Faida Daily Report

FAIDA INVESTMENT BANK

28th May 2020

Kenya Shilling Performance

KES	Value	Daily Change %	YTD Change %
US Dollar	107.0265	0.1%	(5.6%)
STG Pound	131.8571	(0.2%)	0.8%
EURO	117.9565	(0.6%)	(4.0%)

Source: CBK; Negative () = Depreciation, Positive = Appreciation

Market Summary

Index	Value	Daily Change %	YTD Change %
NASI	136.51	(0.9%)	(18.0%)
NSE 20	1,964.46	(0.6%)	(26.0%)
NSE 25	3,214.83	(0.3%)	(21.6%)

	Today	Previous	Daily Change %
Market Capitalization (KES Bn)	2,086.36	2,106.30	(0.9%)
Number of Shares Traded (Q)	14,226,000	16,358,600	(13.0%)
Equity Turnover (KES)	392,181,182	490,695,069	(20.1%)
Foreign Buys (%)	45.9%	54.3%	
Foreign Sells (%)	86.2%	87.0%	
Foreign Participation (%)	66.1%	70.6%	

Source: NSE

Equities Performance

	Top Gainers	Price (KES)	Daily Change	YTD Change %	Volume Traded
1.	Crown Paints	49.50	10.0%	(20.8%)	100
2.	Olympia	2.38	9.7%	18.4%	100
3.	Home Afrika	0.50	6.4%	(16.7%)	25,300
4.	Flame Tree	1.10	4.8%	(55.5%)	172,400
5.	Absa Bank	10.75	3.9%	(19.5%)	997,900

	Top Losers	Price (KES)	Daily Change	YTD Change %	Volume Traded
1.	Kenya Airways	2.44	(9.6%)	19.0%	284,500
2.	NSE	7.70	(4.2%)	(37.7%)	52,700
3.	STANLIB FAHARI	6.34	(3.9%)	(32.7%)	132,000
4.	Kenya Power	1.77	(2.7%)	(37.0%)	781,900
5.	Umeme	7.28	(2.7%)	(12.1%)	210,800

	Movers	Turnover (KES)	Volume (KES))	Price (KES)
1.	Safaricom	226,192,395	8,063,900	28.05
2.	Equity Group	30,311,860	846,700	35.80
3.	KCB Group	25,890,240	715,200	36.20
4.	BAT	24,768,000	77,400	320.00
5.	Stanbic	22,840,350	270,300	84.50

Source: NSE

Market Commentary

The All Share Index eased by 0.9% from the previous session to close the day at 136.51 characterized by reduced trading volumes. Equity dipped marginally by 0.1%; Safaricom eased by 2.1% owing to profit taking activities. Among the day's top gainers were ABSA Kenya (+3.9%), Housing Finance (+2.3%) and KCB (+1.5%). ABSA's after tax profit grew by 3.0% y/y to KES 2.0 billion while Equity's declined by 14.1% y/y to 5.3 billion (see more below).

Recommendations

Counter	Recommendation	Price (KES)	Daily Change %	YTD Change %
KCB Group	Long-term Buy	36.20	1.5%	(33.0%)
Equity Group	Long-term Buy	35.80	(0.1%)	(33.1%)
Absa Kenya	Long-term Buy	10.75	3.9%	(19.5%)
Stanbic Holdings	Long-term Buy	84.50	0.0%	(22.7%)
StanChart	Sell	168.50	(0.9%)	(16.8%)
Safaricom	Hold	28.05	(2.1%)	(11.0%)
Bamburi	Sell	44.00	1.0%	(45.0%)

For more detailed information on the following recommendations, please click [here](#):

Bonds Performance

	Today	Previous	Daily Change %
Total Deals	127	124	2.4%
Bond Turnover	3,078,004,968	3,465,770,596	(11.2%)

Actively Traded Bonds

GOK Bonds	Fixed Rate %	Traded Yield %	Value Traded (Mn)	DTM
FXD1/2019/5	11.3040	11.2500	800.0	1,362
FXD4/2019/10	12.2800	12.2500	200.0	3,455
IFB1/2017/7	12.5000	10.3000	150.0	1,635

Source: NSE; DTM = Days to Maturity

News Highlights

Equity Group Records a 14.1% Decline in PAT for 1Q2020

- Equity Group's after-tax profits for 1Q2020 declined by 14.1% y/y to KES 5.3 bn. The group's profits were weighed down by an increase in:
  - i. Loan loss provisions which rose by 660.4% y/y to KES 3.1 bn as the group enhanced its level of provisioning to manage expected risks.
  - ii. Operating costs which advanced by 16.3% y/y to KES 9.7 bn.
- The higher provisioning was underpinned by a 51.9% y/y rise in gross non-performing loans to KES 44.6 bn – leading to an NPL ratio (gross non-performing loans/gross loans) of 10.9% (1Q2019: 9.0%)
  - o The sectors that recorded the highest NPL ratios were large enterprises, SMEs and agriculture at 13.2%, 12.5% and 9.1% respectively.
  - o South Sudan and Tanzania had significantly higher NPL ratios at 40.8% and 40.5% respectively compared to the rest of regional subsidiaries; DRC at 11.7%, Rwanda at 4.1% and Uganda at 3.2%.
- Operating costs were driven by:
  - i. staff costs which increased by 23.0% y/y to KES 3.2 bn
  - ii. other expenses which rose by 22.7% y/y to KES 4.8 bn
  - o Consequently, the group's cost-to-income ratio edged up to 49.2% (1Q2019: 47.8%).
- Total interest income grew by 14.3% y/y growth to KES 15.4 bn supported by an 18.7% y/y rise in interest income from loans and advances to KES 10.8 bn. The growth in interest income from loans and advances and this was due to a 24.1% y/y rise in the group's loan book (net loans) which outweighed a 50 bps dip in the yield on loans (to 11.6%).
- Total interest expenses increased by 26.7% y/y to KES 3.9 bn on the back of:
  - o A 143.4% y/y increase in other interest expenses (from borrowings) to KES 926.7 mn due to a 3.2% y/y growth in borrowings to KES 52.6 bn.
  - o A 12.0% y/y rise in interest expenses arising from customer deposits to KES 2.8 bn on the back of a 16.5% y/y growth in

customer deposits to KES 499.3 bn. However, cost of customer deposits eased slightly by 10 bps to 2.3%.

- The group realized a net interest income of KES 11.5 bn (reflecting a growth of 10.6% y/y) and a NIM of 7.6% (1Q2019:8.2%). The lower NIM was a result of a faster growth in interest earning assets (+17.0% to KES 604.2 bn) vis-à-vis the growth posted in net interest income.
- Non-funded income grew by 15.8% y/y to KES 8.3 bn (mainly driven by a 16.8% y/y rise in other fees and commissions to KES 4.0 bn) resulting in a 110 bps increase in the proportion of non-funded income to total income to 41.9%.

Commentary

- We have concerns about the group's deteriorating asset quality which we expect to experience further pressure in 2Q2020 owing to the COVID-19 pandemic.
- Moreover, given the fact that the group has waived the fees on mobile money transactions (owing to a government directive aimed at encouraging digital cash transfer), we expect a dip in fees and commissions in 1Q2020 and consequently NFI.
- Lastly, given the low interest rate environment and challenges in lending, we also anticipate reduced interest incomes in 2Q2020.
- Overall, with the exception of the impact of the current pandemic, the group remains fundamentally sound (regional diversification, digitization strategy, high ROaE) and we recommend investment in the counter to investors with a long-term view. Thus, we maintain our **long-term buy** on the counter.

ABSA Kenya Posts a 3.0% y/y Growth in After Tax Profits for 1Q2019

- ABSA Kenya reported a 3.0% y/y growth in after tax profits to KES 2.0 billion (1Q2019: KES 1.9 billion). The performance was characterized by a 15.8% y/y increase in non-funded income to KES 3.0 billion and a 5.4% y/y decline in operating expenses (excluding provisions) to KES 4.1 billion.
- Total interest income grew by 2.8% y/y to KES 7.6 billion primarily driven by a 7.5% y/y increase in income from government securities to KES 2.1 billion (the bank's holdings of government securities edged up by 7.2% y/y to KES 125.4 billion while the yield on government securities dropped to 6.7% from 7.4% in 1Q2019).
- Income from loans and advances rose by 1.0% y/y to KES 5.5 billion on the back of a 12.4% y/y growth in the net loan book to KES 203.0 billion (1Q2019: KES 180.5 billion). The yield on loans and advances fell to 11.0% from 12.1% in 1Q2019.
- Total interest expenses declined by 1.9% y/y to KES 2.0 billion predominantly owing to a 13.2% y/y decrease in interest expenses from customer deposits to KES 1.6 billion. Although customer deposits increased by 6.6% y/y to KES 238.7 billion (1Q2019: KES 224.0 billion), the cost of deposits fell to 2.6% from 3.3% in 1Q2019.
- Consequently, net interest income edged up by 4.5% y/y to KES 5.6 billion. The net interest margin dipped to 6.9% (1Q2019: 7.5%) due to a faster growth in interest earning assets (+10.1% y/y to KES 330.4 billion).
- Non-funded income realized a 15.8% y/y growth to KES 3.0 billion supported by a 47.4% rise in foreign exchange trading income to KES 1.1 billion.
    - Fees and commissions on loans and advances grew by 8.8% y/y to KES 390.7 million.
    - However, other fees and commissions declined by 3.0% y/y to KES 1.1 billion.
    - The contribution of non-funded income to total income grew to 34.5% (1Q2019: 32.2%).
- Operating expenses (excluding provisions) fell by 5.4% y/y to KES 4.1 billion owing to:
    i. an 18.4% y/y dip in other expenses to KES 1.1 billion and
    ii. an 84.0% y/y drop in rental charges to KES 23.7 million
    - The cost to income ratio (excluding provisions) improved to 47.1% (1Q2019: 53.9%).
    - According to management, following the separation from Barclays PLC, the bank will continue to make substantial investments in systems and rebranding over the course of the next two years; as well acquire various services from Barclays PLC.
- Loan loss provisions surged by 75.2% y/y to KES 1.1 billion as gross non-performing loans increased by 12.45 y/y to KES 17.3 billion. The NPL ratio (net gross/net loan book) grew marginally to 3.0% (1Q2019: 2.8%).
- The separation costs increased by 126.8% y/y and amounted to KES 552.1 million. According to the bank, adjusting for this non-recurring "exceptional" item (non-recurring in the long-term), the bank posted after tax profits growth of 13.0% y/y to KES 2.3 billion.

Commentary

- We note that the decline in interest expenses was on the back of a dip in customer deposit expenses which fell, in line with the bank's strategy to lower its cost of deposits. We are optimistic about the bank's focus on cheaper deposits.
- We are also optimistic about:
  - The increased NFI contribution. However, we note with concern the decline in other fees and commissions which had recovered in FY2018 (attributed to the growth of the Timiza platform). In light of the Covid-19 pandemic, the bank has waived fees on digital transactions and provided loan relief options (including loan repayment relief of up to twelve months).
  - The bank's cost management efforts which have resulted in continued improvement in the cost-to-income ratio (C/I) which has fallen below industry average (previously was the highest among Tier 1 banks in FY2017).
- We expect more caution on lending, particularly to the sectors largely affected by the crisis such as the SME sector. This may see reduced lending through the bank's Wezesha Bishara proposition through which the bank offered unsecured loans to SMEs. We note that the bank, as part of its new strategy had gradually started including more risky segments such as SMEs in its lending strategy. We expect resumption once the economy stabilizes.
- We maintain our **long term buy** recommendation on ABSA Kenya. The banks is fundamentally strong with a high dividend yield and is focused on digitization and operational efficiency.
  - We note that the two years (FY2018 and FY2019) into implementation of the new 5-year strategy the bank has recorded improvements in ROaE, cost to income ratio and non-funded income contribution.
  - We expect with the separation from Barclays PLC that the bank will have more flexibility to produce localized products.

E-mail:

research@fib.co.ke

Recommendations Guide

LONG-TERM BUY: The Company has strong fundamentals. However, there are certain investments or strategies that would require an investor to have a long-term view of the company to allow for capital appreciation. Also, the company may be facing head wings which we view as short term

BUY: Strong fundamentals. Minimal risks to the catalysts/growth drivers

NEUTRAL: This is where the positives and negatives in a company almost balance out. You can accumulate for the long term.

SELL: Deteriorating fundamentals. Risks outweigh the catalyst/growth driver

HEAD OFFICE:

Crawford Business Park,
Ground Floor,
State House Road
Tel: 0207606026-37
P.O Box 45236-00100
Nairobi