



Equity Group IH20 Earnings Note

Equity Group's IH20 PAT plummeted 24.9% y/y to KES 9.0B below our expectation of a 7.6% y/y decline in net earnings. The drop was driven by a 773.4% y/y surge in loan loss provisions to KES 8.0B and a 13.0% y/y drop in non-interest income to KES 14.4B. We maintain our BUY recommendation on Equity Group with a target price of KES 41.82 offering a potential upside of 38.3% on the current price of KES 30.25.

Loans and advances maintain double-digit growth despite the pandemic

Deviating from our estimates of a 4.3% y/y growth in loans and advances, the group's loan book grew 22.0% y/y to KES 391.6B. This saw interest income increase 18.5% y/y to KES 32.8B which was further boosted by a 20.5% y/y increase in investment in government securities to KES 216.4B as increased liquidity saw banks opt to invest in government paper.

Interest expense driven by strong growth is customer deposits

Customer deposits grew 18.6% y/y to KES 543.9B higher than our expectation of a 10.0% y/y growth which saw interest expenses surge 23.6% y/y to KES 8.2B. Cost of funds closed at 3.0% higher than our estimate of 2.7%.

Asset book quality deteriorates, NPL ratio worsens to 13.7%

Lower than our expectation of an NPL ratio of 11.7%, NPLs escalated 55.8% y/y to KES 45.6B due the prevailing pandemic that has seen a general slowdown in business activity with a total shutdown in some sectors such as tourism and hospitality. Fueled by this, loan loss provisions galloped 773.4% y/y to KES 8.0B dimming the bottom line. Cost of risk rose to 4.1% higher than our estimate of 3.2%.

Outlook

The Group's IH20 performance was below our expectation with a higher drop in earnings than anticipated. The surge in loan loss provisions given the banks exposure in the SME sector that is deemed to have a high-risk profile was expected. While loan book growth and deposit growth was higher than our estimates, we remain worried of the increase in interest expenses. We expect that following the repeal of the rate cap, we may see further growth in interest income as the bank is able to price loans in consideration of the risk profile. We also anticipate that the bank will maintain its current cost of risk at 4.1% going forward.

The counter is trading at p/e and p/b multiples of 12.7x and 0.9x respectively.

DATE:	18 th Aug 2020
Target Price:	KES 16.82
Current Price:	KES 30.25
Upside:	45.5%
52 Week High:	KES 28.00
52 Week Low:	KES 55.50

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Financial Statements

	1H19	1Q20	2Q20	1H20	AIB-AXYS Estimates	chg y/y	chg q/q	Deviation
Income Statement	KES M	KES M	KES M	KES M	KES M			
Interest Income	27,680	15,423	17,373	32,796	31,609	18.5%	12.6%	3.8%
Interest Expense	6,601	3,878	4,283	8,161	7,605	23.6%	10.4%	7.3%
Net Interest Income	21,079	11,545	13,090	24,635	24,004	16.9%	13.4%	2.6%
Non Interest Income	16,543	8,313	6,087	14,400	15,013	-13.0%	-26.8%	-4.1%
Total Operating Income	37,623	19,858	19,177	39,035	39,017	3.8%	-3.4%	0.0%
Total Operating Expenses	9,159	9,738	17,320	27,058	19,056	195.4%	77.9%	42.0%
Loan Loss Provision Expense	918	3,117	4,906	8,022	6,065	773.4%	57.4%	32.3%
Operating Profit	28,464	10,120	1,857	11,977	19,961	-57.9%	-81.6%	-40.0%
Profit Before Tax	16,989	7,004	4,974	11,977	13,896	-29.5%	-29.0%	-13.8%
Current Tax	4,981	1,679	1,222	2,900	3,474	-41.8%	-27.2%	-16.5%
Profit After Tax	12,008	5,284	3,738	9,022	10,422	-24.9%	-29.3%	-13.4%
EPS (KES)	3.18	1.41	0.98	2.39	2.76	-24.8%	-30.5%	-13.5%

Balance Sheet

Total Shareholders' Equity	102,739	116,404	123,360	123,360	110,137	20.1%	6.0%	12.0%
Customer Deposits	458,595	499,329	543,894	543,894	504,455	18.6%	8.9%	7.8%
Total Liabilities	535,923	576,782	623,109	623,109	588,980	16.3%	8.0%	5.8%
Total Equity and Liabilities	638,663	693,186	746,469	746,469	699,336	16.9%	7.7%	6.7%
Government and Other Securities	179,619	189,878	216,386	216,386	211,412	20.5%	14.0%	2.4%
Net Loans and Advances	320,886	379,215	391,633	391,633	334,684	22.0%	3.3%	17.0%
Total Assets	638,663	693,186	746,469	746,469	707,638	16.9%	7.7%	5.5%

Key Ratios

Gross NPL (KES M)	29,243	44,648	45,550	45,550	39,158	55.8%	2.0%	16.3%
NPL Ratio	8.9%	11.3%	11.2%	11.2%	11.7%			
Cost of Risk	0.6%	3.3%	5.0%	4.1%	3.2%			
Loan to Deposits	70.0%	75.9%	72.0%	72.0%	66.3%			
Yield on Interest Earning Assets	10.1%	10.8%	11.4%	10.8%	11.6%			
Cost of Funds	2.9%	3.1%	3.1%	3.0%	3.0%			
NIM	7.3%	7.7%	8.3%	7.8%	8.6%			
Non Funded income/Total Income	44.0%	41.9%	31.7%	36.9%	38.5%			
Cost to Income Ratio	24.3%	49.0%	90.3%	69.3%	48.8%			
ROE	23.4%	18.2%	12.1%	14.6%	18.9%			
ROA	3.8%	3.0%	2.0%	2.4%	2.9%			
Core Capital/TRWA	17.5%	17.5%	6.9%	16.9%				
Total Capital/TRWA	19.5%	21.0%	20.2%	20.2%				
Liquidity Ratio	56.5%	51.6%	54.2%	54.2%				
P/E (x)				12.7				
P/B (x)				0.9				

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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