



Co-operative Bank IH20 Earnings Note

Co-operative Bank's IH20 net earnings declined 3.6% y/y to KES 7.2B driven by a 57.9% y/y surge in loan loss provisions, a 5.6% decrease in non-funded income and a 11.3% rise in operating expenses. The bottom line was however buoyed by a 19.1% decline in tax paid.

Single digit growth in loans and advances

In line with our expectations of a 5.0% uptick, the loan book grew 5.7% y/y to KES 272.2B premised on slow economic activity due to the prevailing pandemic. Increased liquidity saw banks curl towards government paper; this saw the Group's investment in government securities rise 26.2% y/y to KES 122.4B. In effect interest income rose 6.8% y/y to KES 21.8B.

Cost of funds decline despite growth in customer deposits

Interest expenses dropped 4.4% y/y to KES 5.9B behind a 18.9% y/y incline in customer deposits to KES 384.6B. This was boosted by a 50bps y/y decrease in cost of funds to 3.3%.

Loan loss provisions below target

In line with our expectations, NPLs grew 12.3% y/y to KES 34.3B with an NPL ratio of 12.0% below our expectation of a ratio of 12.5%. Loan loss provisions grew 57.9% y/y to KES 1.9B with a cost of risk of 1.4% below our expectation of a cost of risk of 1.8%. We anticipate a continued worsening of the asset book due to a general slowdown in business activity with a total shutdown in some sectors such as tourism and hospitality. However, the bank's diverse loan book is expected to assist weather the tough business environment.

Outlook

The Group's IH20 performance was largely in line with our expectations; we remain worried on the surge in NPLs that is expected to see provisions eat into the bottom line going forward.

We maintain a BUY recommendation on Co-operative Bank with a target price of KES 16.82 offering a potential upside of 57.9% on the current price of KES 10.65. The counter is trading at p/e and p/b multiples of 8.7x and 0.8x respectively.

DATE: 13th Aug 2020

Fair Value: KES 16.82

Current Price: KES 10.65

Upside: 57.9%

52 Week High: KES 10.05

52 Week Low: KES 17.00

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Financial Statements

	IH19	IQ20	2Q20	IH20	AIB-AXYS estimates	chg y/y	% chg q/q	Deviation
Income Statement	KES M	KES M	KES M	KES M	KES M			
Interest Income	20,425	10,540	11,272	21,811	23,279	6.8%	6.9%	-6.3%
Interest Expense	6,172	3,021	2,876	5,897	6,681	-4.4%	-4.8%	-11.7%
Net Interest Income	14,254	7,519	8,395	15,914	16,599	11.6%	11.7%	-4.1%
Non Interest Income	8,752	4,984	3,324	8,307	9,617	-5.1%	-33.3%	-13.6%
Total Operating Income	23,005	12,502	11,719	24,221	26,216	5.3%	-6.3%	-7.6%
Total Operating Expenses	11,414	6,363	6,340	12,703	13,829	11.3%	-0.4%	-8.1%
Loan Loss Provision Expense	1,181	900	965	1,865	2,386	57.9%	7.2%	-21.8%
Operating Profit	11,591	6,139	5,379	11,518	12,387	-0.6%	-12.4%	-7.0%
Profit Before Tax	10,437	5,118	4,482	9,599	10,087	-8.0%	-12.4%	-4.8%
Current Tax	2,967	1,529	872	2,401	2,522	-19.1%	-42.9%	-4.8%
Profit After Tax	7,469	3,589	3,609	7,198	7,565	-3.6%	0.6%	-4.9%
EPS (KES)	1.27	0.61	0.62	1.23	1.29	-3.1%	1.6%	-4.6%

Balance Sheet								
Total Shareholders' Equity	71,006	82,011	80,116	80,116	84,434	12.8%	-2.3%	-5.1%
Customer Deposits	323,600	339,567	384,637	384,637	346,137	18.9%	13.3%	11.1%
Total Liabilities	357,198	386,865	432,245	432,245	392,789	21.0%	11.7%	10.0%
Total Equity and Liabilities	429,591	470,410	513,924	513,924	477,803	19.6%	9.3%	7.6%
Government and Other Securities	96,995	115,873	122,368	122,368	128,842	26.2%	5.6%	-5.0%
Net Loans and Advances	257,564	276,173	272,157	272,157	272,714	5.7%	-1.5%	-0.2%
Fixed Assets	5,407	9,420	9,076	9,076	12,107	67.9%	-3.6%	-25.0%
Total Assets	429,591	470,410	513,924	513,924	477,803	19.6%	9.3%	7.6%

Key Ratios								
Gross NPL (KES M)	30,556	31,825	34,301	34,301	34,089	12.3%	7.8%	0.6%
NPL Ratio	11.4%	11.0%	12.0%	12.0%	12.5%			
Cost of Risk	0.9%	1.3%	1.4%	1.4%	1.8%			
Loan to Deposits	79.6%	81.3%	70.8%	70.8%	78.8%			
Yield on Interest Earning Assets	11.0%	10.8%	11.4%	11.1%	11.3%			
Cost of Funds	3.8%	3.6%	3.0%	3.1%	3.3%			
NIM	7.2%	7.2%	8.4%	8.0%	8.0%			
Non Funded/Total Income	38.0%	39.9%	28.4%	34.3%	36.7%			
Cost to Income Ratio	49.6%	50.9%	54.1%	52.4%	52.8%			
ROE	21.0%	17.5%	18.0%	18.0%	17.9%			
ROA	3.5%	3.1%	2.8%	2.8%	3.2%			
Core Capital/TRWA	16.0%	15.6%	16.3%	16.3%				
Total Capital/TRWA	16.3%	16.1%	16.8%	16.8%				
Liquidity Ratio	44.6%	49.0%	54.1%	54.1%				
P/B (x)				0.8	1.3			
P/E (x)				8.7	6.5			

Source: AIB-AXYS Research, company filings

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Investment ratings

- **BUY:** Issued on counters with strong fundamentals whose upside lies between 10.0% and 20.0%.
- **HOLD:** Issued on counters with an upside of between 1% and 10.0%
- **SELL:** The counter currently has weak fundamentals coupled with potential downside.

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