Cytonn Q1’2023 Markets Review

Equities

Market Performance:

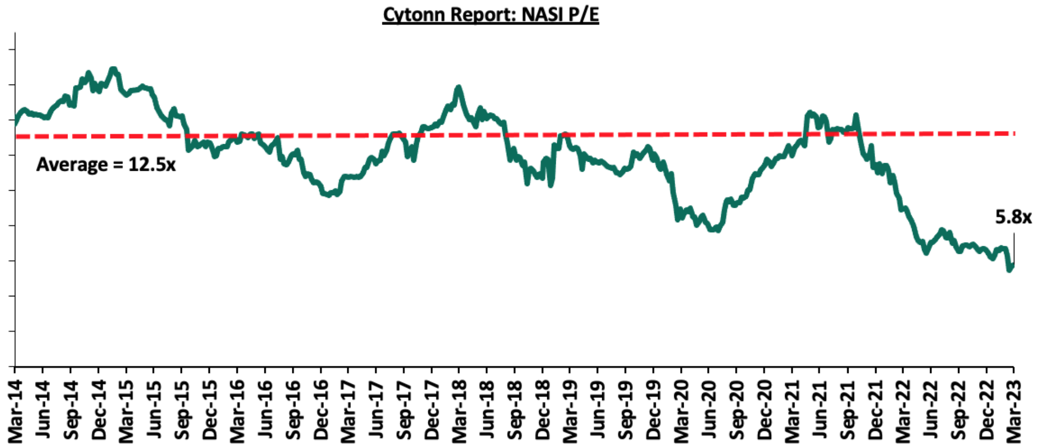
During Q1’2023, the equities market was on a downward trajectory, with NASI, NSE 20 and NSE 25 declining by 11.5%, 3.2% and 5.4%, respectively. The equities market performance during the quarter was driven by losses recorded by large caps such as Safaricom, Bamburi, KCB Group, and NCBA Group of 25.1%, 11.0%, 6.8% and 6.7%, respectively. The losses were however mitigated by gains recorded by banking stocks such as Standard Chartered Bank (SCBK), Co-operative Bank, ABSA Bank and NCBA Group of 19.1%, 6.9%, 4.1% and 2.5%, respectively.

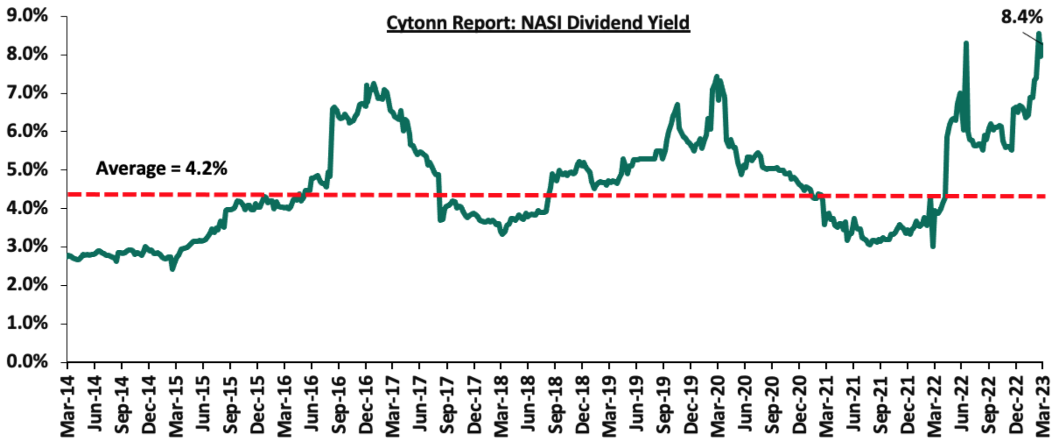
Equities turnover increased by 151.6% during the quarter to USD 348.4 mn, from USD 138.4 mn in Q4’2022. Foreign investors remained net sellers during the quarter, with a net selling position of USD 41.0 mn, from a net selling position of USD 40.1 mn recorded in Q4’2022.

During the week, the equities market was on an upward trajectory, with NASI, NSE 20 and NSE 25 gaining by 1.2%, 3.7% and 4.8%, respectively, taking the YTD performance to losses of 11.4%, 3.2%, and 5.5% for NASI, NSE 20, and NSE 25, respectively. The equities market performance was mainly driven by gains recorded by large cap stocks such as Equity Group, NCBA, BAT Group and ABSA Bank of 17.7%, 12.1%, 9.1% and 7.6%, respectively. The gains were however weighed down by losses recorded by other large stocks such as Safaricom and EABL of 4.2% and 0.4% respectively.

During the week, equities turnover declined by 93.3% to USD 13.3 mn from USD 197.0 mn recorded the previous week taking the YTD turnover to USD 348.4 mn. Foreign investors remained net sellers, recording a net selling position of USD 3.4 mn, from a net selling position of USD 1.6 mn recorded the previous week, taking the YTD net selling position to USD 41.0 mn.

The market is currently trading at a price to earnings ratio (P/E) of 5.8x, 53.6% below the historical average of 12.5x. The dividend yield stands at 8.4%, 4.2% points above the historical average of 4.2%. Key to note, NASI’s PEG ratio currently stands at 0.7x, an indication that the market is undervalued relative to its future growth. A PEG ratio greater than 1.0x indicates the market is overvalued while a PEG ratio less than 1.0x indicates that the market is undervalued. The charts below indicate the historical P/E and dividend yields of the market;





Earnings Releases

During the first quarter of 2023, listed banks in Kenya released their FY'2022 results, recording an increase in their earnings growth, with their average core Earnings per share (EPS) recording a weighted average growth of 26.5%, compared to a weighted average growth of 83.2% in FY'2021. The performance is however largely skewed by the strong EPS growth from HF Group, Diamond Trust Bank of Kenya and NCBA Group of 138.9%, 53.9% and 34.8%, respectively.

I. **Equity Group Holdings Plc FY'2022 performance**

During the week, Equity Group Holdings Plc released their FY'2022 financial results. Below is a summary of the performance:

Balance Sheet Items	FY'2021 (Kshs bn)	FY'2022 (Kshs bn)	y/y change
Government Securities	228.5	219.2	(4.1%)
Net Loans and Advances	587.8	706.6	20.2%
Total Assets	**1,304.9**	**1,447.0**	**10.9%**
Customer Deposits	959.0	1,052.2	9.7%
Deposits per Branch	2.8	3.0	4.4%
Total Liabilities	**1,128.7**	**1,264.8**	**12.1%**
Shareholders' Funds	**169.2**	**176.2**	**4.2%**

Balance Sheet Ratios	FY'2021	FY'2022	% points y/y change
Loan to Deposit Ratio	61.3%	67.2%	5.9%
Gov't Securities to Deposit Ratio	23.8%	20.8%	(3.0%)
Return on average equity	26.6%	26.7%	0.1%
Return on average assets	3.5%	3.4%	(0.1%)

Income Statement	FY'2021 (Kshs bn)	FY'2022 (Kshs bn)	y/y change
Net Interest Income	68.8	86.0	25.0%
Net non-Interest Income	44.6	59.9	34.5%
Total Operating income	**113.4**	**145.9**	**28.7%**
Loan Loss provision	(5.8)	(15.4)	163.7%
Total Operating expenses	(61.5)	(86.1)	40.0%
Profit before tax	51.9	59.8	15.3%
Profit after tax	**40.1**	**46.1**	**15.1%**
Core EPS	**10.6**	**12.2**	**15.1%**

Income Statement Ratios	FY'2021	FY'2022	% points y/y change
Yield from interest-earning assets	9.3%	10.0%	0.7%
Cost of funding	2.7%	2.9%	0.2%
Cost of risk	5.2%	10.6%	5.4%
Net Interest Margin	6.8%	7.2%	0.4%
Net Interest Income as % of operating income	60.7%	58.9%	(1.8%)
Non-Funded Income as a % of operating income	39.3%	41.1%	1.8%
Cost to Income Ratio	54.2%	59.0%	4.8%
Cost to Income Ratio without LLP	49.1%	48.4%	(0.7%)
Cost to Assets	4.8%	5.1%	0.3%

Capital Adequacy Ratios	FY'2021	FY'2022	% Points Change
Core Capital/Total Liabilities	14.2%	16.9%	2.7%
Minimum Statutory ratio	8.0%	8.0%	-
Excess	**6.2%**	**8.9%**	**2.7%**
Core Capital/Total Risk Weighted Assets	12.9%	15.6%	2.7%
Minimum Statutory ratio	10.5%	10.5%	-

Capital Adequacy Ratios	FY'2021	FY'2022	% Points Change
Excess	**2.4%**	**5.1%**	**2.7%**
Total Capital/Total Risk Weighted Assets	17.7%	20.2%	2.5%
Minimum Statutory ratio	14.5%	14.5%	-
Excess	**3.2%**	**5.7%**	**2.5%**
Liquidity Ratio	63.4%	52.1%	(11.3%)
Minimum Statutory ratio	20.0%	20.0%	-
Excess	**43.4%**	**32.1%**	**(11.3%)**
Adjusted core capital/ total deposit liabilities	14.2%	16.9%	2.7%
Adjusted core capital/ total risk weighted assets	12.9%	15.6%	2.7%
Adjusted total capital/ total risk weighted assets	17.7%	20.2%	2.5%

Key Take-Outs:

Earnings Growth- Core earnings per share increased by 15.1% to Kshs 12.2 in FY'2022, from Kshs 10.6 recorded in FY'2021, higher than our projections of a 10.1% increase to Kshs 11.7. The performance was driven by a 28.7% growth in total operating income to Kshs 145.9 bn, from Kshs 113.4 bn in FY'2021 higher than our projections of 25.1%. However, the performance was weighed down by the 40.0% growth in total operating expenses to Kshs 86.1 bn, from Kshs 61.5 bn in FY'2021,

Equity Group's directors recommended a final dividend per share of Kshs 4.0 in FY'2022, representing a dividend yield of 8.8% as at 31st March 2023. The dividends recommended represent a 33.3% increase from dividend per share of Kshs 3.0 paid in FY'2021. Additionally, the dividend payout ratio increased to 33.6% in FY'2022, from 28.9% in FY'2021,

Increased profitability as a result of Group's Geographical diversification- 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 30.0% to the bank's total profitability and 44.0% to the group's total asset base. Cumulatively, the group's subsidiaries, excluding Equity Bank Kenya Ltd, recorded an 61.1% growth in their Profit after Tax (PAT) to Kshs 12.7 bn, from Kshs 7.9 bn in FY'2021, with the Equity Bank South Sudan recording the highest year on year growth of 1381.0% in PAT to Kshs 2.3 bn from a loss of Kshs 0.2 bn in FY'2021, mainly driven by favorable operating business environment following reduction in political instability in the country. However, concerns remain high on the high NPL levels in the group's Tanzanian subsidiary of 18.9% and we expect the group to improve its credit assessment in the country to bring down the high NPL ratio,

Increased Provisioning – The Group increased its Loans Loss Provision (LLPs) by 163.7% to Kshs 15.4 bn in FY'2022, from Kshs 5.8 bn recorded in FY'2021 aimed at mitigating increased credit risk on the back of the elevated inflationary pressures. Additionally, the NPL coverage increased to 70.5%, from 68.7% in FY'2021 as a result of the 13.9% increase in general provisions, coupled with a 39.2% increase in interest in suspense which outpaced the 17.2% growth in Gross non-performing loans. We expect the high provisioning to cushion the Group against high credit risk on the tough operating business environment which has curtailed recovery in some sectors locally and the high NPL ratios in some of the group's subsidiaries,

Improved Lending – FY'2022 was characterized by a 20.2% growth in loans with investments in government securities declining by 4.1%, highlighting the Group's strategy to increase lending despite the tough operating business environment. Notably, the Group diversified risk by extending credit to various sectors in the economy with high lending recorded in sectors such as trade, personal household, and real estate at 23.0%, 22.0% and 14.0%, respectively.

For a comprehensive analysis, please see our Equity Group Holding Plc’s FY’2022 Earnings Note

II. NCBA Group FY’2022 performance

During the week, NCBA Group released their FY’2022 financial results. Below is a summary of NCBA Group FY’2022 performance:

Balance Sheet Items (Kshs bn)	FY’2021	FY’2022	y/y change
Net Loans and Advances	244.0	278.9	14.3%
Government Securities	196.1	205.4	4.8%
Total Assets	**591.1**	**619.7**	**4.8%**
Customer Deposits	469.9	502.7	7.0%
Deposits per Branch	4.5	5.8	29.4%
Total Liabilities	**513.1**	**537.2**	**4.7%**
Shareholders’ Funds	**77.9**	**82.4**	**5.9%**

Balance Sheet Ratios	FY’2021	FY’2022	y/y change
Loan to Deposit Ratio	51.9%	55.5%	3.6%
Gov’t Securities to Deposit Ratio	41.7%	40.9%	(0.8%)
Return on average equity	13.6%	17.2%	3.6%
Return on average assets	1.8%	2.3%	0.4%

Income Statement (Kshs bn)	FY’2021	FY’2022	y/y change
Net Interest Income	27.0	30.7	13.5%
Net non-Interest Income	22.1	30.3	36.8%
Total Operating income	**49.2**	**60.9**	**24.0%**
Loan Loss provision	12.7	13.1	2.7%
Total Operating expenses	**33.4**	**37.9**	**13.4%**
Profit before tax	15.0	22.5	49.6%
Profit after tax	**10.2**	**13.8**	**34.8%**
Core EPS	**6.2**	**8.4**	**34.8%**

Income Statement (Kshs bn)	FY'2021	FY'2022	y/y change
Dividend Per Share	**3.0**	**4.3**	**41.7%**
Dividend payout ratio	**48.3%**	**50.8%**	**2.5%**

Income Statement Ratios	FY'2021	FY'2022	Y/Y Change
Yield from interest-earning assets	9.8%	10.1%	0.3%
Cost of funding	4.2%	4.3%	0.1%
Net Interest Spread	5.6%	5.7%	0.1%
Net Interest Margin	5.7%	5.9%	0.2%
Cost of Risk	25.9%	21.4%	(4.5%)
Net Interest Income as % of operating income	55.0%	50.3%	(4.7%)
Non-Funded Income as a % of operating income	45.0%	49.7%	4.7%
Cost to Income Ratio	68.1%	62.2%	(5.9%)
Cost to Income Ratio without LLP	42.2%	40.8%	(1.4%)

Capital Adequacy Ratios	FY'2021	FY'2022	% points change
Core Capital/Total Liabilities	16.8%	16.3%	(0.5%)
Minimum Statutory ratio	8.0%	8.0%	-
Excess	**8.8%**	**8.3%**	**(0.5%)**
Core Capital/Total Risk Weighted Assets	19.0%	18.4%	(0.6%)
Minimum Statutory ratio	10.5%	10.5%	-
Excess	**8.5%**	**7.9%**	**(0.6%)**
Total Capital/Total Risk Weighted Assets	19.1%	18.4%	(0.7%)
Minimum Statutory ratio	14.5%	14.5%	-
Excess	**4.6%**	**3.9%**	**(0.7%)**
Liquidity Ratio	61.7%	53.2%	(8.5%)
Minimum Statutory ratio	20.0%	20.0%	
Excess	**41.7%**	**33.2%**	**(8.5%)**
Adjusted core capital/ total deposit liabilities	17.5%	16.6%	(0.9%)
Adjusted core capital/ total risk weighted assets	19.8%	18.8%	(1.1%)
Adjusted total capital/ total risk weighted assets	19.9%	18.8%	(1.1%)

Key Take-Outs:

Earnings Growth- Core earnings per share rose by 34.8% to Kshs 8.4 from Kshs 6.2 in FY'2021, slightly higher than our expectations of a 31.8% increase to Kshs 8.2, with the variance stemming from the 24.0% increase in total operating income which was higher than our projection of a 13.5%

increase. The performance was driven by a 24.0% increase in total operating income to Kshs 60.9 bn, from Kshs 49.2 bn in FY'2021, which outpaced the 13.4% increase in the total operating expenses to Kshs 37.9 bn in FY'2022, from Kshs 33.4 bn in FY'2021,

NCBA Group board recommended the payment of a final dividend for the year of Kshs 2.25 per share which added to the interim dividend of Kshs 2.00 per share paid on 30th September 2022, bringing the total dividend for the year 2022 to Kshs 4.25 per share, and a dividend yield of 11.8% as at 31st March 2023. The total dividends for FY'2022 represent a 41.7% increase from the total dividend of Kshs 3.00 per share paid in 2021. Additionally, the dividend payout ratio increased to 50.8%, from 48.3% in FY'2021,

Growth in non-funded income – The total non-funded income grew by 36.8% to Kshs 30.3 bn in FY'2022 from Kshs 22.1 bn in FY'2021, which was higher than the 13.5% increase in net interest income. The growth was mainly driven by a 147.1% increase in foreign exchange income to Kshs 12.5 bn from Kshs 5.1 bn in FY'2021 attributed to increased demand for the dollar amid widening margins. As such, the revenue mix for funded to non-funded income shifted to 50:50 from 55:45, and,

Improvement in Asset Quality – The group's asset quality improved, with the NPL ratio improving by 3.0% points to 13.0% from 16.0% in FY'2021, owing to the 11.7% decline in gross non-performing loans to Kshs 39.1 bn in FY'2022 from Kshs 44.3 bn in FY'2021, while gross loans increased by 9.1% to Kshs 301.8 bn in FY'2022 from 276.7 bn in FY'2021. However, the NPL ratio increase on a q/q from 12.6% recorded in Q3'2022. The y/y decline in gross non-performing loans is an indication of reducing credit risk in the bank loan portfolio.

For a comprehensive analysis, please see our NCBA Group's FY'2022 Earnings Note

III. Diamond Trust Bank Kenya's FY'2022 performance

During the week, Diamond Trust Bank Kenya released their FY'2022 financial results. Below is a summary of the performance:

Balance Sheet Items (Kshs bn)	**FY'2021**	**FY'2022**	**y/y change**
Government Securities	124.3	131.5	5.8%
Net Loans and Advances	220.4	253.7	15.1%
Total Assets	**456.8**	**527.0**	**15.4%**
Customer Deposits	331.5	387.6	16.9%
Deposits per Branch	2.6	3.0	16.0%
Total Liabilities	382.3	449.3	17.5%
Shareholders' Funds	**67.3**	**69.0**	**2.5%**

Balance Sheet Ratios	**FY'2021**	**FY'2022**	**y/y change**
Loan to Deposit Ratio	66.5%	65.5%	(1.0%)
Gov't Securities to Deposit Ratio	37.5%	33.9%	(3.6%)
Return on average equity	6.8%	10.0%	3.2%
Return on average assets	1.0%	1.4%	0.4%

Income Statement (Kshs bn)	FY'2021	FY'2022	y/y change
Net Interest Income	20.0	22.9	14.5%
Non-Interest Income	6.3	9.1	43.5%
Total Operating income	**26.3**	**31.9**	**21.4%**
Loan Loss provision	7.6	7.1	(5.5%)
Total Operating expenses	**19.9**	**22.1**	**11.1%**
Profit before tax	**6.6**	**9.5**	**43.8%**
Profit after tax	**4.4**	**6.8**	**53.9%**
Earnings per share (Kshs)	**15.8**	**24.3**	**53.9%**

Income Statement Ratios	FY'2021	FY'2022	Y/Y Change
Yield from interest-earning assets	8.7%	9.2%	0.5%
Cost of funding	3.9%	4.3%	0.4%
Net Interest Spread	4.8%	5.0%	0.2%
Net Interest Income as % of Total Income	76.0%	71.7%	(4.3%)
Non-Funded Income as a % of Total Income	24.0%	28.3%	4.3%
Cost to Income	75.6%	69.1%	(6.5%)
Cost to Income Ratio without provisions	46.9%	46.8%	(0.1%)
Cost to Assets	4.5%	4.5%	-
Net Interest Margin	5.1%	5.3%	0.2%

Capital Adequacy Ratios	FY'2021	FY'2022	% points change
Core Capital/Total deposit Liabilities	22.0%	21.1%	(0.9%)
Minimum Statutory ratio	8.0%	8.0%	-
Excess	**14.0%**	**13.1%**	**(0.9%)**
Core Capital/Total Risk Weighted Assets	19.9%	19.8%	(0.1%)
Minimum Statutory ratio	10.5%	10.5%	-
Excess	**9.4%**	**9.3%**	**(0.1%)**
Total Capital/Total Risk Weighted Assets	21.2%	20.7%	(0.5%)
Minimum Statutory ratio	14.5%	14.5%	-
Excess	**6.7%**	**6.2%**	**(0.5%)**
Liquidity Ratio	61.6%	58.2%	(3.4%)
Minimum Statutory ratio	20.0%	20.0%	-

Capital Adequacy Ratios	FY'2021	FY'2022	% points change
Excess	**41.6%**	**38.2%**	**(3.4%)**
Adjusted Core Capital/Total Deposit Liabilities	**22.1%**	**21.1%**	**(1.0%)**
Adjusted Core Capital/Total Risk Weighted Assets	**20.0%**	**19.8%**	**(0.2%)**
Adjusted Total Capital/Total Risk Weighted Assets	**21.3%**	**20.7%**	**(0.6%)**

Key Take-Outs:

Earnings Growth - Core earnings per share increased by 53.9% to Kshs 24.3 in FY'2022, from Kshs 15.8 in FY'2021, higher than our projections of 51.3% increase to Kshs 23.9 per share. The performance was driven by a 21.4% increase in total operating income to Kshs 31.9 bn in FY'2022, from Kshs 26.3 bn in FY'2021. However, the growth was weighed down by the 11.1% increase in the total operating expenses to Kshs 22.1 bn in FY'2022, from Kshs 19.9 bn in FY'2021,

DTB-K's directors recommended a first and final dividend per share of Kshs 5.0 in FY'2022, representing a dividend yield of 10.8% as at 31st March 2023. The dividends recommended represents a 66.7% increase from dividend per share of Kshs 3.0 paid in FY'2021. Additionally, the dividend payout ratio increased to 20.6% in FY'2022, from 19.0% in FY'2021, and,

Improved Asset Quality – The group's asset quality improved, with the NPL ratio improving to 12.0% in FY'2022, from 12.9% in FY'2021, owing to the faster 15.3% growth in gross loans, which outpaced the 7.2% increase in gross non-performing loans to Kshs 32.2 bn, from Kshs 30.1 bn in FY'2021. The improvement in asset quality is attributable to proactive credit management strategies leading to increased loan repayment and the declining credit risk in the Kenya's banking sector, with sector's gross NPLs to gross loans ratio improving to 13.3% in Q4'2022 from 13.7% in Q3'2022, and,

For a comprehensive analysis, please see our Diamond Trust Bank Kenya's FY'2022 Earnings Note

IV. **I&M Group FY'2022 performance**

During the week, I&M Group released their FY"2022 financial results. Below is a summary of I&M Group FY'2022 performance:

Balance Sheet Items (Kshs bn)	FY'2021	FY'2022	y/y change
Net Loans and Advances	210.6	238.6	13.3%
Government Securities	125.5	113.1	(9.9%)
Total Assets	**415.2**	**436.6**	**5.2%**
Customer Deposits	296.7	312.3	5.3%
Deposits per Branch	3.3	3.8	12.9%
Total Liabilities	**341.1**	**355.0**	**4.1%**
Shareholders' Funds	**69.6**	**76.5**	**9.9%**

Balance Sheet Ratios	FY'2021	FY'2022	y/y change
Loan to Deposit Ratio	71.0%	76.4%	5.4%
Gov't Securities to Deposit Ratio	29.6%	21.8%	(7.8%)
Return on average equity	12.2%	15.3%	3.1%

Balance Sheet Ratios	FY'2021	FY'2022	y/y change
Return on average assets	2.1%	2.6%	0.5%

Income Statement (Kshs bn)	FY'2021	FY'2022	y/y change
Net Interest Income	20.9	22.9	9.9%
Net non-Interest Income	8.7	12.7	45.7%
Total Operating income	**29.6**	**35.7**	**20.4%**
Loan Loss provision	(4.2)	(5.2)	24.9%
Total Operating expenses	**(17.7)**	**(21.3)**	**20.2%**
Profit before tax	12.4	15.0	20.8%
Profit after tax	**8.6**	**11.6**	**34.3%**
Core EPS	**5.2**	**7.0**	**34.3%**
Dividend Per Share	**1.5**	**2.25**	**9.9%**
Dividend payout ratio	**28.8%**	**32.1%**	**3.4%**

Income Statement Ratios	FY'2021	FY'2022	Y/Y Change
Yield from interest-earning assets	10.0%	10.3%	0.3%
Cost of funding	3.9%	4.2%	0.3%
Cost of risk	14.2%	14.7%	0.5%
Net Interest Margin	6.3%	6.3%	-
Net Interest Income as % of operating income	70.5%	64.3%	(6.2%)
Non-Funded Income as a % of operating income	29.5%	35.7%	6.2%
Cost to Income Ratio	59.9%	59.8%	(0.1%)
CIR without LLP	45.8%	45.1%	(0.6%)
Cost to Assets	3.3%	3.7%	0.4%

Capital Adequacy Ratios	FY'2021	FY'2022	% points change
Core Capital/Total Liabilities	20.9%	22.6%	1.7%
Minimum Statutory ratio	8.0%	8.0%	-
Excess	**12.9%**	**14.6%**	**1.7%**
Core Capital/Total Risk Weighted Assets	16.6%	16.3%	(0.3%)
Minimum Statutory ratio	10.5%	10.5%	-
Excess	**6.1%**	**5.8%**	**(0.3%)**
Total Capital/Total Risk Weighted Assets	21.5%	20.5%	(0.9%)

Capital Adequacy Ratios	FY’2021	FY’2022	% points change
Minimum Statutory ratio	14.5%	14.5%	-
Excess	**7.0%**	**6.0%**	**(0.9%)**
Liquidity Ratio	52.3%	46.1%	(6.1%)
Minimum Statutory ratio	20.0%	20.0%	-
Excess	**32.3%**	**26.1%**	**(6.1%)**
Adjusted core capital/ total deposit liabilities	21.0%	22.6%	1.7%
Adjusted core capital/ total risk weighted assets	16.6%	16.3%	(0.3%)
Adjusted total capital/ total risk weighted assets	21.5%	20.5%	(1.0%)

Key Take-Outs:

Earnings Growth- Core earnings per share rose by 34.3% to Kshs 7.0 from Kshs 5.2 in FY’2021, higher than our expectations of a 10.1% increase to Kshs 5.2, with the variance stemming from the 20.4% increase in total operating income, higher than our projection of a 14.2% increase. The group’s overall performance was mainly driven by the 20.4% increase in total operating income to Kshs 35.7 bn in FY’2022 from Kshs 29.6 bn in FY’2021, which outpaced the 20.2% increase in the total operating expenses to Kshs 21.3 bn in FY’2022 from Kshs 17.7 bn in FY’2021**,**

I&M Group board recommended the payment of a first and final dividend for the year of Kshs 2.25 per share which represents a dividend yield of 10.8% as at 31st March 2023, and dividend payout ratio of 32.1%, an improvement from 28.8% in 2021. The dividends recommended represent a 50.0% increase from the dividend of Kshs 1.5 per share paid in 2021.

Increase in foreign exchange income – The group recorded a 191.0% increase in foreign exchange income to Kshs 5.0 bn from Kshs 1.7 bn in FY’2021. As such, the total non-funded income grew by 45.7% to Kshs 12.7 bn in FY’2022 from Kshs 8.7 bn in FY’2021 which was higher than the 9.9% increase in net interest income, as such, the revenue mix for funded to non-funded income shifted to 64:36 in FY’2022 from 71:29 in FY’2021,

For a comprehensive analysis, please see our I&M Group’s FY’2022 Earnings Note

V. **HF Group Plc FY’2022 performance**

During the week, HF Group Plc released their FY’2022 financial results. Below is a summary of the performance:

Balance Sheet Items	FY'2021	FY'2022	y/y change
Net loans	34.7	36.3	4.6%
Government Securities	6.6	8.5	30.4%
Total Assets	**53.2**	**57.0**	**7.1%**
Customer Deposits	37.7	39.8	5.5%
Deposits Per Branch	1.7	1.8	5.5%
Total Liabilities	44.9	48.2	7.3%
Shareholder's Funds	**8.3**	**8.8**	**6.0%**

Balance Sheet Ratios	FY'2021	FY'2022	y/y change
Loan to deposit ratio	92.0%	91.2%	(0.8%)
Gov't Securities to Deposit Ratio	17.4%	21.5%	4.1%
Return on Average Equity	(8.1%)	3.1%	11.2%
Return on Average Assets	(1.3%)	0.5%	1.8%

Income Statement	FY'2021	FY'2022	y/y change
Net Interest Income	1.8	2.2	18.2%
Net non-Interest Income	0.5	0.9	63.5%
Total Operating income	**2.4**	**3.0**	**28.5%**
Loan Loss provision	(0.3)	(0.2)	(30.8%)
Total Operating expenses	(3.3)	(2.8)	(14.3%)
Profit before tax	(1.0)	0.2	119.7%
Profit after tax	**(0.7)**	**0.3**	**138.9%**
Core EPS	**(1.8)**	**0.7**	**138.9%**

Income Statement Ratios	FY'2021	FY'2022	y/y change
Yield from interest-earning assets	9.0%	9.9%	0.9%
Cost of funding	4.8%	4.9%	0.1%
Net Interest Spread	4.3%	5.0%	0.7%
Net Interest Margin	4.2%	5.0%	0.8%
Cost of Risk	11.9%	6.4%	(5.5%)
Net Interest Income as % of operating income	77.3%	71.1%	(6.2%)
Non-Funded Income as a % of operating income	22.7%	28.9%	6.2%
Cost to Income Ratio	140.1%	93.5%	(46.6%)
Cost to Income Ratio without LLP	128.3%	87.1%	(41.1%)
Cost to Assets	5.7%	4.6%	(1.1%)

Capital Adequacy Ratios	FY'2021	FY'2022	% Change
Core Capital/Total Liabilities	8.3%	8.0%	(0.3%)
Minimum Statutory ratio	8.0%	8.0%	-
Excess	**0.3%**	**0.0%**	**(0.3%)**
Core Capital/Total Risk Weighted Assets	8.3%	8.3%	-
Minimum Statutory ratio	10.5%	10.5%	-

Capital Adequacy Ratios	FY'2021	FY'2022	% Change
Excess	**(2.3%)**	**(2.3%)**	**0.1%**
Total Capital/Total Risk Weighted Assets	12.1%	12.2%	0.1%
Minimum Statutory ratio	14.5%	14.5%	-
Excess	**(2.4%)**	**(2.3%)**	**0.1%**
Liquidity Ratio	22.9%	25.2%	2.3%
Minimum Statutory ratio	20.0%	20.0%	-
Excess	**2.9%**	**5.2%**	**2.3%**
Adjusted core capital/ total deposit liabilities	8.4%	8.1%	(0.3%)
Adjusted core capital/ total risk weighted assets	8.4%	8.4%	0.0%
Adjusted total capital/ total risk weighted assets	12.3%	12.4%	0.1%

Key Take Outs

Earnings Growth- Core earnings per share rose by 138.9% to Kshs 0.7, from a loss of Kshs 1.8 registered in FY’2021. This was higher than our expectations of a 116.6% increase to an EPS of Kshs 0.3, with the variance stemming from the 28.5% growth in total operating income to Kshs 3.0 bn, higher than our expected projection of a 22.7% growth to Kshs 2.9 bn. As such, the core earnings per share performance was driven by the 28.5% growth in total operating income to Kshs 3.0 bn, from Kshs 2.4 bn in FY’2021, coupled with the 14.3% decline in total operating expenses to Kshs 2.8 bn from Kshs 3.3 bn in FY’2021. HF Group’s directors did not recommend a dividend payment for the FY’2022,

Full Year Profits – HF Group made a profit after tax of Kshs 0.3 bn, a 138.9% increase from a loss after tax of Kshs 0.7 bn recorded in FY’2021, ending a four-year loss making performance. The performance of the Group is attributable to efficient operations to minimize costs, evidenced by the total operating expenses declining by 14.3% to Kshs 2.8 bn, from Kshs 3.3 bn in FY’2021,

Improved Asset Quality - The group’s asset quality improved significantly, with the gross NPL ratio improving to 19.7% in FY’2022, from 21.1% in FY’2021, attributable to the 2.1% decline in gross non-performing loans to Kshs 8.5 bn, from Kshs 8.7 bn in FY’2021, coupled with 4.7% growth in Gross loans during the year to Kshs 43.0 from Kshs 41.1 bn in FY’2021. The asset quality improvement was a continuing trend from the Group’s Q3’2022 performance where Gross NPL ratio came in at 20.3%, down from 22.0% in Q3’2021. Notably, on a q/q basis, HF Group’s Asset quality improved by 0.5% points to 19.7%, from 20.3% recorded in Q3’2022,

Sustained Efficiency – Cost to Income Ratio (CIR) improved by 46.6% points to 93.5%, from 140.1% in FY’2021, attributable to the 28.5% increase in total operating income to Kshs 3.0 bn in FY’2022, from Kshs 2.4 bn in FY’2021, coupled with the 14.3% decline in total operating expenses to Kshs 2.8 bn, from Kshs 3.3 bn recorded in FY’2021. Key to note, this is the first full year that HF Group’s total operating expenses have been lower than its total operating income, evidenced by the Cost to Income ratio of below 100.0% in all the four quarters of FY’2022, and,

Cautious Lending – HF Group’s FY’2022 result was characterized by a faster 63.5% growth in government securities as compared to the 18.2% rise in net loans, depicting the group’s adoption of conservative lending strategy to take advantage of the higher interest rates in Fixed Income, coupled with the fact that Real Estate credit risk remains elevated, with the Real Estate Gross Non-performing loans of Kshs 80.3 bn in Q4’2022 contributing to 16.5% of the total banking gross NPLs loans of Kshs 487.7 bn in FY’2022. Key to note, this was a 7.5% increase in Real Estate Gross Non-

Performing Loans from Kshs 74.7 bn in Q4’2021, compared to the total banking sector gross NPL loans of Kshs 426.8 bn in FY’2021.

For a comprehensive analysis, please see our HF Group’s FY’2022 Earnings Note

Asset Quality

The table below is a summary of the listed banks that have released their FY’2022 results:

Cytonn Report: Q1’2023 Listed Banks Asset Quality

	FY'2022 NPL Ratio*	FY'2021 NPL Ratio**	% point change in NPL Ratio	FY'2022 NPL Coverage*	FY'2021 NPL Coverage**	% point change in NPL Coverage
ABSA Bank Kenya	7.5%	7.9%	(0.4%)	80.5%	77.7%	2.8%
Equity Group	8.4%	8.6%	(0.2%)	70.5%	68.7%	1.8%
I&M Holdings	9.7%	9.5%	0.2%	71.9%	71.4%	0.5%
Stanbic Bank	10.0%	9.3%	0.7%	63.1%	58.1%	5.0%
Diamond Trust Bank	12.0%	12.9%	(0.9%)	46.3%	41.8%	4.5%
NCBA Group	13.0%	16.0%	(3.0%)	58.5%	73.6%	(15.1%)
Co-operative Bank of Kenya	14.0%	14.6%	(0.6%)	69.3%	62.6%	6.7%
Standard Chartered Bank Kenya	14.2%	16.0%	(1.8%)	87.1%	84.4%	2.7%
KCB	17.0%	16.6%	0.4%	52.4%	52.9%	(0.5%)
HF Group	19.7%	21.1%	(1.4%)	78.8%	73.6%	5.2%
Mkt Weighted Average	**11.8%**	**12.3%**	**(0.5%)**	**67.8%**	**65.5%**	**2.3%**
*Market cap weighted as at 31/03/2023						
**Market cap weighted as at 14/04/2022						

Key take-outs from the table include;

1. Asset quality for the listed banks improved during the year, with market weighted average NPL ratio declining by 0.5% points to 11.8%, from 12.3% in FY’2021. The improvement was largely driven by an improvement in NCBA Group’s, Standard Chartered Bank Kenya’s and HF Group’s asset quality with their NPL ratios declining by 3.0%, 1.8% and 1.4%% points to 13.0%, 14.2% and 19.7% respectively in FY’2022, from 16.0%, 16.0%, and 21.1% respectively in FY’2021, and,

- **Market weighted average NPL Coverage for the listed banks increased by 2.3% points to 67.8% in FY’2022, from 65.5% recorded in FY’2021, majorly on the back of increased NPL coverage recorded b Co-operative Bank of Kenya, HF Group and Stanbic Holdings of 6.7%, 5.2% and 5.0% respectively. However, NCBA Group’s NPL coverage declined by**

15.1% points to 58.5% in FY’2022 from 73.6% in FY’2021, owing to a decline of 36.1% in General Loan Loss Provisions to Kshs 15.6 bn, from Kshs 24.4 bn in FY’2021, an indication of reducing credit risk in the bank loan portfolio.

Summary performance

The table below highlights the performance listed banks, showing the performance using several metrics:

Cytonn Report: Q1’2023 Listed Banks metrics

Bank	Core EPS Growth	Interest Income Growth	Interest Expense Growth	Net Interest Income Growth	Net Interest Margin	Non-Funded Income Growth	NFI to Total Operating Income	Growth in Total Fees & Commissions	Deposit Growth	Growth in Government Securities	Loan to Deposit Ratio	Loan Growth	Return on Average Equity
HF Group	138.9%	8.8%	0.7%	18.2%	5.0%	63.5%	28.9%	(1.9%)	5.5%	30.4%	91.2%	4.6%	3.1%
DTB-K	53.9%	18.2%	23.5%	14.5%	5.3%	43.5%	28.3%	19.9%	16.9%	5.8%	66.5%	15.1%	10.0%
NCBA	34.8%	12.7%	11.5%	13.5%	5.9%	36.8%	49.7%	5.0%	7.0%	4.8%	55.5%	14.3%	17.2%
I&M	34.3%	12.9%	18.0%	9.9%	6.3%	45.7%	35.7%	20.7%	5.3%	(9.9%)	76.4%	13.3%	15.3%
ABSA	34.2%	27.5%	25.9%	27.9%	8.2%	17.2%	29.7%	0.3%	13.0%	0.7%	93.4%	21.1%	24.3%
SCBK	34.0%	14.3%	6.5%	18.1%	7.0%	13.5%	34.6%	(17.7%)	5.1%	10.6%	50.0%	10.7%	22.1%
CO-OP	33.2%	11.0%	11.0%	10.9%	8.9%	32.7%	36.1%	32.7%	3.9%	(5.9%)	80.1%	9.4%	21.2%
Stanbic	25.7%	31.8%	15.2%	31.8%	5.9%	23.7%	40.9%	(0.5%)	19.5%	42.9%	87.8%	16.4%	15.3%
KCB	19.5%	15.3%	27.1%	11.5%	7.5%	11.5%	33.3%	18.6%	35.6%	2.7%	81.3%	27.8%	22.0%
Equity	15.1%	26.8%	31.7%	25.0%	7.2%	34.5%	41.1%	26.2%	9.7%	(4.1%)	67.2%	20.2%	26.7%
FY'22 Mkt Weighted Average*	**26.5%**	**20.0%**	**21.6%**	**19.1%**	**7.2%**	**26.6%**	**37.5%**	**13.9%**	**14.0%**	**3.0%**	**73.0%**	**18.3%**	**21.9%**
FY'21 Mkt Weighted Average**	**82.9%**	**13.8%**	**11.5%**	**15.2%**	**7.1%**	**10.9%**	**34.7%**	**16.6%**	**13.5%**	**18.1%**	**69.7%**	**13.5%**	**20.2%**
*Market cap weighted as at 31/03/2023													
**Market cap weighted as at 14/04/2022													

Key take-outs from the table include;

1. The listed banks recorded a 26.5% growth in core Earnings per Share (EPS) in FY’2022, compared to the weighted average growth of 82.9% in FY’2021, an indication of sustained performance despite the tough operating environment experienced in FY’2022,
2. The listed Banks’ Interest income grew by 20.0% compared to the market weighted average growth of 13.8% in FY’2021. The growth in interest income is attributable to the 18.3% weighted average growth in the loan book in FY’2022 which was higher than the 13.5% growth in FY’2021. The higher loan book growth took the loan to deposit ratio to 73.0% from the 69.7% market weighted average loan to deposit ratio in FY’2021,
3. Non-Funded Income grew by 26.6% compared to market weighted average growth of 10.9% in FY’2021, pointing to increased revenue diversification efforts by the banking sector, and,

The Banks recorded a deposit growth of 14.0%, higher than the market weighted average deposit growth of 13.5% in FY’2021, highlighting increased investment risk in the business environment.

Q1’2023 Highlights:

1. Centum Investment Plc announced that it had terminated the Share Purchase Agreement (SPA) to sell its 83.4% stake in Sidian Bank Limited to Access Bank Plc. The termination was due to the lapse of time arising from expiry of the Long Stop Date and the two parties could not agree to extend the duration, as well as the set conditions between the two parties having not been met. For more information, please see our Cytonn Weekly #02/2023,
2. The Insurance Regulatory Authority of Kenya (IRA) released the Quarterly Insurance Industry Report for the period ending 30th September 2022 highlighting that the industry’s profits after tax declined by 3.3% to Kshs 6.2 bn in Q3’2022, from Kshs 6.4 bn recorded in Q3’2021. For more information, please see our Cytonn Weekly #03/2023,
3. East African Breweries Plc (EABL) released their H1’2023 financial results for the period ending

31st December 2022, recording a stagnation in the Profits After Tax (PAT) at Kshs 8.7 bn as was recorded in a similar period last year. For more information, please see our Cytonn 2023 Markets Outlook,

4. Equity Group Holdings Plc, through Equity Bank Kenya Limited (EBKL) announced that it had completed the acquisition of certain assets and liabilities of Spire Bank Limited after obtaining all the required regulatory approvals. For more information, please see our Cytonn Monthly January 2023,
5. The Nairobi Stock Exchange (NSE) amended the trading rules for equity securities to allow for block trades, aimed at boosting liquidity in the bourse, after receiving approval from the Capital Markets Authority (CMA). For more information, please see our Cytonn Monthly January 2023,
6. The Central Bank of Kenya (CBK) released the Commercial Banks' Credit Survey Report for the quarter ended December 2022, highlighting that the banking sector's loan book recorded a 15.6% y/y growth, with gross loans increasing to Kshs 3.7 tn in Q4'2022, from Kshs 3.2 tn in Q4'2021. For more information, please see our Cytonn Weekly #06/2023,
7. British American Tobacco Kenya Plc released their FY'2022 financial results, recording a 6.3% growth in Profits after Tax (PAT) to Kshs 6.9 bn, from Kshs 6.5 bn recorded in FY'2021, majorly attributed to the 5.5% increase in Gross Sales to Kshs 42.2 bn in FY'2022 from Kshs 40.0 bn recorded in FY'2021. For more information, please see our Cytonn Weekly #07/2023,
8. The Central Bank of Kenya (CBK) announced that Premier Bank Limited Somalia (PBLS) had completed acquisition of 62.5% shareholding of First Community Bank Limited (FCB) effective 27th March 2023; For more information, please see our Cytonn Weekly #11/2023, and,

Diageo UK, through its wholly-owned indirect subsidiary Diageo Kenya, announced that it had successfully completed the partial tender offer to acquire an additional 15.0% stake in East African Breweries Plc (EABL). For more information, please see our Cytonn Weekly #12/2023.

Universe of coverage:

Company	Price as at 24/03/2023	Price as at 31/03/2023	w/w change	q/q change	YTD Change	Year Open 2023	Target Price*	Dividend Yield	Upside/ Downside**	P/TBv Multiple	Recommendation
Jubilee Holdings	150.0	177.0	18.0%	(10.9%)	(10.9%)	198.8	305.9	7.9%	80.8%	0.3x	Buy
KCB Group***	35.5	35.5	0.0%	(6.8%)	(7.4%)	38.4	52.5	5.6%	53.5%	0.6x	Buy
Britam	4.7	4.7	(0.4%)	(10.6%)	(10.6%)	5.2	7.1	0.0%	53.1%	0.8x	Buy
Sanlam	9.1	8.2	(9.9%)	(14.2%)	(14.2%)	9.6	11.9	0.0%	44.9%	0.9x	Buy
Liberty Holdings	4.8	4.8	1.1%	(14.1%)	(4.6%)	5.0	6.8	0.0%	40.3%	0.4x	Buy
Kenya Reinsurance	1.8	1.9	3.8%	3.3%	1.1%	1.9	2.5	5.3%	38.1%	0.2x	Buy
Equity Group***	38.7	45.5	17.7%	2.2%	1.0%	45.1	58.4	8.8%	37.0%	1.1x	Buy
ABSA Bank***	11.9	12.8	7.6%	4.1%	4.9%	12.2	15.5	10.5%	31.3%	1.1x	Buy
NCBA***	32.8	36.7	12.1%	(6.7%)	(5.8%)	39.0	43.4	11.6%	29.8%	0.8x	Buy
Co-op Bank***	12.6	13.2	4.4%	6.9%	8.7%	12.1	15.5	11.4%	29.0%	0.6x	Buy
CIC Group	2.0	2.0	(0.5%)	0.5%	2.6%	1.9	2.3	6.6%	25.0%	0.7x	Buy
Diamond Trust Bank***	47.8	51.3	7.3%	2.5%	2.8%	49.9	57.1	9.8%	21.2%	0.2x	Buy
Stanbic Holdings	109.0	110.0	0.9%	7.8%	7.8%	102.0	112.0	11.5%	13.3%	1.0x	Accumulate
Standard Chartered***	167.8	170.0	1.3%	19.1%	17.2%	145.0	166.3	12.9%	10.7%	1.2x	Accumulate
I&M Group***	17.1	20.9	22.3%	22.6%	22.3%	17.1	20.8	10.8%	10.6%	0.5x	Accumulate
HF Group	3.4	3.8	11.4%	19.4%	21.0%	3.2	3.4	0.0%	(10.0%)	0.2x	Sell

***Target Price as per Cytonn Analyst estimates**
****Upside/ (Downside) is adjusted for Dividend Yield**
*****For Disclosure, these are stocks in which Cytonn and/or its affiliates are invested in**

We are "Neutral" on the Equities markets in the short term due to the current adverse operating environment and huge foreign investor outflows, and, "Bullish" in the long term due to current cheap valuations and expected global and local economic recovery.

With the market currently trading at a discount to its future growth (PEG Ratio at 0.7x), we believe that investors should reposition towards value stocks with strong earnings growth and that are trading at discounts to their intrinsic value. We expect the current high foreign investors sell-offs to continue weighing down the equities outlook in the short term.

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