Nairobi Metropolitan Area Serviced Apartments Report 2019, & Cytonn Weekly #47/2019

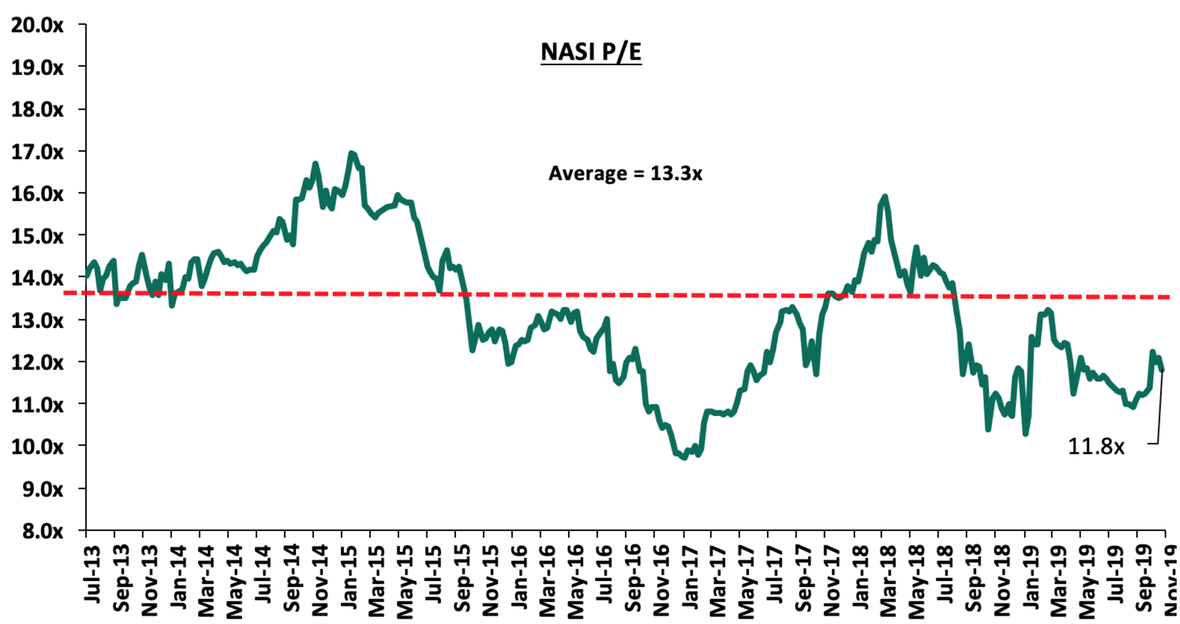
Equities

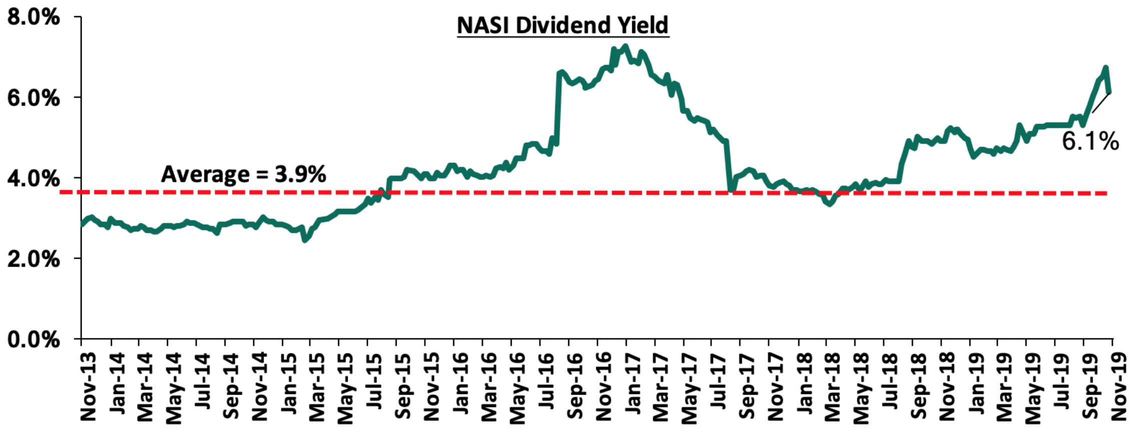
Market Performance

During the week, the equities market was on a downward trend with NASI, NSE 20 and NSE 25 declining by 0.7%, 1.3% and 0.2%, respectively, taking their YTD performance to gains/(losses) of 10.3%, (7.6%), and 8.2%, respectively. The performance in NASI was driven by losses recorded by large-cap stocks with Bamburi, KCB, BAT, and DTBK recording losses during the week of 9.8%, 2.1%, 2.0%, and 1.1%, respectively.

Equities turnover decreased by 81.2% during the week to USD 5.0 mn, from USD 26.4 mn the previous week, taking the YTD turnover to USD 1,331.8 mn. Foreign investors became net sellers for the week, with a net selling position of USD 0.3 mn, a 113.0% decrease from a net buying position of USD 2.3 mn recorded the previous week.

The market is currently trading at a price to earnings ratio (P/E) of 11.8x, 11.2% below the historical average of 13.3x, and a dividend yield of 6.1%, 2.2% points above the historical average of 3.9%. With the market trading at valuations below the historical average, we believe there is value in the market. The current P/E valuation of 11.8x is 21.6% above the most recent trough valuation of 9.7x experienced in the first week of February 2017, and 42.2% above the previous trough valuation of 8.3x experienced in December 2011. The charts below indicate the historical P/E and dividend yields of the market.





Weekly Highlights

Equity Bank Group ('Equity'), in line with its regional expansion strategy, announced during the week that it is set to pay Kshs 107.8 bn to acquire a 66.5% stake in Banque Commerciale du Congo (BCDC), a top bank in the Democratic Republic of Congo owned by the George Arthur Forrest family. Equity is expected to acquire 625,354 shares in a deal that is inclusive of dividends that the bank will declare early next year. Equity is not new to the DRC market as it already acquired 86.0% stake in Pro Credit Bank in 2015. The bank is also seeking to acquire an additional 7.6% from German Development Bank (Kfw), thus, pushing its ownership in Pro Credit Bank to 93.6%. By acquiring an additional subsidiary in DRC and merging the two banks, Equity will create the second largest bank in the country, after Raw Bank, with an asset base of more than Kshs 100.0 bn. The country provides a large customer base having a population of around 80.0 mn people which is attractive to banks looking to grow in the continent. It is our view that the regional acquisitions by Equity will strengthen its footprint in the region. Equity has also signed a binding term sheet with Atlas Mara Ltd to acquire certain banking assets in Rwanda, Zambia, Tanzania and Mozambique. This highlights Kenyan banks' continued pursuit for inorganic growth strategies, and moreover the strategy of Equity to enter markets where there exists a large underserved banking population.

Earnings Releases

Standard Chartered Bank of Kenya Plc released Q3'2019 results:

Standard Chartered Bank released their Q3'2019 results, recording a 1.3% decrease in core earnings per share to Kshs 18.1, from Kshs 18.4 in Q3'2018, attributed to a 0.9% increase in total operating expenses to Kshs 12.5 bn, from Kshs 12.4 bn in Q3'2018, with total operating income remaining flat at Kshs 21.6 bn. Key highlights of the performance from Q3'2018 to Q3'2019 include:

- Core earnings per share declined by 1.3% to Kshs 18.1, from Kshs 18.4 in Q3'2018, which was not in line with our expectation of a 4.0% increase to Kshs 19.1. The performance was driven by a 0.9% increase in total operating expenses to Kshs 12.5 bn from Kshs 12.4 bn, with total operating income remaining flat at Kshs 21.6 bn. The variance in core earnings per share growth was largely due to the 0.9% increase in total operating expenses, which was not in line with our expectations of a 4.5% decline,
- Total operating income remained flat at Kshs 21.6 bn, unchanged from Q3'2018. This was due to a 1.1% decline in Non-Funded Income (NFI) to Kshs 6.96 bn from Kshs 7.04 bn in Q3'2018, which offset the 0.6% increase in Net Interest Income (NII) to Kshs 14.7 bn, from Kshs 14.6 bn in Q3'2018,
- Interest income declined by 6.3% to Kshs 19.1 bn, from Kshs 20.3 bn in Q3'2018. This was driven by a 15.4% decline in interest income on government securities to Kshs 8.1 bn, from Kshs 9.5 bn in Q3'2018. Interest on loans and advances however increased marginally by 1.5% to Kshs 10.1

bn, from Kshs 9.9 bn in Q3'2018. Consequently, the yield on interest-earning assets declined to 9.9%, from 10.6% in Q3'2018,

- Interest expense declined by 23.7% to Kshs 4.4 bn from Kshs 5.8 bn in Q3'2018, following a 42.7% decline in other interest expenses to Kshs 442.2 mn from Kshs 771.5 mn in Q3'2018, coupled with a 20.4% decline in interest expense on customer deposits to Kshs 3.9 bn, from Kshs 4.9 bn in Q3'2018. Consequently, cost of funds declined to 3.0%, from 3.4% in Q3'2018, with the Net Interest Margin (NIM) also declining to 7.5%, from 7.8 in Q3'2018, owing to the faster 5.9% growth in average total interest earning assets that outpaced the 0.6% growth in the trailing net interest income,
- Non-Funded Income (NFI) declined by 1.1% to Kshs 6.96 bn, from Kshs 7.04 bn in Q3'2018. The decline was mainly driven by a 9.3% decline in other fees to Kshs 3.6 bn from Kshs 4.0 bn in Q3'2018. The decline in NFI was however mitigated by a 12.6% growth in foreign exchange trading income to Kshs 2.4 bn from Kshs 2.1 bn and a 7.0% rise in fees and commissions on loans and advances to Kshs 207.4 mn, from Kshs 193.9 mn in Q3'2018. The revenue mix shifted to 68:32 funded to non-funded income, from 67:33 in Q3'2018, largely due to the 1.1% decline in NFI despite net interest income (NII) increasing by 0.6%,
- Total operating expenses increased by 0.9% to Kshs 12.5 bn from Kshs 12.4 bn in Q3'2018, largely driven by a 9.8% increase in staff costs to Kshs 5.6 bn, from Kshs 5.1 bn in Q3'2018, and a 16.8% increase in other operating expenses to Kshs 4.9 bn from Kshs 4.2 bn in Q3'2018. The increases were however mitigated by a 61.2% decline in in loan loss provisions to Kshs 728.2 mn, from Kshs 1.9 bn in Q3'2018. Consequently, the Cost to Income Ratio (CIR) deteriorated to 57.7%, from 57.2% in Q3'2018. Without LLP, the cost to income ratio also deteriorated to 54.4%, from 48.5% in Q3'2018, and,
- Profit before tax declined by 1.2% to Kshs 9.1 bn, from Kshs 9.2 bn in Q3'2018. Profit after tax declined by 1.3% to Kshs 6.2 bn in Q3'2019, from Kshs 6.3 bn in Q3'2018, as the effective tax rate rose marginally to 31.9%, from 31.8% in Q3'2018,
- The balance sheet recorded an expansion as total assets increased by 0.7% to Kshs 290.6 bn, from Kshs 288.6 bn in Q3'2018. The increase was driven by a 6.8% expansion of the loan book to Kshs 118.5 bn from Kshs 111.0 bn in Q3'2018, and a 27.4% increase in cash and balances due from Central Bank of Kenya to Kshs 19.4 bn from Kshs 15.2 bn in Q3'2018. The increases were however mitigated by the 7.9% decline in government securities to Kshs 98.7 bn from Kshs 107.2 bn in Q3'2018,
- Total liabilities increased marginally by 0.3% to Kshs 242.7 bn from Kshs 241.8 bn in Q3'2018, mainly driven by a 2.4% increase in customer deposits to Kshs 224.8 bn from Kshs 219.5 bn in Q3'2018. Deposits per branch increased by 8.4% to Kshs 6.6 bn from Kshs 6.1 bn in Q3'2018, as the number of branches declined by 2 to 34 from 36 in Q3'2018,
- The faster growth in loans which outpaced the growth in deposits led to a rise in the loan to deposit ratio to 52.7%, from 50.6% in Q3'2018,
- Gross Non-Performing Loans (NPLs) increased by 12.0% to Kshs 19.9 bn in Q3'2019, from Kshs 17.8 bn in Q3'2018. The NPL ratio deteriorated to 14.9% in Q3'2019, from 14.2% in Q3'2018, due to the faster growth in gross Non-performing Loans (NPLs), which outpaced the growth in gross loans. General Loan Loss Provisions increased by 10.9% to Kshs 7.9 bn, from Kshs 7.2 bn in Q3'2018. The NPL coverage however deteriorated to 77.0% , from 81.4% in Q3'2018, due to the faster growth in gross Non-performing Loans (NPLs) that outpaced the growth in General Loan Loss Provisions,
- Shareholders' funds increased by 2.4% to Kshs 47.9 bn in Q3'2019, from Kshs 46.8 bn in Q3'2018, supported by a 1.3% increase in retained earnings to Kshs 31.4 bn, from Kshs 31.0 bn in Q3'2018, coupled with an inclusion of Kshs 1.1 bn in Q3'2019 Statutory loan loss reserve, as the CBK provisions were higher than IFRS 9 provisions. As per the CBK guidance on the implementation of IFRS 9, where the CBK provisions are higher than IFRS 9, the excess provisions shall be treated as an appropriation of retained earnings and not expenses in determining profit and loss and thus the excess provision shall be credited to the statutory loan loss reserve,

- Standard Chartered Bank Kenya remains sufficiently capitalized with a core capital to risk-weighted assets ratio of 15.7%, 5.2% points above the statutory requirement of 10.5%. In addition, the total capital to risk-weighted assets ratio came in at 18.9%, exceeding the statutory requirement by 4.4% points. Adjusting for IFRS 9, the core capital to risk weighted assets stood at 15.8%, while total capital to risk-weighted assets came in at 18.9%, and,
- The bank currently has a Return on Average Assets (ROaA) of 2.8%, and a Return on Average Equity (ROaE) of 16.9%.

Key Take-Outs:

1. The bank registered a weak deposit growth, following the 2.4% increase in customer deposits to Kshs 224.8 bn from Kshs 219.5 bn in Q3'2018. The deposit growth rate at 2.4% is lower than the industrial average of 11.7%,
2. The bank registered a decline in operating revenue, following the 1.1% decline in NFI to Kshs 6.96 bn, from Kshs 7.04 bn in Q3'2018. This has bucked the trend of similar Tier I banks that have generally reported an expansion in NFI, with Standard Chartered bank's NFI contribution to total revenue at 32%, lower than the industry average of 37.0%
3. The bank's asset quality deteriorated, with the NPL ratio increasing to 14.9% from 14.2% in Q3'2018. This was due to the faster 12.0% growth in gross Non-performing Loans (NPLs) that outpaced the 6.6% growth in gross loans.

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

1. Continued focus on promoting the usage of the bank's alternative channels is likely to boost the company's Non-Funded Income (NFI) as well as aiding in improving operational efficiency levels, which deteriorated in Q3'2019 as evidenced by the worsening of the cost to income ratio to 57.7% from 57.2% in Q3'2018. Revenue expansion coupled with cost containment will be key in boosting the bank's bottom line.

For more information, see our Standard Chartered Bank Kenya Q3'2019 Earnings Note

Barclays Bank Kenya released Q3' 2019 results:

Barclays Bank released their Q3'2019 results, recording a 19.0% increase in core earnings per share to Kshs 1.2, from Kshs 1.0 in Q3'2018, attributed to a 3.9% increase in total operating income to Kshs 24.8 bn, from Kshs 23.9 bn in Q3'2018. Key highlights of the performance from Q3'2018 to Q3'2019 include:

- Core earnings per share increased by 19.0% to Kshs 1.2 from Kshs 1.0 in Q3'2018, driven by a 3.9% growth in total operating income to Kshs 24.8 bn from Kshs 23.9 bn in Q3'2018. The core earnings per share grew faster than our expectations of 12.7%, with the variance being attributable to the 2.7% decrease in total expenses to Kshs 15.7 bn from Kshs 16.1 bn in Q3'2018, which fell short of our expectations of a 2.0% increase,
- Total operating income increased by 3.9% to Kshs 24.8 bn from Kshs 23.9 bn in Q3'2018. This was due to a 8.1% increase in Non-Funded Income (NFI) to Kshs 8.0 bn, from Kshs 7.4 bn in Q3'2018, coupled with a 2.0% increase in Net Interest Income (NII) to Kshs 16.8 bn from Kshs 16.5 bn in Q3'2018,
- Interest income increased by 5.6% to Kshs 22.9 bn, from Kshs 21.7 bn in Q3'2018. This was driven by a 10.0% increase in interest income from government securities to Kshs 6.1 bn, from Kshs 5.6 bn in Q3'2018, coupled with a 3.0% increase in interest income on loans and advances to Kshs 16.5 bn from Kshs 16.0 bn in Q3'2018. The yield on interest-earning assets however declined to 11.5% from 11.8% in Q3'2018 attributed to the decline in yields on government securities,
- Interest expenses increased by 17.1% to Kshs 6.1 bn, from Kshs 5.2 bn in Q3'2018, following an 41.1% increase in interest expense on deposits and placements from banking institutions to Kshs 0.9 bn from Kshs 0.7 bn in Q3'2018, coupled with a 11.3% rise in interest expense on customer

deposits to Kshs 5.0 bn from Kshs 4.5 bn in Q3’2018. The cost of funds thus increased to 3.4% from 3.1% in Q3’2018. The Net Interest Margin (NIM) declined to 6.4%, from 6.8% in Q3’2018,

- Non-Funded Income (NFI) increased by 8.1% to Kshs 8.0 bn, from Kshs 7.4 bn in Q3’2018. The increase was mainly driven by a 30.9% rise in fees and commissions on loans to Kshs 1.1 bn, from Kshs 0.8 bn in Q3’2018, coupled with a 4.1% and 7.5% increase in other fees and forex trading income to Kshs 3.6 bn and Kshs 2.7 bn from Kshs 3.4 bn and Kshs 2.5 bn, respectively. As a result, the revenue mix shifted to 68:32 from 69:31 funded to non-funded income, due to the faster growth in NFI compared to NII,
- Total operating expenses decreased by 2.7% to Kshs 15.7 bn, from Kshs 16.1 bn, largely driven by a 9.7% decrease in other expenses to Kshs 5.3 bn in Q3’2019, from Kshs 5.9 bn in Q3’2018, coupled with a 1.6% decrease in staff costs to Kshs 7.3 bn in Q3’2019, from Kshs 7.5 bn in Q3’2018,
- Due to the faster growth of operating income that outpaced the decline in total operating expenses, Cost to Income Ratio (CIR) improved to 63.3%, from 67.6% in Q3’2018. Also without LLP, the cost to income ratio improved, to 50.9%, from 55.8% in Q3’2018, and,
- Profit before tax increased by 17.8% to Kshs 9.1 bn, up from Kshs 7.7 bn in Q3’2018. Profit after tax grew by 19.0% to Kshs 6.5 bn in Q3’2019, from Kshs 5.4 bn in Q3’2018 with the effective tax rate remaining unchanged at 32.1%,
- The balance sheet recorded an expansion as total assets increased by 11.7% to Kshs 359.8 bn, from Kshs 322.2 bn in Q3’2018. This growth was largely driven by an 8.8% increase in the loan book to Kshs 194.2 bn from Kshs 178.4 bn in Q3’2018. Investment in government and other securities also recorded a 3.0% growth to Kshs 76.8 bn, from Kshs 74.6 bn in Q3’2018,
- Total liabilities rose by 13.0% to Kshs 315.8 bn, from Kshs 279.5 bn in Q3’2018, driven by a 6.9% increase in deposits to Kshs 235.4 bn, from Kshs 220.2 bn in Q3’2018. Deposits per branch increased by 8.0% to Kshs 2.7 bn from Kshs 2.5 bn in Q3’2018, with the number of branches has reduced to 88 from 89 in Q3’2018,
- The marginal growth in loans as compared to deposits led to a rise in the loan to deposit ratio to 82.5% from 81.0% in Q3’2018,
- Gross Non-Performing Loans (NPLs) decreased by 4.8% to Kshs 13.9 bn in Q3’2019 from Kshs 14.6 bn in Q3’2018. The NPL ratio thus improved to 6.8% from 7.7% in Q3’2018 due to the slower growth in Gross Non-Performing Loans (NPLs) which was slower than the growth in loans. General Loan Loss Provisions increased by 8.8% to Kshs 3.1 bn, from Kshs 2.8 bn in Q3’2018. The NPL coverage, however, increased to 78.6% from 70.5% in Q3’2018 due to the decline in Gross Non-Performing Loans (NPLs) relative to the 11.1% growth in General Loan Loss Provisions to Kshs 8.0 bn from Kshs 7.2 bn recorded in Q3’2018,
- Shareholders’ funds increased by 3.1% to Kshs 44.0 bn in Q3’2019, from Kshs 42.7 bn in Q3’2018, as retained earnings grew by 3.7% y/y to Kshs 5.6 bn, from Kshs 5.4 bn recorded in Q3’2018,
- Barclays Bank Group is currently sufficiently capitalized with a core capital to risk-weighted assets ratio of 14.2%, 3.7% above the statutory requirement. In addition, the total capital to risk-weighted assets ratio was 16.1%, exceeding the statutory requirement by 1.6%. Adjusting for IFRS 9, the core capital to risk-weighted assets stood at 14.7%, while total capital to risk-weighted assets came in at 16.7 %, and,
- The bank currently has a Return on Average Assets (ROaA) of 2.4%, and a Return on Average Equity (ROaE) of 17.4%.

Key Take-Outs:

1. The bank’s asset quality improved, with the NPL ratio decreasing to 6.8% from 7.7% in Q3’2018 due to a 4.8% decrease in Gross Non-Performing Loans (NPLs) to Kshs 13.9 bn from Kshs 14.6 bn which was slower than the growth in loans,
2. Barclays Bank benefited from the restructuring exercise it conducted in 2017, as it continues to record a decline in staff costs y/y, which reduced by 1.6% y/y, and, NFI supported the

improvement in the top-line revenue, as it expanded by 8.1% y/y, largely supported by other fees and commissions, as well as the forex trading income segments, which recorded growths of 4.1% and 7.5%, respectively. Recovery in the fees and commissions on loans is presumably due to the low base of 2018, on the initial implementation of the Effective Interest Model (EIR) under IFRS 9, which required banks to amortize fees and commissions on loans over the tenor of the loan. As a result of the performance, the revenue mix shifted to 68:32 from 69:31 funded to non-funded income, due to the faster growth in NFI compared to NII and,

3. There was an improvement in operational efficiency as evidenced by the decline in the Cost to Income Ratio (CIR) without LLP to 50.9% in Q3'2019, from 55.8% in Q3'2018.

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

1. **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 accelerated growth, and consequently higher Non-Interest Revenue. This, coupled with the expansion of its agent banking network and product offerings such as bancassurance and fixed income trading will see the bank expand its top-line revenue, going forward.

For more information, see our Barclays Bank Kenya Q3'2019 Earnings Note

NIC Group released Q3' 2019 results:

NIC Group released their Q3'2019 results, recording a 3.3% decrease in core earnings per share to Kshs 4.4, from Kshs 4.6 in Q3'2018, attributed to a 22.9% increase in total operating expenses to Kshs 8.2 bn, from Kshs 6.6 bn in Q3'2018, which was slightly mitigated by increase in total operating income by 15.2% to Kshs 12.6 bn, from Kshs 11.0 bn in Q3'2018. Key highlights of the performance from Q3'2018 to Q3'2019 include:

- Core earnings per share declined by 3.3% to Kshs 4.4 from Kshs 4.6 in Q3'2018. The performance was driven by a 22.9% increase in total operating expenses to Kshs 8.2 bn from Kshs 6.6 bn in Q3'2018, this was mitigated by the 15.2% increase in total operating income,
- Total operating income increased by 15.2% to Kshs 12.6 bn from Kshs 11.0 bn in Q3'2018. This was driven by both, a 10.6% increase in Net Interest Income (NII) to Kshs 8.4 bn from Kshs 7.6 bn in Q3'2018, and a 25.6% increase in Non-Funded Income (NFI) to Kshs 4.3 bn from Kshs 3.4 bn in Q3'2018,
- Interest income increased by 3.4% to Kshs 14.7 bn from Kshs 14.2 bn in Q3'2018. Interest income on government securities increased by 5.1% to Kshs 5.3 bn in Q3'2019 from Kshs 5.0 bn in Q3'2018, while that on loans and advances increased by 1.8% to Kshs 9.2 bn from Kshs 9.1 bn in Q3'2018. The yield on interest-earning assets, however, declined to 7.9% in Q3'2019 from 8.3% in Q3'2018,
- Interest expense decreased by 4.7% to Kshs 6.4 bn from Kshs 6.7 bn in Q3'2018, as interest expense on customer deposits decreased by 4.9% to Kshs 5.3 bn from Kshs 5.5 bn in Q3'2018. The cost of funds fell to 3.4% from 3.9% in Q3'2018, while the Net interest margin increased to 6.1% from 6.0% in Q3'2018,
- Non-Funded Income increased by 25.6% to Kshs 4.3 bn from Kshs 3.4 bn in Q3'2018. The increase in NFI was mainly driven by a 91.4% increase in Other Income to Kshs 1.1 bn from Kshs 0.6 bn in Q3'2018, coupled with a 19.4% increase in Fees & commissions on loans and advances to Kshs 1.3 bn from Kshs 1.1 bn in Q3'2018. Forex trading came in at Kshs 1.1 bn, compared to Kshs 1.0 bn in Q3'2018. The revenue mix shifted to 66:34 funded to non-funded income in Q3'2019 from 69:31 in Q3'2018, owing to the higher increase in NFI,
- Total operating expenses increased by 22.9% to Kshs 8.2 bn from Kshs 6.6 bn, largely driven by a 44.4% increase in loan loss provision (LLP) to Kshs 2.3 bn in Q3'2019 from Kshs 1.6 bn in Q3'2018. Staff costs, also increased by 10.8% to Kshs 2.9 bn in Q3'2019 from Kshs 2.6 bn in Q3'2018,

- The cost to income ratio deteriorated to 64.6% from 60.6% in Q3’2018. Without LLP, the cost to income ratio also deteriorated to 46.3% from 46.0% in Q3’2018,
- NIC Group incurred an exceptional item of Kshs 344.2 mn following the integration, advisory and legal expenses related to the merger with CBA,
- Profit before tax decreased by 4.5% to Kshs 4.1 bn from Kshs 4.3 bn in Q3’2018. Profit after tax decreased by 3.3% to Kshs 3.1 bn in Q3’2019 from Kshs 3.2 bn in Q3’2018, with the difference being a decline in the effective tax rate to 35.9% from 42.9% in Q3’2018,
- The balance sheet recorded an expansion with total assets growth of 7.0% to Kshs 215.9 bn from Kshs 201.8 bn in Q3’2018. This growth was largely driven by a 9.4% increase in government securities to Kshs. 65.8 bn from Kshs. 60.2 bn in Q3’2018,
- The loan book expanded by 4.3% to Kshs 119.9 bn in Q3’2019 from Kshs 114.9 bn in Q3’2018,
- Total liabilities rose by 5.6% to Kshs 177.4 bn from Kshs 167.9 bn in Q3’2018, driven by a 9.2% increase in customer deposits to Kshs 158.2 bn from Kshs 145.0 bn in Q3’2018. This was however mitigated by a 46.8% decline in borrowings to Kshs 8.4 bn from Kshs 15.8 bn in Q3’2018. Deposits per branch stood at Kshs. 3.8 bn with the bank operating 42 branches,
- The faster growth in deposits compared to the growth in loans led to a slight decline in the loan to deposit ratio to 75.8% from 79.3% in Q3’2018,
- Gross non-performing loans increased by 13.8% to Kshs 18.7 bn in Q3’2019 from Kshs 16.4 bn in Q3’2018. Consequently, the NPL ratio deteriorated to 14.6% in Q3’2019 from 13.3% in Q3’2018. General Loan loss provisions decreased by 19.2% to Kshs 5.3 bn from Kshs 6.6 bn in Q3’2018. Consequently, the NPL coverage deteriorated to 45.9% in Q3’2019 from 51.4% in Q3’2018,
- Shareholders’ funds increased by 14.4% to Kshs 38.3 bn in Q3’2019 from Kshs 33.5 bn in Q3’2018,
- NIC Group is currently sufficiently capitalized with a core capital to risk-weighted assets ratio of 19.6%, 9.1% above the statutory requirement. In addition, the total capital to risk-weighted assets ratio was 20.3%, exceeding the statutory requirement by 5.8%. Adjusting for IFRS 9, the core capital to risk-weighted assets stood at 20.4%, while total capital to risk-weighted assets came in at 21.9%, and,
- NIC Group currently has a return on average assets of 1.0% and a return on average equity of 5.4%.

Key Take-Outs:

1. NIC Group’s operating income increased by 15.2% to Kshs 12.6 bn, from Kshs 11.0 bn in Q3’2018, mainly supported by the 25.6% increase in non-funded income for the period ending 30th September 2019. This shows improved diversification with the bank improving its alternative sources of income.

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

1. The merger with CBA will likely enable NIC to mobilize cheaper funding, leveraging on the scale and market reach of the combined entity as well as the digital channels. We expect NCBA Group Plc to focus on branding and increased consumer awareness campaigns in the near term, as they endeavor to minimize service disruptions to clientele as well as highlight the synergies and benefits expected to be reaped from the merger.

For more information, see our NIC Group Q3’2019 Earnings Note

The table below summarizes the performance of listed banks that have released their Q3’2019 results:

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

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
Equity Group	10.4%	11.2%	16.8%	9.5%	8.4%	13.7%	41.1%	15.0%	18.9%	7.8%	73.0%	21.0%	22.8%
KCB Group	6.2%	4.6%	(0.8%)	6.5%	8.2%	16.9%	35.2%	28.5%	11.4%	7.5%	82.9%	11.7%	22.2%
Co-operative Bank	5.5%	(1.6%)	0.9%	(2.7%)	8.3%	33.3%	40.0%	46.6%	8.9%	13.6%	83.4%	5.8%	18.4%
NBK	(4.7%)	4.7%	(8.2%)	11.6%	7.2%	(4.6%)	23.8%	4.5%	(11.1%)	(17.1%)	58.0%	(0.3%)	5.5%
BBK	19.0%	5.6%	17.1%	2.0%	6.4%	8.1%	32.1%	30.9%	6.9%	3.0%	81.0%	8.8%	17.4%
SCBK	(1.3%)	(6.3%)	(23.7%)	0.6%	7.5%	(1.1%)	32.2%	7.0%	2.4%	(7.9%)	52.7%	6.8%	16.9%
NIC Group	(3.3%)	3.4%	(4.7%)	10.6%	6.1%	25.6%	34.0%	19.4%	9.2%	9.4%	75.8%	4.3%	5.4%
Q3'2019 Mkt Weighted Average*	**7.5%**	**4.5%**	**4.1%**	**5.1%**	**7.9%**	**15.6%**	**37.0%**	**24.3%**	**11.7%**	**6.2%**	**75.8%**	**12.5%**	**19.9%**
Q3'2018 Mkt Weighted Average**	**16.2%**	**6.1%**	**12.5%**	**3.8%**	**8.0%**	**5.9%**	**34.5%**	**0.6%**	**7.4%**	**17.8%**	**75.3%**	**4.2%**	**18.8%**

***Market cap weighted as at 22/11/2019**

****Market cap weighted as at 30/11/2018**

Key takeaways from the table above include:

i. The seven listed Kenyan banks that have released their results recorded a 7.5% average increase in core Earnings per Share (EPS), compared to an increase of 16.2% in Q3’2018 for all listed banks. Consequently, the Return on Average Equity (ROaE) increased to 19.9%, from 18.8% in Q3’2018,
ii. The banks recorded stronger deposit growth, which came in at 11.7%, faster than the 7.4% growth recorded in the sector in Q3’2018. Interest expenses increased at a slower pace of 4.1%, compared to 12.5% in Q3’2018, indicating the banks have been able to mobilize relatively cheaper deposits,
iii. Average loan growth came in at 12.5%, which was faster than the 4.2% recorded in the sector in Q3’2018, indicating that there was an improvement in credit extension by the banks. Government securities recorded a growth of 6.2% y/y, which was slower compared to the loans, and a decline from the 17.8% recorded in the sector in Q3’2018. This highlights that banks are beginning to adjust their business models back to private sector lending as opposed to investing in government securities, as the yields on government securities declined during the year. Interest income increased by 4.5%, lower than the 6.1% growth recorded in the sector in Q3’2018. Consequently, the Net Interest Income (NII) grew by 5.1% compared to a growth of 3.8% in the sector in Q3’2018,
iv. The banks recorded a Net Interest Margin of 7.9%, 10 bps lower than 8.0% the sector recorded in Q3’2018 and,
v. Non-Funded Income grew by 15.6% y/y, faster than the 5.9% recorded in the sector in Q3’2018. The growth in NFI was boosted by the total fee and commission income which improved by 24.3%, compared to the 0.6% growth recorded in the sector Q3’2018, owing to the faster loan growth.

Universe of Coverage

Below is a summary of our universe of coverage:

(All values in Kshs unless stated otherwise)

Banks	Price at 15/11/2019	Price at 22/11/2019	w/w change	YTD Change	Target Price*	Dividend Yield	Upside/ Downside**	P/TBv Multiple	Recommendation
Sanlam	17.0	16.5	(2.9%)	(14.8%)	29.0	0.0%	75.8%	**0.7x**	**Buy**
I&M Holdings* **	49.1	50.0	1.9%	5.9%	79.8	7.8%	67.3%	**0.8x**	**Buy**
NCBA	34.0	34.5	1.5%	7.7%	37.9	55.2%	65.2%	**0.8x**	**Buy**

Banks	Price at 15/11/2019	Price at 22/11/2019	w/w change	YTD Change	Target Price*	Dividend Yield	Upside/ Downside**	P/TBv Multiple	Recommendation
Diamond Trust Bank	115.3	114.3	(0.9%)	(27.2%)	175.6	2.3%	56.0%	**0.6x**	**Buy**
Kenya Reinsurance	3.1	3.1	(1.6%)	(17.2%)	3.8	14.7%	36.8%	**0.3x**	**Buy**
KCB Group* **	50.3	49.1	(2.4%)	12.1%	61.4	7.1%	32.2%	**1.3x**	**Buy**
CIC Group	3.2	3.1	(1.3%)	(20.5%)	3.8	4.2%	26.0%	**1.1x**	**Buy**
Liberty Holdings	10.5	9.6	(8.6%)	(24.7%)	11.3	5.2%	22.9%	**0.6x**	**Buy**
Barclays Bank* **	11.9	12.0	1.3%	0.0%	12.6	16.7%	21.5%	**0.5x**	**Buy**
Jubilee holdings	350.0	355.0	1.4%	(13.5%)	418.5	2.5%	20.4%	**0.9x**	**Buy**
Britam	7.5	7.7	2.1%	(30.2%)	8.8	0.0%	14.9%	**0.7x**	**Accumulate**
Equity Group* **	47.5	48.7	2.5%	7.5%	53.0	3.1%	12.0%	**1.0x**	**Accumulate**
Co-op Bank* **	15.0	15.0	(0.3%)	(16.8%)	15.0	6.7%	7.0%	**1.3x**	**Hold**
Standard Chartered	200.0	198.0	(1.0%)	2.7%	208.0	0.6%	5.6%	**1.5x**	**Hold**
Stanbic Holdings	109.5	109.3	(0.2%)	5.8%	100.5	4.4%	(3.6%)	**1.2x**	**Sell**
HF Group	6.7	6.4	(3.9%)	27.1%	2.8	0.0%	(56.8%)	**0.3x**	**Sell**

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

We are "Positive" on equities for investors as the sustained price declines has seen the market P/E decline to below its historical average. We expect increased market activity, and possibly increased inflows from foreign investors, as they take advantage of the attractive valuations, to support the positive performance.