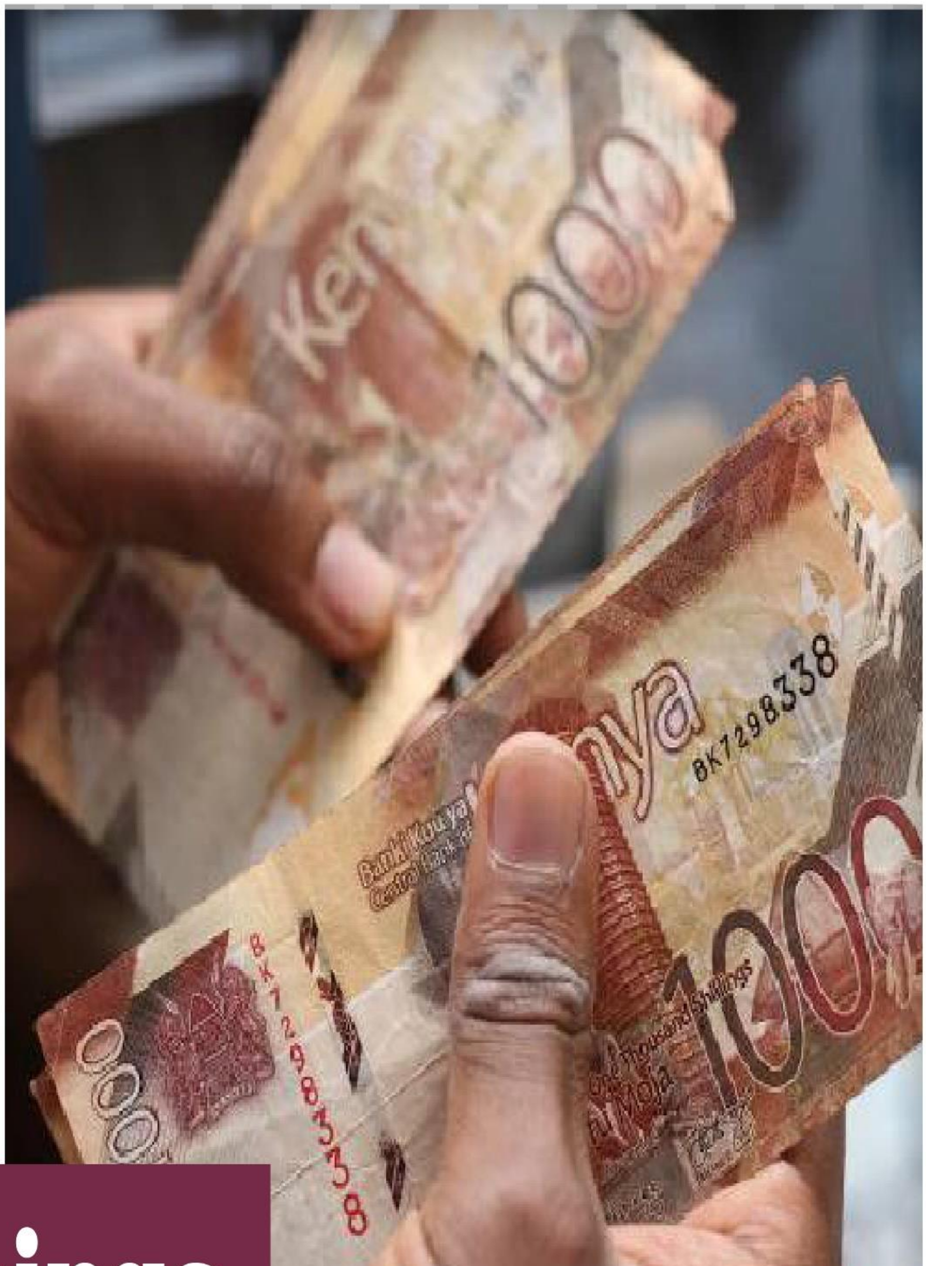
www.aib-axysafrica.com



Earnings Note

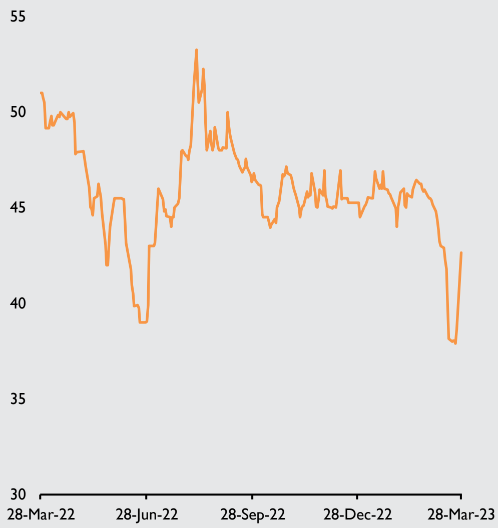
research@aib-axysafrica.com

Company details

Bloomberg Ticker	EQTY:KN
NSE Code:	EQT
Issued Shares (Bn)	3.77
52-week high:	53.50
52-week Low	37.90

As at 29th March 2023

Price chart – Last 12 Months



AIB-AXYS Research, NSE

Historical Price Performance

	1m	3m	6m	12m
Absolute	**-6.26%**	**-5.75%**	**-8.28%**	**-7.04%**

AIB-AXYS Research, NSE

Analysts

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Faith Sang

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March 29th 2023

Equity Group FY'22 Earnings Note

Recomm: **BUY**	**Current Price:** KES 42.65	**Target Price:** KES 57.92

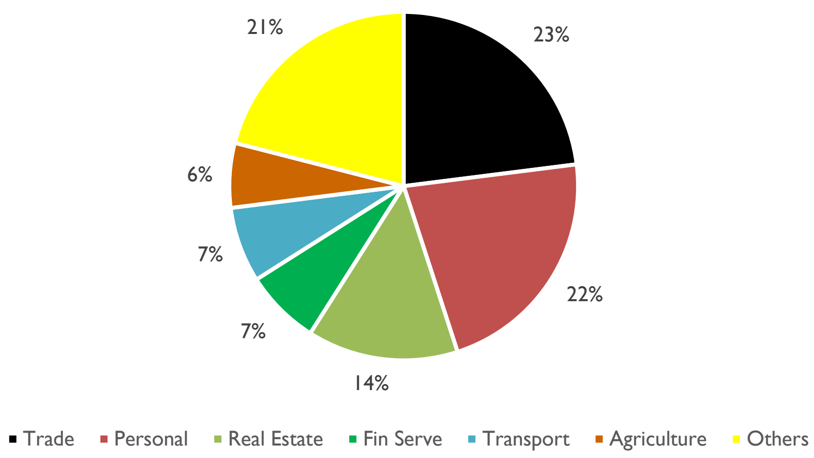
Summary

- **Equity Group released their FY'22 earnings results posting a 14.64% & 15.35% climb in EPS & PAT respectively** to KES 11.90/share and KES 46.10Bn respectively. Bottomline growth was driven by a 24.98% increase in net interest income and a 34.46% growth in non-interest income. Trailing ROaE & ROaA improved to 29.05% & 3.35% respectively in FY'22. NIMs remained adequate at 7.18% while the profit margin edged down to 31.59%. Better than our expectation of KES3.00 DPS, the board of directors recommended a final dividend of KES 4.00 representing a 33.33% increase from KES 3.00 paid out in FY'21.
- **Loan book grew 20.21% y/y to KES 706.59Bn faster than the 9.72% y/y growth in the customer deposits to KES 1.05Tn** leading to a 586bps decline in the loan deposit ratio to 67.16% from 61.29% recorded in FY'21. In terms of value digital loans disbursed , the mobile loan to branch loan mix was at 19:81 while the transaction count was at 83:17 signifying the higher loan tickets in the branches. Loan book concentration shifted to corporate with 41.00% of the loan book compared to 37.00% in FY'21 while allocation to SMEs as a percentage of total loan book declined to 25.00% from 28.00% in FY'21. We also observed the share of foreign currency loans jumping to 48.50% from 44.10% in FY'21 attributable to shilling depreciation and dollar shortage leading to difficulties in settling loans. We observed a 10.89% jump in the balance sheet size to KES 1.45Tn, which we believe has opened a race to KES 2.00Tn with close competitors KCB who have already crossed the KES 1.50Tn mark. We foresee majority of this growth being inorganic through regional expansion.

Key Highlights

- **Non-Funded Income Outperformed Net Interest Income:** Non-Funded income grew 34.46% y/y to KES 59.94Bn faster than a 24.98% y/y increase in Net Interest Income to KES 86.00Bn. The jump in NFI was mainly driven by a 58.42% y/y jump in income from forex trading income highlighting the impact of the prevailing dollar shortage as the bid/ask spreads widened to between 5-8.00% of the CBK indicative rate. Subsequently, the NII:NFI revenue mix shifted to 60:40 in favor of non funded income from 61:39 recorded in FY'21. The lender's balance between higher asset yields and sourcing for cheaper deposits led to a flat Net Interest Margin (NIM) to 7.18% while the Yield on assets marginally increased by 69bps y/y to 9.99% in FY'22, while cost of funds increased 28bps to 2.93% y/y.
- **Digital Channels Drive Efficiency:** The Cost to Income ratio less impairment improved 66bps on a year-on-year basis to 48.43% mainly attributed to continued uptake of digital channels. Growth from digital channels was driven by growth in pay with Equity (PWE) and Equitel. However, we noticed a decline in the usage of the mobile app and internet banking. In line with FY'22 industry trend, Loan loss provisions grew 163.73% y/y to KES 15.41Bn indicating increased lending risk despite the implementation of risk-based lending.
- **Asset Quality Improvement Continues:** Gross NPLs edged up 17.23% y/y to KES 63.13Bn lower than the loan book growth, leading to the NPL ratio declining 21bps y/y to 8.41% lower than the latest industry average of 13.30%. Meanwhile, the NPL Coverage improved to 70.53% from 68.73% in FY'21 driven by impairment provisioning growing faster than gross NPLs. At subsidiary level, Tanzania and Uganda recorded the highest NPL ratios at 18.90% and 12.60%, while the rest are below the group figure.

FY'22 Loan Book Composition



Other Performance Metrices

I. **DRC is Proving to be a Shrewd Acquisition** – Equity BCDC in DRC continues to be the most profitable regional subsidiary by recording an impressive 45.00% y/y surge in PAT to KES 5.80Bn which was marginally lower than our KES 6.00-7.00Bn estimates. However, we noticed slow growth in deposits (+2.00%) contrary to an impressive loan book growth (+53.00%) compared to the other regional subsidiaries. The subsidiary's ROaE of 15.70% in FY'22 (versus 14.90% in FY'21) remains below the group's average of 27.60%. Additionally, we remain concerned about the high cost to income ratio (64.80% in HY'22 vs Group's CIR of 48.43%) and we expect BCDC costs to remain the highest, of all subsidiaries, as it is still in the investment phase. We also noted impressive PAT performance by the Rwandan (+104.00% y/y to KES 2.80Bn) and Tanzania (+409.00% y/y to KES 400.00Mn) subsidiaries. However, Uganda's PAT declined 25.00% y/y to KES 2.00Bn. We noted the improvement in the Tanzanian business with improvements in the ROaE, ROA, Cost-to-Income and NPLs after lagging the other regional businesses in previous reporting periods.

II. **Trade Finance is the New Growth Frontier** - In recent past, EQTY has organized several trade missions more so focused on DRC and other frontier markets, as well as, placing themselves at the forefront of off-balance sheet financing in the Kenyan market. The results of which we saw in the FY'22 results where lending associated to trade finance jumped 5.07% y/y to KES 22.80Bn while off balance sheet and guarantees items also increased 36.75% y/y to KES 162.60Bn. As such, income from trade finance activities jumped 75.76% y/y to KES 5.80Bn. We expect to see growth in this front driven by the continued economic recovery in the region coupled with trading between EAC countries which is the key operating market for EQTY.

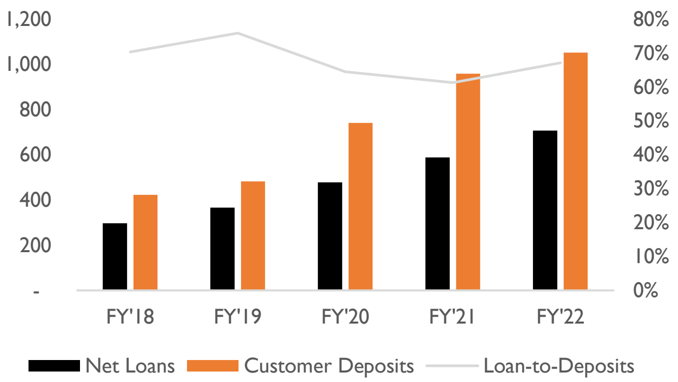
III. **Allocation to Government Securities Remained Flat** – We observed the allocation to government securities maintain at KES 394.00Bn which we suspect is largely driven by the 942x jump in the mark-to-market losses from government securities holdings to KES 43.80Bn. The yields from government securities increased to 10.50% from 9.60% in FY'21. Notably, exposure to Kenya Eurobonds has left the lender in the red following a spike in the sovereign yields (Yields have an inverse relationship with bond prices so a rise in yields is negative for bond valuation). We expect the losses to be maintained in FY'23 given the rising political risks, dim economic outlook and shilling depreciation continuing to provide an unpleasant view for the Kenyan macro story. However, given that majority of the bonds will mature after 2032, we still see room for readjustment and a correction of the pricing.

Outlook – We expect regional subsidiaries, use of digital channels and Forex trading revenue to drive Noninterest Income. The bank's lending will be supported by the focus on more SME credit and sector specific initiatives such as trade finance and infrastructure funding in subsidiary markets in Rwanda, Uganda and DR Congo. We expect the yield on loans to improve driven by the approval of the risk-based model by CBK.

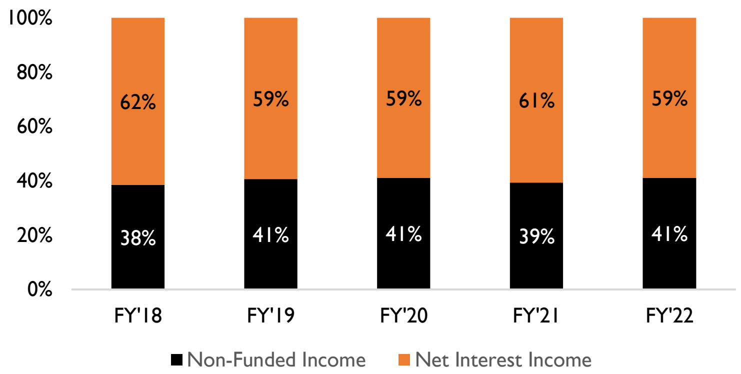
Valuation – The counter is currently trading at a P/B multiple of 0.95x compared to a sector average of 0.77x. The counter closed yesterday's trading at KES 42.65, a YTD loss of 5.75%. However, we maintain our **BUY** recommendation on the counter as we believe the current price provides an attractive entry point for long-term investors coupled with the 9.37% dividend yield.

Equity Group FY'22 Earnings Charts

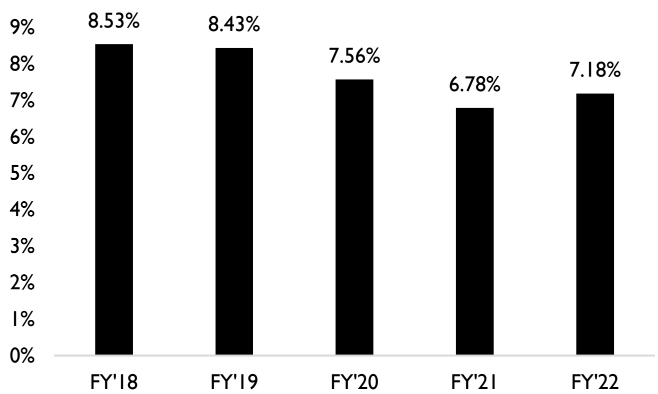
Graph 1: Customer Deposits continue to drive Balance sheet growth



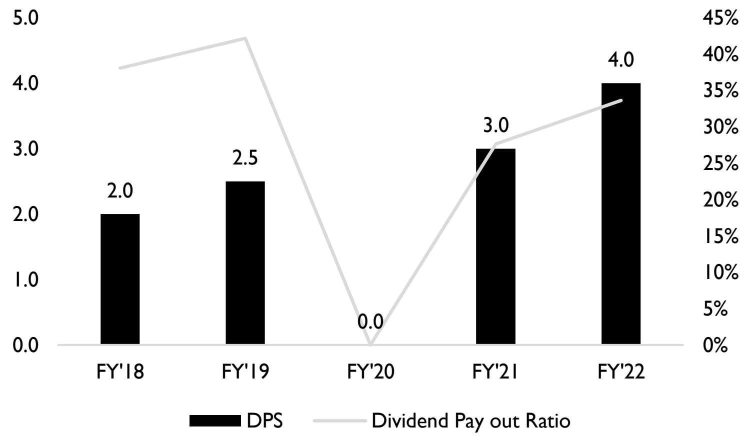
Graph 2: Revenue mix continues to favour Non-Funded Income



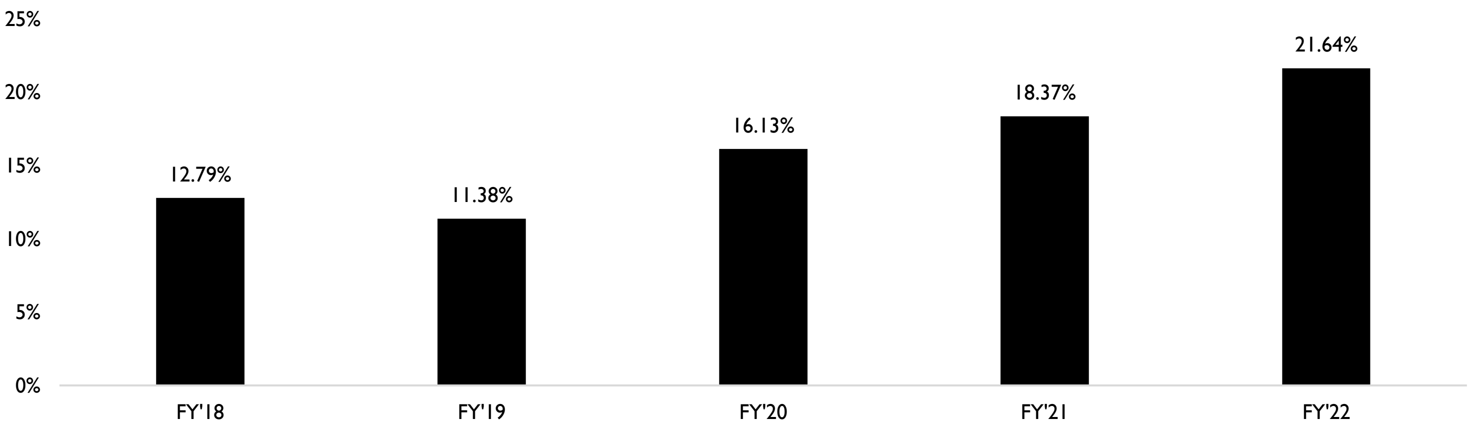
Graph 3: We observed a slight uptick in Net Interest Margins



Graph 4: Dividend Payout Ratio Improved



Graph 5: Forex Income as a % of Net Income Continues to Pick up



Source: NSE, CBK, Company Fillings, AIB-AXYS Analyst Estimates

Financial Statement Summary

1. Statement of Profit and Loss

Income Statement	FY20	FY'21	Q1'22	Q2'22	Q3'22	FY'22	y/y % Change
Net Interest Income	55.15	68.81	19.35	39.80	59.84	86.00	24.98%
Net non-Interest Income	38.51	44.58	11.91	25.84	42.22	59.94	34.46%
Total Operating income	93.66	113.39	31.27	65.65	102.06	145.94	28.71%
Provision for Impairment	(26.63)	(5.84)	(1.81)	(4.09)	(9.66)	(15.41)	163.73%
Total Operating expenses	(72.66)	(61.51)	(15.98)	(34.73)	(57.74)	(86.09)	39.97%
Profit before tax	22.17	51.88	15.28	30.92	44.32	59.84	15.35%
Profit after tax	19.79	40.97	11.54	23.75	33.35	44.89	9.58%
Core EPS	5.24	10.38	3.06	6.29	8.84	11.90	14.61%

2. Statement of Financial Position

Balance Sheet	FY20	FY'21	Q1'22	Q2'22	Q3'22	FY'22	y/y % Change
Government Securities	217.41	394.10	389.41	365.02	366.45	393.98	-0.03%
Loans and Advances	477.85	587.78	623.56	650.56	673.91	706.59	20.21%
Total Assets	**1,015.09**	**1,304.91**	**1,269.46**	**1,333.86**	**1,363.75**	**1,447.01**	**10.89%**
Customer Deposits	740.80	958.98	900.92	970.94	1,007.34	1,052.16	9.72%
Total Liabilities	876.45	1,128.72	1,095.25	1,183.47	1,209.67	1,264.80	12.06%
Total Equities and Liabilities	**1,015.09**	**1,304.91**	**1,269.46**	**1,333.86**	**1,363.75**	**1,447.01**	**10.89%**

3. Key Metrics

	FY20	FY'21	Q1'22	Q2'22	Q3'22	FY'22
Growth Metrices (y/y)						
Loan book Growth	30.40%	23.00%	27.85%	28.86%	20.55%	20.21%
Customer Deposits Growth	53.45%	29.45%	14.05%	18.45%	15.11%	9.72%
PAT Growth	-10.91%	99.37%	35.98%	36.16%	27.91%	15.05%
Spreads Analysis						
Yield on Assets	10.12%	9.30%	9.88%	9.53%	10.14%	9.99%
Cost of Funds	2.70%	2.65%	2.84%	2.83%	2.93%	2.93%
Net Interest Margin	7.56%	6.78%	7.20%	6.92%	7.29%	7.18%
ROaE	16.55%	25.99%	28.05%	30.48%	29.98%	29.05%
ROaA	2.38%	3.45%	3.70%	3.80%	3.73%	3.35%
Profit Margin	21.46%	35.34%	37.94%	37.21%	33.68%	31.59%
Operating Efficiency						
Cost of Income Less LLP	49.15%	49.09%	45.34%	46.68%	47.11%	48.43%
Cost of Assets	5.45%	4.80%	1.21%	2.50%	3.77%	5.14%
Loan to Deposit	64.50%	61.29%	69.21%	67.00%	66.90%	67.16%
Asset Quality						
NPL	11.53%	8.62%	8.96%	8.85%	9.47%	8.41%
NPL Coverage	62.40%	68.73%	66.03%	64.07%	62.95%	70.53%
Cost of Risk	5.57%	0.99%	0.29%	0.63%	1.43%	2.18%
Capital Adequacy						
Core Capital/TRWA	14.80%	12.90%	13.90%	15.50%	16.10%	15.60%
Total Capital /TRWA	18.90%	17.70%	18.70%	20.20%	20.70%	20.20%
Liquidity	59.30%	63.40%	56.90%	53.20%	51.80%	52.10%

******Key Metrices are on a Trailing basis***

Source: Company Fillings, AIB-AXYS Estimates

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