3% to Kshs 41.4 bn, from Kshs 37.6 bn in FY'2017,
- The bank improved on its operating efficiency, as the Cost to Income Ratio (CIR) improved to 57.7%, from 58.7% in FY'2017. Without LLP, the cost to income ratio improved by a wider margin to 52.2% from 53.5% in FY'2017.
- The balance sheet recorded an expansion as total assets increased by 9.3% to Kshs 573.4 bn, from Kshs 524.5 bn in FY'2017, while total liabilities rose by 10.9% to Kshs 478.4 bn from Kshs 431.3 bn in FY'2017,
- Asset quality deteriorated as Gross Non-Performing Loans (NPLs) increased by 33.6% to Kshs 24.0 bn in FY'2018 from Kshs 18.0 bn in FY'2017,
- Going forward, we expect the bank's growth to be driven by:
    a) 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, and,
    b) 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 in the event of a repeal of the interest rate cap. The bank's balance sheet agility is seen given the bank's high liquidity ratio of 54.1%.

Financial Statements Extracts

Equity Group's PAT is expected to grow at a 5-year CAGR of 16.0%

Income Statement	2017	2018	2019e	2020e
Net Interest Income	37.6	41.4	45.9	51.0
Non Funded Income	27.6	25.9	29.0	33.2
Loan Loss Provision	(3.4)	(3.7)	(3.6)	(3.9)
Other Operating Expenses	(34.8)	(35.1)	(38.2)	(42.1)
Total Operating Expenses	**(38.3)**	**(38.8)**	**(41.9)**	**(46.0)**
Profit Before Tax	26.9	28.5	33.0	38.2
Profit After tax	18.9	19.8	23.1	26.7
% PAT Change YoY	**14.0%**	**4.8%**	**16.6%**	**15.6%**
EPS	5.0	5.3	6.1	7.1
DPS	2.0	2.0	2.0	2.0
Cost to Income	58.7%	57.7%	55.9%	54.6%
NIM	8.9%	8.5%	8.7%	8.6%
ROaE	21.6%	22.5%	22.7%	22.4%
ROaA	3.8%	3.8%	3.8%	3.9%

Balance Sheet	2017	2018e	2019e	2020e
Net Loans and Advances	279.1	297.2	334.4	375.6
Government Securities	128.0	130.4	148.6	165.4
Other Assets	117.4	145.7	159.4	177.6
Total Assets	**524.5**	**573.4**	**642.4**	**718.7**
Customer Deposits	373.1	422.8	475.7	532.8
Other Liabilities	58.2	55.7	56.1	56.2
Total Liabilities	**431.3**	**478.4**	**531.8**	**589.0**
Shareholders Equity	93.1	94.1	109.7	128.8
Book value Per share	24.7	24.9	29.1	34.1
% Change in BPS YoY	**13.6%**	**1.0%**	**16.6%**	**17.5%**

Valuation Summary

Equity Group is undervalued with a potential upside of 53.0%

Cost of Equity Assumptions:	19-Apr-19
Default Spread Adjusted Risk free rate*	13.2%
Beta	0.90
Mature Market Risk Premium	7.6%
Extra Risk Premium	1.0%
Cost of Equity	21.0%

Terminal Assumptions:	
Growth rate	5%
Mature Company Beta	1.00
Terminal Cost of Equity	21.8%
Return on Average Equity 2023	21.9%
Terminal Price to Book value per share	2.0x
Shareholder Equity - FY23e	211.60
Terminal Value-(Year 2023)	448.80

Valuation Summary:	Implied Price	Weighting	Weighted Value
Intergrated DDM	73.0	40.0%	29.2
Residual Income	61.5	35.0%	21.5
PBV Multiple	27.3	20.0%	5.5
PE Multiple	36.6	5.0%	1.8
Fair Value			**58.1**
Current Price			**39.3**
Upside/(Downside)			47.9%
Dividend Yield			5.1%
Total Potential Return			**53.0%**

** Five years average yields on a 10 year Treasury bond*

II. KCB Group

KCB Group Summary of Performance – FY’2018

- Profit before tax increased by 16.3% to Kshs 33.9 bn, up from Kshs 29.1 bn in FY’2017. Profit after tax grew by 21.8% to Kshs 24.0 bn in FY’2018, from Kshs 19.7 bn in FY’2017
- The bank recorded a 0.1% decline in Non-Funded Income (NFI) % to Kshs 22.97 bn, from Kshs 23.0 bn in FY’2017, and o a 0.9% increase in Net Interest Income (NII) to Kshs 48.8 bn, from Kshs 48.4 bn in FY’2017
- Total operating expenses declined by 10.2% to Kshs 37.9 bn, from Kshs 42.3 bn, largely driven by a 50.2% decline in Loan Loss Provisions (LLP) to Kshs 2.9 bn in FY’2018, from Kshs 5.9 bn in FY’2017, coupled with an 11.2% decline in staff costs to Kshs 17.0 bn in FY’2018, from Kshs 19.1 bn in FY’2017
- Consequently, the Cost to Income Ratio (CIR) improved to 52.8%, from 59.2% in FY’2017. Without LLP, the cost to income ratio also improved to 48.7%, from 50.9% in FY’2017,
- The balance sheet recorded an expansion as total assets increased by 10.5% to Kshs 714.3 bn from Kshs 646.7 bn in FY’2017.
- The bank’s asset quality improved, with the NPL ratio improving to 6.9% from 8.4% in FY’2017. The improved NPL ratio was mainly attributed to an improvement in the corporate loan book’s NPL ratio to 8.5% in FY’2018 from in 11.0% in ’2017, as well as the SME and Micro loan book, which improved to 13.0% in FY’2018, down from 16.4% in FY’2017.
- Going forward, we expect the bank’s growth to be driven by:
    a) Increased Channel diversification, which is likely to help the bank to continue improving its operational efficiency. The benefits of this are already being felt, as the bank aligned its staff head count to its operational needs, which led to lower staff cost demands

Financial Statements Extracts

KCB Group's PAT is expected to grow at a 5-year CAGR of 9.8%

Income Statement	2017	2018	2019f	2020F
Net Interest Income	48.4	48.8	55.5	60.6
Non Funded Income	23.0	23.0	25.2	27.3
Total Operating Income	71.4	71.8	80.7	87.9
Loan Loss Provision	5.9	2.9	4.7	5.1
Other Operating Expenses	36.4	35.0	38.5	40.9
Total Operating Expenses	**42.3**	**37.9**	**43.2**	**46.0**
Profit Before Tax	29.1	33.9	37.5	41.9
Profit After tax	19.7	24.0	26.2	29.3
% PAT Change YoY	**(0.1%)**	**21.8%**	**9.3%**	**11.9%**
EPS	6.3	7.7	8.4	9.4
DPS	3.0	3.5	4.0	4.5
Cost to Income	59.2%	52.8%	53.6%	52.3%
ROE	19.5%	21.9%	21.7%	21.7%
ROA	3.2%	3.6%	3.7%	4.0%

Balance Sheet	2017	2018	2019f	2020f
Net Loans and Advances	422.7	455.9	492.5	527.2
Government Securities	110.0	120.1	128.4	140.2
Total Assets	**646.7**	**714.3**	**771.7**	**830.8**
Customer Deposits	499.5	537.5	576.6	618.7
Total Liabilities	**540.7**	**600.7**	**644.1**	**688.0**
Shareholders Equity	**106.0**	**113.7**	**127.6**	**142.8**
Book value Per share	34.1	36.6	41.1	46.0
% Change in BPS YoY	**9.7%**	**7.3%**	**12.2%**	**12.0%**

Valuation Summary

KCB Group is undervalued with a total potential return of 41.2%

Cost of Equity Assumptions:	18/04/2019
Default Spread Adjusted Risk free rate	13.2%
Beta	0.9
Market Risk Premium	7.6%
Cost of Equity	20.1%

Terminal Assumptions:	
Growth rate	5%
Mature Company Beta	1.0
Terminal Cost of Equity	20.8%
Return on Average Equity 2023	20.6%
Terminal Price to Book value per share	1.4x
Shareholder Equity - FY23e	195.7
Terminal Value - (Year 2023)	296.8

Valuation Summary	Implied Price	Weighting	Weighted Value
Residual Income	62.1	35%	21.7
PBV Multiple	49.0	20%	9.8
PE Multiple	58.2	5%	2.9
DDM Integrated	63.9	40%	25.5
Target Price			**60.0**
Current Price			**45.0**
Upside/(Downside)			33.3%
Dividend Yield			7.8%
Total Return			**41.2%**

** Five years average yields on a 10 year Treasury bond*

III. Co-operative Bank

Co-operative Bank's Summary of Performance – FY'2018

- Co-operative Bank recorded a profit before tax increase of 10.7% to Kshs 18.2 bn, up from Kshs 16.4 bn in FY'2017, and a profit after tax increase of 11.6% to Kshs 12.7 bn in FY'2018, from Kshs 11.4 bn in FY'2017,
- Non-Funded Income (NFI) declined by 4.4% to Kshs 12.9 bn, from Kshs 13.5 bn in FY'2017., while Net Interest Income (NII) rose by 9.5% to Kshs 30.8 bn from Kshs 28.1 bn in FY'2017,
- The Cost to Income Ratio (CIR) improved to 58.8%, from 60.9% in FY'2017. However, without LLP, the cost to income ratio deteriorated to 54.6%, from 52.2% in FY'2017,
- The balance sheet recorded an expansion as total assets increased by 6.9% to Kshs 413.4 bn from Kshs 386.9 bn in FY'2017, while Total liabilities rose by 8.1% to Kshs 342.2 bn from Kshs 316.6 bn in FY'2017,
- The bank experienced a deterioration in asset quality, as the Gross Non-Performing Loans (NPLs) increased by 56.7% to Kshs 29.4 bn in FY'2018 from Kshs 18.8 bn in FY'2017,
- Going forward, we expect the bank's growth to be driven by:
  a) **Branch Transformation and deepening financial inclusion**: Increased focus on branch transformation and innovation centered on alternative channels will continue to drive NFI growth as well as transform braches to handle advisory, wealth management and advisory services,
  b) **Enhanced Credit Management**: The bank continues to manage its loan portfolio through cherry-picking of loan issuances, proactive debt management such as loan due reminders, enhancement of systems, processes and tooling to support credit management mainly loan origination process, and sustained collections. This could help the bank manage its asset quality, which has been pressured by the relatively tougher economic environment

Financial Statements Extracts

Co-operative Bank's PAT is expected to grow at a 5-year CAGR of 10.0%

Income Statement	2017	2018	2019	2020
Net Interest Income	28.1	30.8	33.3	35.7
Non Funded Income	13.5	12.9	14.1	15.6
Loan Loss Provision	3.6	1.8	3.1	3.3
Other Operating Expenses	21.7	23.9	24.4	26.7
Total Operating Expenses	25.3	25.7	27.5	30.0
Profit Before Tax	16.4	18.2	20.1	21.5
Profit After tax	11.4	12.7	14.0	15.1
% PAT Change YoY	**-10.0%**	**11.6%**	**10.2%**	**7.3%**
EPS	2.3	2.6	2.9	3.1
DPS	1.0	1.2	1.2	1.2
Cost to Income	60.9%	58.8%	58.1%	58.4%
NIM	8.8%	9.5%	9.2%	9.3%
ROE	17.4%	18.3%	18.3%	17.0%
ROA	3.1%	3.3%	3.2%	3.2%

Balance Sheet	2017	2018	2019f	2020f
Net Loans and Advances	253.9	245.4	268.4	279.1
Government Securities	44.0	49.7	54.4	57.0
Other Assets	89.0	118.3	136.8	149.8
Total Assets	**386.9**	**413.4**	**459.6**	**485.8**
Customer Deposits	287.4	306.1	337.9	354.8
Other Liabilities	29.2	36.1	36.4	36.6
Total Liabilities	**316.6**	**342.2**	**374.3**	**391.4**
Shareholders Equity	69.6	69.9	83.9	93.1
Book value Per share	14.2	14.3	17.2	19.0

Valuation Summary

Co-op Bank is undervalued with a potential upside of 37.7%

Cost of Equity Assumptions:	4/19/2019
Default Spread Adjusted Risk free rate*	13.2%
Beta	0.9
Mature Market Risk Premium	7.6%
Extra Risk Premium	0.9%
Cost of Equity	20.9%

Terminal Assumptions:	
Growth rate	5%
Mature Company Beta	1.0
Terminal Cost of Equity	21.7%
Return on Average Equity 2023	15.5%
Terminal Price to Book value per share	1.5x
Shareholder Equity - FY23e	122.82
Terminal Value-(Year 2023)	192.8

Valuation Summary:	Implied Price	Weighting	Weighted Value
DDM Integrated	21.96	40%	8.78
Residual income	16.51	35%	5.78
PBV Multiple	15.64	20%	3.13
PE Multiple	15.82	5%	0.79
Target Price			**18.5**
Current Price			**14.2**
Upside/(Downside)			30.6%
Dividend Yield			7.1%
Total Return			**37.7%**

** Five years average yields on a 10 year Treasury bond*

IV. NIC Group

NIC Group Summary of Performance – FY’2018

- Profit before tax increased by 4.0% to Kshs 5.8 bn, from Kshs 5.6 bn in FY’2017. Profit after tax grew by 2.0% to Kshs 4.2 bn in FY’2018, from Kshs 4.1 bn in FY’2017
- The bank recorded an 11.4% increase in Non-Funded Income (NFI) % to Kshs 4.6 bn, from Kshs 4.2 bn in FY’2017, and a 1.8% decline in Net Interest Income (NII) o Kshs 10.6 bn, from Kshs 10.8 bn in FY’2017
- Total operating expenses increased by 0.6% to Kshs 9.4 bn, from Kshs 9.3 bn, largely driven by a 13.6% rise in staff costs to Kshs 3.6 bn from Kshs 3.2 bn in FY’2017, and a 7.9% rise in other operating expenses to Kshs 3.4 bn from Kshs 3.2 bn. This offset the 21.0% decline in Loan Loss Provisions (LLP) to Kshs 2.4 bn in FY’2018, from Kshs 3.0 bn in FY’2017
- Consequently, the Cost to Income Ratio (CIR) improved to 61.7%, from 62.5% in FY’2017. Without LLP, the cost to income however deteriorated to 46.3%, from 42.6% in FY’2017,
- The balance sheet recorded an expansion as total assets increased by 1.1% to Kshs 208.5 bn from Kshs 206.2 bn in FY’2017.
- The bank’s asset quality deteriorated, with the NPL ratio rising to 13.4% from 11.3% in FY’2017. The deteriorating NPL ratio is attributable to a 17.6% rise in gross non-performing loans to Kshs 16.8 bn from Kshs 14.3 bn in FY’2017
- Going forward, we expect the bank’s growth to be driven by:
    a) Synergies arising from the merger between the Bank and CBA group. Some of the potential growth synergies expected to enhance profitability and shareholder value

NIC/CBA Merged Financial Statements

NIC Group's PAT is expected to grow at a 5-year CAGR of 11.8%

Income Statement	2017	2018	2019f	2020f
Net Interest Income	20.4	20.3	22.3	25.6
Non Funded Income	14.6	16.1	17.0	18.6
Loan Loss Provision	6.0	6.1	6.3	6.7
Total Operating Expenses	22.7	24.1	25.0	27.4
Profit Before Tax	12.4	12.3	14.2	16.8
Profit After tax	8.2	8.9	10.0	11.8
% PAT Change YoY		**9.3%**	**11.3%**	**18.0%**
EPS	12.8	14.0	15.6	18.4
DPS	1.0	0.0	1.1	1.1
Cost to Income	64.7%	66.3%	63.8%	62.0%
NIM	5.6%	5.2%	5.4%	5.8%
ROE	13.6%	13.7%	14.1%	14.5%
ROA	1.9%	2.0%	2.1%	2.3%

Balance Sheet	2017	2018e	2019f	2020f
Net Loans and Advances	233.4	239.6	258.2	280.8
Government Securities	120.2	129.7	141.1	153.2
Other Assets	98.3	84.3	81.8	93.7
Total Assets	**452.0**	**453.6**	**481.1**	**527.7**
Customer Deposits	332.7	341.0	363.7	392.8
Other Liabilities	54.4	46.2	41.8	48.3
Total Liabilities	**387.1**	**387.2**	**405.5**	**441.0**
Shareholders Equity	64.4	66.0	75.3	86.3
Book value Per share	7.19	7.37	8.41	9.64
% Change in BVPS	**14.8%**	**2.5%**	**14.0%**	**14.7%**

Valuation Summary

NIC Group is undervalued with a total potential return of 36.0%

Cost of Equity Assumptions:	
Default Spread Adjusted Risk free rate	13.20%
Beta	1.00
Mature Market Risk Premium	7.6%
Extra Risk Premium	1.0%
Cost of Equity	21.8%

Terminal Assumptions:	
Growth rate	5%
Mature Company Beta	1.00
Terminal Cost of Equity	21.8%
Return on Average Equity 2023	13.0%
Terminal Price to Book	0.9x
Shareholder Equity - FY23e	127.2
Terminal Value-(Year 2023)	121.5

Valuation Summary	Implied Price	Weighting	Weighted Value
DDM Integrated	53.6	40%	21.4
Residual Valuation	36.5	35%	12.8
PBV Multiple	64.0	20%	12.8
PE Multiple	90.9	5%	4.5
Target Price			**48.8**
Current Price			**36.8**
Upside/(Downside)			32.6%
Dividend Yield			3.4%
Total Potential Return			**36.0%**

** Five years average yields on a 10 year Treasury bond*

V. Standard Chartered Bank Kenya

SCBK's Summary of Performance – FY'2019

- Profit before tax increased by 17.6% to Kshs 11.9 bn, from Kshs 10.1 bn in FY'2017. Profit after tax grew by 17.1% to Kshs 8.1 bn in FY'2018, from Kshs 6.9 bn in FY'2017
- The bank recorded a 4.9% increase in Non-Funded Income (NFI) to Kshs 9.2 bn from Kshs 8.8 bn in FY'2017, and a 4.5% increase in Net Interest Income (NII) to Kshs 19.4 bn, from Kshs 18.6 bn in FY'2017
- The bank recorded a decline in efficiency levels as the cost to income ratio without LLP worsened to 51.8% from 47.9% in FY'2017. The deterioration was largely attributable to a 9.5% rise in staff costs coupled with a 17.3% rise in other operating expenses, which depressed the bottom line. The rising inefficiency was largely due to the bank's investment in the development of robust ICT systems so as to enhance service delivery to clients
- The balance sheet recorded a slight contraction as total assets declined by 0.1% to Kshs 285.4 bn, from Kshs 285.7 bn in FY'2017
- The bank's asset quality deteriorated, with the NPL ratio rising to 16.3%, from 12.6% in FY'2017. The deteriorating NPL ratio is attributable to a 22.9% rise in gross non-performing loans to Kshs 21.7 bn, from Kshs 17.6 bn in FY'2017m due to recovery problems of loans made to key troubled sectors such as real estate and manufacturing
- Going forward, we expect the bank's growth to be driven by:
    a) Continued focus on promoting the usage of the bank's alternative channels is likely to continue boosting the company's Non-Funded Income (NFI) as well as aiding in improving operational efficiency levels

Financial Statements Extracts

SCBK's PAT is expected to grow at a 5-year CAGR of 8.2%

Income Statement	2017	2018	2019f	2020f
Net Interest Income	18.6	19.4	19.8	19.5
Non Funded Income	8.8	9.2	9.1	9.7
Loan Loss Provision	4.2	1.9	2.9	3.1
Other Operating Expenses	13.1	14.8	14.4	14.7
Total Operating Expenses	**17.3**	**16.8**	**17.4**	**17.8**
Profit Before Tax	10.1	11.8	11.5	11.5
Profit After tax	6.9	8.1	7.9	7.8
% PAT Change YoY	**-23.6%**	**17.1%**	**-2.9%**	**-0.5%**
EPS	20.1	23.6	22.9	22.8
DPS	17.0	19.0	17.2	17.1
Cost to Income	63.2%	58.6%	60.2%	60.8%
NIM	7.9%	7.5%	8.3%	8.4%
ROaE	15.4%	17.5%	16.5%	15.8%
ROaA	2.6%	2.8%	2.7%	2.6%

Balance Sheet	2017	2018	2019f	2020f
Net Loans and Advances	126.3	118.7	120.1	131.5
Government Securities	110.5	98.7	94.2	99.3
Other assets	48.9	68.0	84.3	82.4
Total Assets	**285.7**	**285.4**	**298.6**	**313.3**
Customer Deposits	213.3	224.3	235.5	248.2
Other Liabilities	26.7	14.5	14.5	14.5
Total Liabilities	**240.1**	**238.8**	**250.0**	**262.7**
Shareholders Equity	45.7	46.6	48.6	50.6

Valuation Summary

SCBK is undervalued with a total potential total return of 8.1%

Cost of Equity Assumptions:	18-April-2019
Default Spread Adjusted Risk free rate *	13.2%
Beta	0.8
Mature Market Risk Premium	7.64%
Extra Risk Premium	0.0%
Cost of Equity	19.3%

Terminal Assumptions:	
Growth rate	5%
Mature Company Beta	1.00
Terminal Cost of Equity	20.9%
Return on Average Equity 2023	21.6%
Terminal Price to Book value per share	1.7x
Shareholder Equity - FY23e	58.34
Terminal Value-(Year 2023)	96.12

Valuation Summary	Implied Price	Weighting	Weighted Value
DDM Integrated	218.04	40%	87.22
Residual Income	195.63	35%	68.47
PBV Multiple	195.04	20%	39.01
PE Multiple	182.06	5%	9.10
Target Price			**203.8**
Current Price			**206.0**
Upside/(Downside)			(1.1%)
Dividend Yield			9.2%
Total Return			**8.1%**

** Five years average yields on a 10 year Treasury bond*

VI. Diamond Trust Bank Kenya

DTBK's Summary of Performance – FY'2018

- DTBK recorded a Profit before tax increase of 8.9% to Kshs 11.0 bn, up from Kshs 10.1 bn in FY'2017. Profit after tax grew by 2.3% to Kshs 7.1 bn in FY'2018, from Kshs 6.9 bn in FY'2017,
- Non-Funded Income (NFI) rose by 3.0% to Kshs 5.4 bn, from Kshs 5.3 bn in FY'2017, while Net Interest Income (NII) rose by 1.8% to Kshs 20.0 bn, from Kshs 19.7 bn in FY'2017,
- The Cost to Income Ratio (CIR) improved to 56.9%, from 59.6% in FY'2017. However, without LLP, the cost to income ratio deteriorated to 45.2%, from 42.3% in FY'2017
- The balance sheet recorded an expansion as total assets increased by 4.0% to Kshs 377.7 bn from Kshs 363.3 bn in FY'2017 while Total liabilities rose by 2.9% to Kshs 318.8 bn from Kshs 309.7 bn in FY'2017
- The bank experienced an improvement in its asset quality as the Gross Non-Performing Loans (NPLs) declined by 8.2% to Kshs 13.6 bn in FY'2018 from Kshs 14.8 bn in FY'2017,
- Going forward, we expect the bank's growth to be driven by:

    Geographical diversification: The bank's forays into other markets such as Tanzania, Uganda and Burundi, may aid the bank's growth, given the lack of loan pricing controls in those markets. Continued focus on those markets would aid in alleviating the compressed interest income regime in the Kenyan market.

Financial Statements Extracts

DTBK's PAT is expected to grow at a 5-year CAGR of 8.0%

Income Statement	2017	2018	2019e	2020e
Net Interest Income	19.7	20.0	20.6	22.5
Non Funded Income	5.3	5.4	5.7	4.8
Loan Loss Provision	(4.3)	(3.0)	(4.4)	(3.2)
Other Operating Expenses	(10.6)	(11.5)	(11.6)	(12.3)
Total Operating Expenses	**(14.9)**	**(14.5)**	**(15.9)**	**(15.6)**
Profit Before Tax	10.1	11.0	10.4	11.7
Profit After tax	6.9	7.1	7.1	8.0
% PAT Change YoY	**-10.3%**	**2.3%**	**0.2%**	**12.1%**
EPS	24.8	25.3	25.4	28.4
DPS	2.6	2.6	2.7	3.0
Cost to Income	(42.3%)	(45.2%)	(43.9%)	(45.3%)
NIM	6.5%	6.2%	6.2%	6.3%
ROaE	12.9%	13.1%	11.8%	11.9%
ROaA	2.0%	1.8%	1.7%	1.8%

Balance Sheet	2017	2018e	2019e	2020e
Net Loans and Advances	196.0	193.1	206.6	226.2
Government Securities	114.4	117.3	122.4	133.6
Other Assets	52.9	67.3	74.0	75.6
Total Assets	**363.3**	**377.7**	**402.9**	**435.4**
Customer Deposits	266.2	282.9	300.2	325.7
Other Liabilities	43.4	35.9	37.1	37.3
Total Liabilities	**309.7**	**318.8**	**337.3**	**363.1**
Shareholders Equity	48.4	53.7	60.4	67.1
Book value Per share	173.0	191.9	215.9	239.9
% Change in BPS YoY	**17.9%**	**10.9%**	**12.5%**	**11.1%**

Valuation Summary

DTBK is undervalued with a potential upside of 87.8%

Cost of Equity Assumptions:	19-Apr-19
Default Spread Adjusted Risk free rate*	13.2%
Beta	0.90
Mature Market Risk Premium	7.6%
Extra Risk Premium	1.0%
Cost of Equity	21.0%

Terminal Assumptions:	
Growth rate	5%
Mature Company Beta	1.00
Terminal Cost of Equity	21.8%
Return on Average Equity 2023	21.9%
Terminal Price to Book value per share	2.0x
Shareholder Equity - FY23e	211.60
Terminal Value-(Year 2023)	448.80

Valuation Summary:	Implied Price	Weighting	Weighted Value
DDM Integrated	255.0	40.0%	102.0
Residual Income	213.0	35.0%	74.6
PBV Multiple	279.1	20.0%	55.8
PE Multiple	182.9	5.0%	9.1
Target Price			**241.5**
Current Price			**130.0**
Upside/(Downside)			85.8%
Dividend yield			2.0%
Total return			**87.8%**

** Five years average yields on a 10 year Treasury bond*

VII. Barclays Bank of Kenya

Barclays Bank's Summary of Performance – FY'2018

- Barclays Bank recorded a Profit before tax increase of 2.7% to Kshs 10.7 bn, up from Kshs 10.4 bn in FY'2017. Profit after tax grew by 7.1% to Kshs 7.4 bn in FY'2018, from Kshs 6.9 bn in FY'2017,
- Non-Funded Income (NFI) rose by 14.7% to Kshs 9.7 bn, from Kshs 8.5 bn in FY'2017, while Net Interest Income (NII) rose by 0.9% to Kshs 22.0 bn from Kshs 21.8 bn in FY'2017,
- Cost to Income Ratio (CIR) deteriorated albeit marginally to 66.4%, from 65.8% in FY'2017. Without LLP, the cost to income ratio improved to 54.2%, from 55.5% in FY'2017,
- The balance sheet recorded an expansion as total assets increased by 19.8% to Kshs 324.8 bn from Kshs 271.2 bn in FY'2017, while Total liabilities rose by 23.6% to Kshs 280.6 bn from Kshs 227.1 bn in FY'2017,
- The bank experienced a deterioration in asset quality, with Gross Non-Performing Loans (NPLs) rising by 10.3% to Kshs 13.9 bn in FY'2018 from Kshs 12.6 bn in FY'2017,
- Going forward, we expect the bank's growth to be driven by:
    a) **Increased Channel diversification**, which is likely to help the bank to continue improving its operational efficiency. The benefits of this are already being felt with "Timiza" already recording an accelerated growth, and consequently higher Non-Interest Revenue. This, coupled with the expansion of its agent banking network and product offerings such as banc assurance and fixed income trading will see the bank expand its topline revenue, going forward.

Financial Statements Extracts

Barclays Bank's PAT is expected to grow at a 5-year CAGR of 8.0%

Income Statement	2017	2018	2019f	2020f
Net Interest Income	21.8	22.0	24.0	23.9
Non Funded Income	8.5	9.7	10.4	11.5
Total Operating Income	**30.3**	**31.7**	**34.4**	**35.4**
Loan Loss Provision	(3.1)	(3.9)	(4.0)	(4.0)
Other Operating Expenses	(16.8)	(17.2)	(18.4)	(19.0)
Total Operating Expenses	**(19.9)**	**(21.0)**	**(22.3)**	**(22.9)**
Profit Before Tax	10.4	10.6	12.0	12.4
Profit After tax	**6.9**	**7.4**	**8.4**	**8.7**
% PAT Change YoY	**-6.4%**	**7.1%**	**13.6%**	**3.4%**
EPS	1.3	1.4	1.6	1.6
DPS	1.0	1.1	1.2	1.3
Cost to Income	65.8%	66.4%	65.0%	64.8%
NIM	9.7%	8.6%	8.8%	8.7%
ROaE	16.0%	16.8%	17.4%	17.3%
ROaA	2.7%	2.7%	2.8%	2.8%

Balance Sheet	2017	2018	2019f	2020f
Net Loans and Advances	168.4	177.4	183.9	194.0
Government Securities	58.5	92.9	75.5	77.4
Other Assets	44.3	54.5	85.5	87.7
Total Assets	**271.2**	**324.8**	**344.9**	**359.0**
Customer Deposits	186.0	207.4	218.9	230.9
Other Liabilities	41.1	73.2	73.4	73.7
Total Liabilities	**227.1**	**280.6**	**292.3**	**304.6**
Shareholders Equity	44.1	44.2	52.6	54.4
Book value Per share	8.1	8.1	9.7	10.0

Valuation Summary

Barclays Bank is undervalued with a potential upside of 19.1%

Cost of Equity Assumptions:	19-Apr-19
Default Spread Adjusted Risk free rate	13.2%
Beta	0.90
Mature Market Risk Premium	7.6%
Extra Risk Premium	0.0%
Cost of Equity	19.0%

Terminal Assumptions:	
Growth rate	5.0%
Mature Company Beta	100.0%
Terminal Cost of Equity	20.8%
Return on Average Equity 2022	20.0%
Terminal Price to Book value per share	1.6x
Shareholder Equity - FY23e	60.6
Terminal Value-(Year 2021)	104.8

Valuation Summary:	Implied Price	Weighting	Weighted Value
DDM Integrated	13.9	40%	5.5
Residual Income	14.4	35%	5.0
PBV Multiple	10.4	20%	2.1
PE Multiple	9.3	5%	0.5
Target Price			**13.1**
Current Price			**12.0**
Upside/(Downside)			9.9%
Dividend Yield			9.2%
Total Return			**19.1%**

** Five years average yields on a 10 year Treasury bond*

VIII. Stanbic Holdings

Stanbic Holding's Summary of Performance – FY'2018

- Stanbic Holdings recorded a profit before tax increase of 65.7% to Kshs 8.9 bn from Kshs 5.4 bn, and a profit after tax (PAT) increase of 45.7% to Kshs 6.3 bn from Kshs 4.3 bn in FY'2017,
- Non-funded income (NFI) rose by 18.3% to Kshs 10.0 bn from Kshs 8.4 bn in FY'2017, while Net Interest Income (NII) rose 14.0%
- The Cost to Income Ratio (CIR) improved to 59.5% from 71.7% in FY'2017. Without LLP, the cost to Income ratio also improved to 50.2% from 57.2% in FY'2017
- The balance sheet recorded a contraction as total assets declined by 10.4% to Kshs 60.5 bn, from Kshs 67.5 bn in FY'2017 while Total liabilities increased by 19.5% to Kshs 246.0 bn from Kshs 205.8 bn in FY'2017,
- The bank experienced a deterioration in asset quality, with Gross Non-Performing Loans (NPLs) rising by 60.7% to Kshs 16.6 bn from Kshs 10.4 bn in FY'2017
- Going forward, we expect the bank's growth to be driven by:
    a) **Efficient operating** model-The bank's increased focus on cost containment is likely to boost the bank's growth prospects, as it looks to drive its strategy of increased deposit mobilization capacity and lending. The bank bucked the decline in loans trend in the sector, and recorded a 22.1% growth in loans. This will likely ring in additional interest income, thereby improving the top line revenue. Furthermore, the banks well diversified revenue structure will likely buffer the bottom in the event of a significant decline in one of the revenue streams

Financial Statements Extracts

Stanbic Holdings is expected to grow at a 5-year CAGR of 10.0%

Income Statement	2017	2018	2019e	2020e
Net Interest Income	10.6	12.1	13.1	14.7
Non Funded Income	8.4	10.0	11.5	12.9
Loan Loss Provision	(2.8)	(2.1)	(2.7)	(2.9)
Total Operating Expenses	**(13.7)**	**(13.1)**	**(15.1)**	**(16.9)**
Profit Before Tax	5.4	9.0	9.5	10.7
Profit After tax	4.3	6.3	6.7	7.5
% PAT Change YoY	**-2.5%**	**45.8%**	**6.1%**	**12.1%**
EPS	10.9	15.9	16.9	18.9
DPS	5.3	5.8	5.8	5.8
Cost to Income	57.2%	50.2%	50.5%	51.0%
NIM	**5.1%**	**5.0%**	**4.9%**	**4.9%**
ROaE	10.4%	14.3%	14.2%	14.5%
ROaA	1.9%	2.3%	2.2%	2.2%

Balance Sheet	2017	2018e	2019e	2020e
Net Loans and Advances	143.3	175.0	179.9	200.8
Other Assets	105.5	115.6	138.3	151.7
Total Assets	**248.7**	**290.6**	**318.2**	**352.5**
Customer Deposits	193.4	219.5	242.7	271.9
Borrowings	4.0	7.1	7.1	7.1
Other Liabilities	8.4	19.4	19.4	19.4
Total Liabilities	**205.8**	**245.9**	**269.2**	**298.3**
Shareholders Equity	43.0	44.6	49.0	54.2
Book value Per share	108.7	112.9	123.9	137.0
% Change in BVPS	**7.0%**	**3.9%**	**9.8%**	**10.6%**

Valuation Summary

Stanbic Holdings is undervalued with a potential upside of 22.7%

Cost of Equity Assumptions:	19-Apr-19
Default Spread Adjusted Risk free rate*	13.2%
Beta	0.8
Mature Market Risk Premium	7.6%
Extra Risk Premium	1.0%
Cost of Equity	20.1%

Terminal Assumptions:	
Growth rate	5%
Mature Company Beta	1.0
Terminal Cost of Equity	21.8%
Return on Average Equity 2023f	14.3%
Terminal Price to Book value per share	1.1x
Shareholder Equity - FY23e	75.0
Terminal Value-(Year 2023)	86.6

Valuation Summary:	Implied Price	Weighting	Weighted Value
DDM Integrated	132.1	40%	52.9
Residual income	119.3	35%	41.8
PBV Multiple	81.5	20%	16.3
PE Multiple	94.4	5%	4.7
Target Price			**115.6**
Current Price			**99.0**
Upside/(Downside)			16.8%
Dividend Yield			5.9%
Total return			**22.7%**

** Five years average yields on a 10 year Treasury bond*

B. Tier II Banks

I. I&M Holdings

I&M Holdings Summary of Performance – FY’2018

- Profit before tax increased by 16.2% to Kshs 11.5 bn, up from Kshs 9.9 bn in FY’2017. Profit after tax grew
- by 17.1% to Kshs 8.5 bn in FY’2018, from Kshs 7.3 bn in FY’2017
- The bank recorded a a 31.8% increase in Non-Funded Income (NFI) to Kshs 7.6 bn from Kshs 5.8 bn in FY’2017, and a a 0.3% increase in Net Interest Income (NII) to Kshs 15.6 bn from Kshs 15.55 bn in FY’2017
- Total operating expenses rose by 2.6% to Kshs 12.3 bn from Kshs 12.0 bn in FY’2017, largely driven by a 9.7% increase in staff costs to Kshs 4.1 bn from Kshs 3.7 bn in FY’2017, with the rise being mitigated by an 8.1% decline in Loan Loss Provisions (LLP) to Kshs 3.8 bn from Kshs 4.1 bn in FY’2017
- The balance sheet recorded an expansion as total assets increased by 20.2% to Kshs 288.5 bn, from Kshs 240.1 bn in FY’2017
- The bank’s asset quality deteriorated, with the NPL ratio deteriorating to 13.2% from 12.1% in FY’2017. NPL coverage however improved to 56.5% up from 40.0% in FY’2017, as the 51.8% rise in provisions to Kshs 8.0 bn from Kshs 5.3 bn outpaced the 22.3% growth in gross NPL to Kshs 23.8 bn, from Kshs 19.5 bn in FY’2017.
- Going forward, we expect the bank’s growth to be driven by:
    a) Non-Funded Income growth Initiatives, as the bank continues to focus on digital innovation to augment transaction volumes and increase fee income. The bank needs to increase capacity of its brokerage and advisory businesses so as to increase income contribution from investment and advisory services. The acquisition of Youjays Insurance Brokers provides the bank with an avenue to grow its bancassurance business, thereby putting the firm’s NFI on a positive growth trajectory.

Financial Statement Extracts

I&M Holdings PAT is expected to grow at a 5-year CAGR of 11.5%

Income Statement	2017	2018	2019f	2020f
Net Interest Income	15.6	15.6	17.2	17.9
Non- Funded Income	5.8	7.6	8.8	10.0
Total Operating Income	**9.8**	**8.0**	**8.4**	**7.9**
Loan Loss Provision	4.1	3.8	3.5	4.0
Other Operating Expenses	4.1	4.4	5.5	5.9
Total Operating Expenses	**12.0**	**12.3**	**13.5**	**14.6**
Profit Before Tax	9.9	11.5	13.2	13.8
Profit After Tax	7.3	8.5	9.2	9.7
% PAT Change YoY	**(6.4%)**	**17.1%**	**8.4%**	**5.1%**
EPS	17.6	20.6	22.3	23.4
DPS	3.5	3.9	3.9	3.9
Cost to Income	56.2%	53.0%	51.7%	52.5%
ROaE	16.6%	17.7%	16.9%	16.3%
ROaA	3.0%	3.1%	2.9%	2.8%
Balance Sheet	**2017**	**2018**	**2019f**	**2020f**
Government securities	51.7	52.2	45.6	51.0
Net Loans and Advances	153.0	166.7	187.1	209.5
Other Assets	35.4	69.6	90.2	99.1
Total Assets	**240.1**	**288.5**	**322.8**	**359.7**
Customer Deposits	169.3	213.1	239.8	268.6
Other Liabilities	23.8	24.5	24.5	24.5
Total Liabilities	**193.1**	**237.6**	**264.3**	**293.1**
Shareholders Equity	44.3	47.9	55.5	63.5
Book Value Per Share	107.2	115.8	134.2	153.7
% BVPS Change YoY	**13.6%**	**8.0%**	**15.9%**	**14.6%**

Valuation Summary

I&M Holdings is undervalued with a total potential return of 48.8%

Cost of Equity Assumptions:	19/04/2019
Default Spread Adjusted Risk free rate	13.20%
Beta	0.5
Mature Market Risk Premium	7.6%
Extra Risk Premium	0.5%
Cost of Equity	17.5%

Terminal Assumptions:	
Growth rate	5%
Mature Company Beta	1.00
Terminal Cost of Equity	21.3%
Return on Average Equity 2023	**16.2%**
Terminal Price to Book value per share	**1.2x**
Shareholder Equity - FY23e	97.3
Terminal Value-(Year 2023)	123.8

Valuation Summary:	Implied Price	Weighting	Weighted Value
DDM Integrated	182.5	40%	73.01
Residual income	194.4	35%	68.05
PBV Multiple	102.6	20%	20.52
PE Multiple	121.4	5%	6.07
Target Price			**167.7**
Current Price			**115.0**
Upside/(Downside)			45.8%
Dividend yield			3.0%
Total return			**48.8%**

** Five years average yields on a 10 year Treasury bond*

II. National Bank of Kenya

National Bank's Summary of Performance – FY'2018

- National Bank recorded loss before tax of Kshs 0.1 bn, down from a profit before tax of Kshs 0.8 bn in FY'2017. Profit after tax declined by 98.3% to Kshs 7.0 mn in FY'2018, from Kshs 0.4 bn in FY'2017,
- Non-Funded Income (NFI) declined by 18.0% to Kshs 2.0 bn, from Kshs 2.4 bn in FY'2017, while Net Interest Income declined by 10.4% to Kshs 6.0 bn from Kshs 6.7 bn in FY'2017,
- Cost to Income Ratio (CIR) deteriorated to 94.3%, from 91.4% in FY'2017 owing to the faster decline in total operating income. Without LLP, the cost to income ratio deteriorated by a wider margin to 92.0%, from 83.2% in FY'2017,
- The balance sheet recorded an expansion as total assets increased by 4.5% to Kshs 114.8 bn, from Kshs 109.9 bn in FY'2017, while Total liabilities rose by 5.1% to Kshs 107.9 bn, from Kshs 102.6 bn in FY'2017,
- The bank experienced a deterioration in asset quality, with Gross Non-Performing Loans (NPLs) rising by 13.8% to Kshs 31.5 bn in FY'2018 from Kshs 27.7 bn in FY'2017
- Going forward, we expect the bank to focus on :
    a) **Asset quality improvement:** With the bank's deteriorated asset quality, the bank's focus on recoveries and remediation of troubled entities should significantly aid the bank in improving the quality of its book. Furthermore, the bank's capital position would need to be improved, and improve the bank's lending, and deposit mobilization capacity

Financial Statements Extracts

NBK'S PAT is expected to grow at a 5-year CAGR of 120.0% given the low base

Income Statement	2017	2018	2019e	2020e
Net Interest Income	37.6	41.4	45.9	51.0
Non Funded Income	27.6	25.9	29.0	33.2
Loan Loss Provision	(3.4)	(3.7)	(3.6)	(3.9)
Other Operating Expenses	(34.8)	(35.1)	(38.2)	(42.1)
Total Operating Expenses	**(38.3)**	**(38.8)**	**(41.9)**	**(46.0)**
Profit Before Tax	26.9	28.5	33.0	38.2
Profit After tax	18.9	19.8	23.1	26.7
% PAT Change YoY	**14.0%**	**4.8%**	**16.6%**	**15.6%**
EPS	5.0	5.3	6.1	7.1
DPS	2.0	2.0	2.0	2.0
Cost to Income	58.7%	57.7%	55.9%	54.6%
NIM	8.9%	8.5%	8.7%	8.6%
ROaE	21.6%	22.5%	22.7%	22.4%
ROaA	3.8%	3.8%	3.8%	3.9%

Balance Sheet	2017	2018e	2019e	2020e
Net Loans and Advances	279.1	297.2	334.4	375.6
Government Securities	128.0	130.4	148.6	165.4
Other Assets	117.4	145.7	159.4	177.6
Total Assets	**524.5**	**573.4**	**642.4**	**718.7**
Customer Deposits	373.1	422.8	475.7	532.8
Other Liabilities	58.2	55.7	56.1	56.2
Total Liabilities	**431.3**	**478.4**	**531.8**	**589.0**
Shareholders Equity	93.1	94.1	109.7	128.8
Book value Per share	24.7	24.9	29.1	34.1
% Change in BPS YoY	**13.6%**	**1.0%**	**16.6%**	**17.5%**

Valuation Summary

NBK is undervalued with a potential upside of 10.8%

Cost of Equity Assumptions:	19-Apr-19
Default Spread Adjusted Risk free rate*	13.2%
Beta	1.3
Mature Market Risk Premium	7.6%
Extra Risk Premium	2.5%
Cost of Equity	26.7%

Terminal Assumptions:	
Growth rate	5%
Mature Company Beta	1.00
Terminal Cost of Equity	23%
Return on Average Equity	5.9%
Terminal Price to Book value per share	0.31x
Preference Shares	5.68
Shareholder Equity - FY23e	9.51
Terminal Value-(Year 2022)	2.97

Valuation Summary:	Implied Price	Weighting	Weighted Value
Integrated DDM	(0.98)	40%	-0.4
Residual Income	12.69	35%	4.4
PBV Multiple	2.97	20%	0.6
PE Multiple	2.59	5%	0.1
Target Price			**5.2**
Current Price			**4.7**
Upside/(Downside)			10.8%
Dividend yield			0.0%
Total return			**10.8%**

** Five years average yields on a 10 year Treasury bond*

III. HF Group

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HF Group's Summary of Performance – FY'2018

- HF Group recorded a loss before tax of Kshs 642.7 mn from a profit before tax of Kshs 311.6 mn in FY'2017. HF Group also recorded a loss after tax of Kshs 598.2 mn from a profit after tax of Kshs 126.2 mn in FY'2017,
- Non-Funded Income declined by 2.0% to Kshs 1.32 bn from Kshs 1.35 bn in FY'2017, while Net Interest Income (NII) declined by 23.9% to Kshs 2.3 bn, from Kshs 3.0 bn in FY'2017,
- The Cost to Income Ratio (CIR) deteriorated to 118.0%, from 92.3% in FY'2017. Without LLP, the cost to income ratio also deteriorated to 107.7%, from 78.9% in FY'2017
- The balance sheet recorded a contraction as total assets declined by 10.4% to Kshs 60.5 bn, from Kshs 67.5 bn in FY'2017
- The bank experienced a deterioration in asset quality, with gross non-performing loans (NPLs) rising by 62.4%, to Kshs 13.3 bn in FY'2018, from Kshs 8.2 bn in FY'2017
- Going forward, we expect the bank's growth to be driven by:
    a) NFI growth expansion, supported by increased adoption of alternative channels, with the bank currently focusing on deepening its digital banking proposition having launched their digital banking platform in July 2018, dubbed HF Whizz, and
    b) Continued investment in digital channels to enhance accessibility as well as reduce operating expenses mainly through aligning staff costs to the bank's operational needs

Financial Statements Extracts

HF Group's PAT is expected to grow at a 5-year CAGR of 5.0%

Income Statement	2017	2018	2019f	2020f
Net Interest Income	3.0	2.3	2.4	2.3
Non Funded Income	1.3	1.3	1.3	1.4
Loan Loss Provision	0.6	0.4	0.3	0.5
Other Operating Expenses	3.4	3.9	3.5	3.5
Total Operating Expenses	**4.0**	**4.2**	**3.9**	**4.1**
Profit Before Tax	0.3	(0.6)	(0.1)	(0.3)
Profit After tax	0.1	(0.6)	(0.1)	(0.2)
% PAT Change YoY	**-86.1%**	**-**	**-**	**-**
EPS	0.3	(1.5)	(0.2)	(0.6)
DPS	0.4	-	-	-
Cost to Income	92.3%	118.2%	102.5%	108.8%
NIM	5.2%	4.4%	5.0%	4.7%
ROaE	1.1%	-5.5%	-0.6%	-2.3%
ROaA	0.2%	-0.9%	-0.1%	-0.4%

Balance Sheet	2017	2018	2019f	2020f
Net Loans and Advances	49.6	43.4	43.3	43.4
Government Securities	2.3	3.2	3.3	3.1
Other assets	15.6	13.9	12.2	11.9
Total Assets	**67.5**	**60.5**	**58.8**	**58.5**
Customer Deposits	36.7	34.7	33.2	33.0
Other Liabilities	19.4	15.5	15.5	15.5
Total Liabilities	**56.1**	**50.2**	**48.7**	**48.6**
Shareholders Equity	11.4	10.4	10.1	9.9

Valuation Summary

HF Group is overvalued with a total potential downside of 31.8%

Cost of Equity Assumptions:	18-April-2019
Default Spread Adjusted Risk free rate *	13.2%
Beta	1.1
Country Risk Premium	7.64%
Extra Risk Premium	1.50%
Cost of Equity	23.3%

Terminal Assumptions:	
Growth rate	5.0%
Mature Company Beta	1.00
Terminal Cost of Equity	22.0%
Return on Average Equity	(4.9%)
Terminal Price to Book	0.6x
Shareholder Equity - FY22e	9.1
Terminal Value-(Year 2022)	5.37

Valuation Summary:	Implied Price	Weighting	Weighted Value
DDM Integrated	5.7	40%	2.3
Residual Income	(1.9)	35%	(0.7)
PTBV Multiple	5.5	20%	1.1
PE Multiple	4.3	5%	0.2
Fair Value			**2.9**
Current Price			**4.3**
Upside/(Downside)			(30.8%)
Dividend Yield			0.0%
Total return			**(31.8%)**

** Five years average yields on a 10 year Treasury bond*

Appendix

Feedback Summary

During the preparation of this FY'2018 Banking Sector Report, we shared with the subject companies the operating metrics that were used in the rankings for their confirmation and verification

Below is a summary of the banks we were able to acquire feedback from and those that went unresponsive.

Bank	Operating Metrics Shared	Sent Feedback
Diamond Trust Bank	Yes	Yes
National Bank Kenya	Yes	Yes
KCB Group	Yes	Yes
I&M Holdings	Yes	Yes
NIC Group	Yes	Unresponsive
Standard Chartered Bank Kenya	Yes	Unresponsive
Housing Finance Group	Yes	Unresponsive
Stanbic Holdings	Yes	Unresponsive
Equity Group Holdings	Yes	Unresponsive
Barclays Bank of Kenya	Yes	Unresponsive
Cooperative Bank of Kenya	Yes	Unresponsive

Thank You!

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