



**KCB Group
FY'23 Earnings
Note**





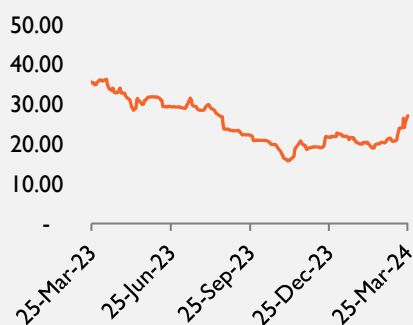
KCB Group FY'23 Earnings Note

March 26th, 2024

Ticker Information

NSE Code:	KCB
Bloomberg Ticker	KNCB:KN
Issued Shares (Bn):	3.21
52-week high:	KES 39.50
52-week low:	KES 15.00

Chart 1: Price Trend (Last 12 Months)



Source: NSE, AIB-AXYS Research

Historical Share Performance

Last	1M	3M	6M	12M
Change	33.3%	25.6%	22.2%	-23.4%

Source: NSE, AIB-AXYS Research

Analysts

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Recommendation

BUY

Current Price

KES 27.20

Target Price

KES 36.25

Summary

- **KCB Group FY'23 earnings surprised on the downside to post an 8.3% y/y decline in net earnings to KES 37.46Bn.** The decline was prompted by a 154.7% jump in loan loss provisions – reflecting the impact of increased downgrades and adverse FX movements over the period. Net Interest Margins shrunk considerably on account of a faster surge in cost of funds and lagged returns on interest earning assets.
- **The Board of Directors elected to pause dividends in FY'23 amid a drive to reshore capital buffers in the Kenyan Banking Unit.** Management also announced the kickstart of the nine-month sale process of its 100% shareholding in National Bank of Kenya to Access Holdings at a targeted multiple of 1.25x of Net Book Value. If successful, KCB Group aims to accelerate their ROE to 25% by end year 2024.

Key Highlights

- **Tale of Two Halves:** Net Interest Income 23.9% y/y to KES 40.04Bn propelled by organic loan demand growth and loan up-pricing under the risk-based pricing regime. Non-funded income grew 33.9% y/y to KES 14.53Bn. Total Operating Expenses (excluding provisions) however grew 40.1% to KES 83.15Bn – leading to a 460bps rise in the Cost to Income ratio to 50.3%. The average yield on interest earning assets paced up 20bps y/y to 10.3% - despite higher market reinvestment yields and the rollout of risk-based pricing. The cost of funds however quickened 110bps y/y across subsidiaries to 4.0% owing to the rising rate landscape. Consequently, the trailing net interest margin shrunk 90bps y/y to 6.4%.
- **A Hypervigilant Approach:** The stock of Gross Non-Performing Loans (NPLs) increased 29.2% y/y to KES 208.3Bn – stemming largely from adverse FX movements and increased downgrades in the manufacturing and real estate sectors. In response to the macroeconomic uncertainty especially in the Kenyan franchises, management jacked up credit impairment provisions by 154.7% y/y – signaling an overly cautious approach.

Balance Sheet Dynamics

KCB Group's Total Assets grew 39.7% y/y to KES 2.17Bn – driven by deposit growth appended from the TMB subsidiary and subsequent loan book expansion. The bulk of additional lending was channeled towards households and businesses in trade, tourism and manufacturing sectors – which unluckily witnessed elevated delinquency rates.

72% of the loan book was priced in Local currency – affording a fair hedge against adverse FX movements. On the funding side, deposits growth accelerated to 48.9% y/y with the bulk of the growth arising from retail and corporate demand and savings deposits. 73% of deposits comprised demand and savings accounts, whereas 27% comprised term and call deposits.

The decision to withhold dividends in 2023 has helped lift capital buffers in the KCB Kenya by 60bps to 1.3 percentage points above regulatory minimum. As of the close of 2023, all subsidiaries except NBK were compliant with core and total capital requirements,

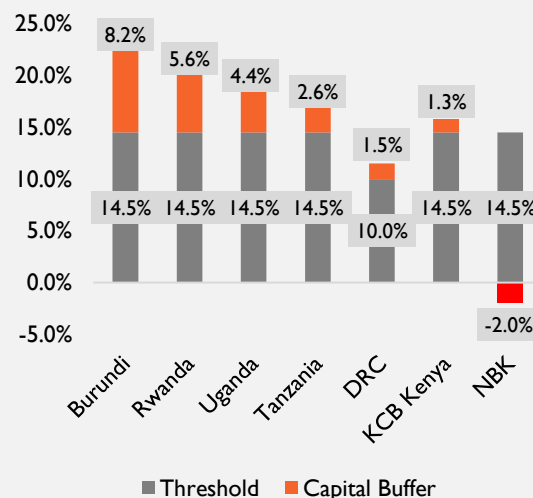
Subsidiary Performance

Subsidiaries posted remarkable growth in 2023 led by Trust Merchant Bank in DRC, which posted a 69% y/y revenue growth to KES 25.8Bn. Uganda and Tanzania posted revenue growth rates of 54% and 52% respectively to KES 4.4 and KES 6.1Bn respectively. All Kenyan franchises recorded a mild growth of 6%, supported by growth in non-banking subsidiaries – yet dragged by a 2% y/y revenue decline in the National Bank of Kenya.

Recommendation

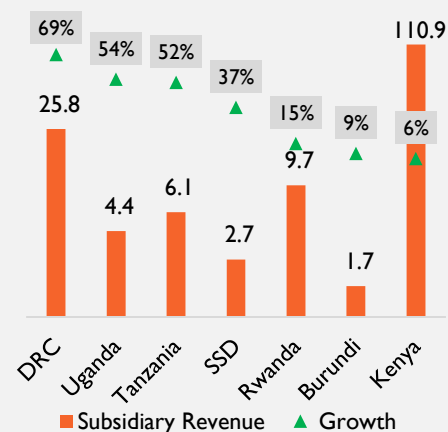
- **We upgrade our recommendation to BUY on KCB Group on account of its strategic restructuring to restore capital buffers to adequate thresholds.** From our point of view, we expect the successful sale of NBK to yield long-term savings for the Group franchise. Ongoing market leadership in G-to-G oil financing is set support further profitability growth. At the current market price, the stock is trading at P/E ratio of 2.3x and a P/B ratio of 0.4x. Our one-year target price for KCB Group currently stands at KES 36.25 per share - representing a c.33.3% upside potential from current levels.

Chart 2: Capital Adequacy Buffers Across Subsidiaries



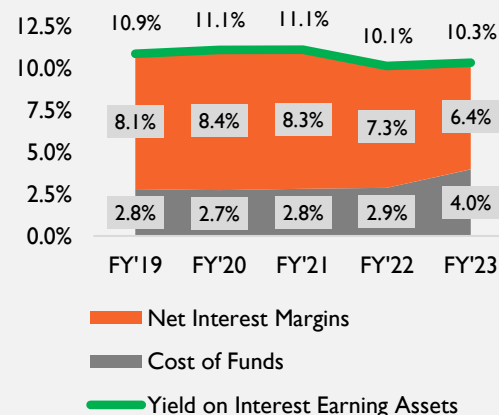
Source: Company filings, AIB-AXYS Research.

Chart 3: Agile Subsidiary Revenue Growth



Source: Company filings, AIB-AXYS Research.

Chart 4: Shrinking Net Interest Margin



Source: Company filings, AIB-AXYS Research.

Income Statement (KES Mn)	FY'19	FY'20	FY'21	FY'22	FY'23	y/y % Change
Net Interest Income	56,131.0	67,535.9	77,694.0	86,653.3	107,334.0	▲ 23.9%
Net non-Interest Income	28,171.5	28,450.6	30,940.6	30,550.7	57,904.7	▲ 89.5%
Total Operating income	84,302.5	95,986.5	108,634.6	117,204.0	165,238.7	▲ 41.0%
Provision for Impairment	(8,888.9)	(27,508.4)	(12,988.1)	(13,206.9)	(33,635.6)	▲ 154.7%
Total Operating expenses	(47,405.2)	(70,669.3)	(60,820.3)	(72,573.5)	(116,786.6)	▲ 60.9%
Profit before tax	36,897.4	25,317.2	47,814.3	43,303.0	48,452.1	▲ 11.9%
Profit after tax	25,165.2	19,201.9	34,173.0	40,837.7	37,461.5	▼ (8.3%)
Core EPS Annualized	7.83	5.98	10.63	12.71	11.66	▼ (8.3%)
Dividend Per Share	3.50	1.00	2.00	2.00	0.00	▼ (100.0%)

Balance Sheet (KES Mn)	FY'19	FY'20	FY'21	FY'22	FY'23	y/y % Change
Government Securities	128,459.5	208,764.9	270,835.0	310,425.1	397,202.2	▲ 28.0%
Loans and Advances	539,747.3	595,254.3	675,480.4	863,268.1	1,095,933.2	▲ 27.0%
Total Assets	898,572.2	987,810.3	1,139,672.6	1,554,030.0	2,170,874.0	▲ 39.7%
Customer Deposits	686,583.2	767,224.5	837,141.4	1,135,417.4	1,690,908.4	▲ 48.9%
Total Liabilities	768,831.1	845,386.0	966,165.0	1,347,753.7	1,934,516.1	▲ 43.5%
Shareholder's Funds	129,741.1	142,424.3	171,713.2	200,200.4	228,320.0	▲ 14.0%

Ratio Analysis	FY'19	FY'20	FY'21	FY'22	FY'23	y/y % Change
Spreads Analysis						
Yield on Assets	10.9%	11.1%	11.1%	10.1%	10.3%	▲ 0.2%
Cost of Funds	2.8%	2.7%	2.8%	2.9%	4.0%	▲ 1.1%
Net Interest Margin	8.1%	8.4%	8.3%	7.3%	6.4%	▼ (0.9%)
ROE	20.7%	14.1%	21.8%	22.0%	17.5%	▼ (4.5%)
ROA	3.1%	2.0%	3.2%	3.0%	2.0%	▼ (1.0%)
Profit Margin	29.9%	20.0%	31.5%	31.4%	22.7%	▼ (8.8%)
Operating Efficiency						
Cost to Income Less LLP	45.7%	45.0%	44.0%	45.7%	50.3%	▲ 4.6%
Cost to Assets Less LLP	4.3%	4.4%	4.2%	3.8%	3.8%	▲ 0.0%
Loan to Deposit Ratio	78.6%	77.6%	80.7%	76.0%	64.8%	▼ (11.2%)
Asset Quality						
Total NPL Ratio	11.2%	15.1%	16.9%	17.3%	17.3%	▲ 0.0%
NPL Coverage	59.5%	59.8%	52.9%	52.4%	62.5%	▲ 10.1%
Cost of Risk	10.5%	28.7%	12.0%	10.2%	20.4%	▲ 10.2%
Capital Adequacy						
Core Capital/TRWA	17.2%	17.9%	18.0%	14.5%	12.2%	▼ (2.3%)
Total Capital /TRWA	19.0%	19.5%	21.7%	18.1%	17.4%	▼ (0.7%)
Liquidity	40.1%	37.3%	39.1%	38.5%	48.5%	▲ 10.0%



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