Equity Group receives approval on risk-based loan pricing model

- Equity Group has today 7th March 2022 announced in its Africa recovery and resilience plan that the Central Bank of Kenya (CBK) has approved its risk based loan pricing model after 2 years of discussions.
- The model takes into account the Group's base rate, cost of funds, Return on Assets (ROA), Operating Expenses (OPEX) and adds a risk premium to the same.
- The Group's rates will include all negotiation and appraisal fees on an annualized basis and as such, the Group will offer loans in the range of **13% - 18.5%.**
- The Group's yields on loans stood at 11.8% (as at Q3'2021) and this news will result in an increase in the above and subsequently Net interest margins (NIMs) going forward.
- We estimate Equity's yields on loans at 11.8% - 12% for FY2021 and +12% FY2022 due to the impact of risk based loan pricing.

Effect on the banking sector

- As was stated in both our Q3 banking report, "Banks up and onwards" and our 2022 macro-economic report, "Will politics overshadow economics?" we expected loan pricing formula approval to begin as early as Q1'22.
- Equity Group is among the first tier 1 banks to confirm approval with many more likely to follow in the first half of the year.
- The news signals a rise in domestic debt interest rates with the Government now having to compete with the private sector for bank capital.
- We expect private sector credit (PSC) growth to improve going forward, with a high likelihood of it exceeding the double digit range in the cause of the year as businesses have greater access to credit.
- Banks are likely to increase lending significantly which on the back of higher interest rates being charged will translate into higher interest income.
- We rate the possibility of the resumption of banking charges that were suspended in the wake of the Covid-19 pandemic as moderate a scenario that would bolster Non-Funded Income (NFI).
- These two pieces of news combined means higher earnings for banks going forward which we expect to act as a catalyst that will return activity into the NSE as investors' price this news into share prices.

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