Q3 2020 Kenya Banks Earnings Update – KCB Group

- KCB Group has reported a 43.2% decline in **Profit After Tax** (PAT) to KES.10.9Bn in Q3 2020 attributed to a 243% increase in loan loss provisions as a result of heightened credit risk in private sector lending due to COVID-19 pandemic.
- During the period NBK's PAT dipped 76.7% to KES.87.9Mn from KES.376.5Mn in Q3 2019.
- **Asset book** grew 27.2% to KES.972.0Bn driven by business growth and consolidation with NBK.
- **Loan book** up 18.7% to KES.577.5Bn as the lender restructured KES.105Bn in response to corona virus pandemic. Total mobile loans advanced during the period declined 26.2% to KES.117.7Bn with KCB-M-pesa, Fuliza and KCB Mobi disbursing KES.49.7Bn, KES.53.3Bn and KES.14.7Bn respectively.
- Investment in **Government securities** grew 83.8% to KES.236.2Bn compared to KES.128.5Bn same period in 2019.
- **Customer deposits** rose 31.7% to KES.772.7Bn with demand, term, call and savings representing 68%, 21%, 6% and 5% respectively.
- **Total operating income** up 15.9% to KES.69.1Bn as a result of 23.8% growth in net interest income (KES.47.9Bn) and 1.4% increase in non-funded income (NFI).
- **Total interest income** increased 23.2% to KES.63.3Bn driven by 65.7% and 12.9% growth in interest from government securities (KES.16.8Bn) and loans and advances (KES.45.8Bn) respectively.
- **Interest expense** went up 20.3% to KES.15.4Bn owing to a 23.6% increase in customer deposits interest expense to KES.14Bn.
- **NFI** increased marginally 1.4% to KES.21.3Bn attributable to 20.8% growth in other fees and commissions (KES.7.5Bn) which outweighed a 14.2% decline in fees and commissions on loans and advances (KES.6.8Bn).
- **Total Operating expenses** rose 60.1% to KES.52Bn majorly due to 242.5% and 12.8% increase in loan loss provisions (KES.20Bn) and staff costs (KES.15.2Bn) respectively.
- **Asset Quality - Gross Non-Performing Loans** (NPLs) increased 127.7% to KES.97Bn from KES.42.6Bn due to increased customer defaults as a result of COVID-19 pandemic.
- The bank's NPL ratio deteriorated to 15.2% from 8.3% in Q3 20219 mainly due to consolidation of NBK and COVID-19 related downgrades.
- **Cost to Income Ratio** (CIR) deteriorated to 46.3% from 44.7% same period in 2019 owing to an increase in operating expenses and majorly loan loss provisions.

FY2020 Outlook

- The economic slowdown due to COVID-19 pandemic has had a negative impact on KCB's performance and this is expected in FY2020 results.
- Due to these shocks, the Group has increased their holdings in Government securities which are deemed to be safer especially in this period.
- Despite the heightened risk in the private sector, the lender seems to have done well with a double digit growth in loan book unlike its peers whose loan books are growing modestly.
- The waiver on fees for funds transfer from bank to/from mobile wallets and account balance enquiry has resulted in a marginal growth in NFI and this is likely to continue until the fees are re-instated.
- The bank's asset quality is expected to deteriorate further which means an increase in loan loss provisions and thus total operating expenses which will erode the bank's profitability.
- Despite the decline in NBK's profitability, we are positive on the bank's performance in the medium to long term due to improved management, strategic focus on reduction of NPLs and capital base injected into the bank by KCB to shore up its liquidity and fund its growth.
- At KES.37.90, KCB share price is highly discounted compared to fundamental valuations before the coronavirus pandemic started, presenting an opportunity for positive returns to investors.
- We maintain a **BUY** recommendation on the stock guided by our fair value estimate of KES.47.80, a 26.1% upside from the current price of KES.37.90 (11th November, 2020).