EQUITY GROUP HOLDINGS LTD
FY16 RESULTS NOTE

AIB CAPITAL LTD

YOUR VISION OUR MISSION

Equity Group released their full year 2016 results this week, announcing a net profit drop for the first time since listing in 2000. Net profits reduced by 4% to Kes 16.6 bn, which was worse than our expected 9% growth forecast, mainly due to a sudden increase in loan loss provisions in Q4. Year-on-year, provisions increased by 173% to Kes 6.6 bn with half of this coming in the last quarter of the year.

The group's loan book shrunk by 1.4% to Kes 266 bn against our estimated 8% growth. This was mainly due to a 5% contraction in the Kenyan loan book. Despite a contraction of 82% in the South Sudan loan book, the regional loan book grew by 15%, increasing its proportion to the total loan book from 17% to 20%. The group experienced a contraction of Kes 5 bn in the loan book in Q4, as it shifted funds towards government securities. This was reflected in the loan to deposit ratio which reduced from 89% to 79% year-on-year. Total investment in government securities for the year grew by 135% to Kes 100.6 bn, increasing the proportion of government securities to total assets to 21% from 10% in 2015.

As expected, the quality of the loan book deteriorated with the NPL ratio closing the year at 6.8% compared to 3.3% in 2015, with total NPLs increasing by 128% from Kes 7.3 bn to Kes 16.7 bn. The group's NPL coverage reduced from 50.7% to 41.9%. Management expects a decline a decline in the ratio to 5.5-6% in 2017.

Despite the contraction of the loan book, interest income grew by 19.3% to Kes 51.8 Bn, attributed to improved yields in 2016 and increased investment in government securities. The yield on interest earning assets averaged 12.8 % in 2016 against an average yield of 12.5% in 2015. Interest from loans therefore grew by 13% and interest from government securities grew by 80%, now contributing 15% of total interest income, up from 10%.

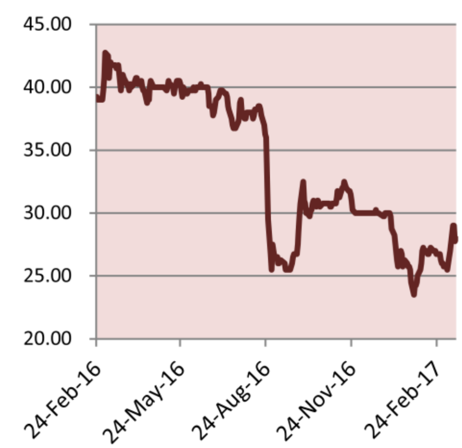
Interest expense increased by 7.5% to Kes 10.0 bn, despite a drop in cost of funds from 2.7% to 2.6%. Total deposits grew by 11% to Kes 337 bn, in line with our 11% projection, with most of the growth coming from the Kenyan business. The proportion of Kenya deposits to the group deposits increased from 77.4% to 79.3%.

Regional deposit growth was negatively impacted by a 50% contraction in South Sudan deposits. Management indicates that excluding this impact, total deposits would have grown by 14%. Interest bearing deposits grew by 30% to Kes 100 bn, increasing its proportion to total deposits to 30% from 25%.

RATING: HOLD

Bloomberg ticker	**EQBNK KN**
Last close (KES)	28.75
Target price (KES)	30.39
Upside potential	5.7%
Market cap (KES bn)	105.66
Dividend Yield	7.0%
52-week range	42.25 – 23.50

1-Yr Price Movement



Analysts

Dominic Ruriga
rurigad@aibcapital.com

Abdulrahman Hussein
husseina@aibcapital.com

Jeff Mburu
mburuj@aibcapital.com

Dealing

Bernard Kung'u
kungub@aibcapital.com

Ben Gichuru
gichurub@aibcapital.com

Mary Byera
byeram@aibcapital.com

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Non-funded income was flat at Kes 22 bn with fees and commissions income from loans declining by 15% to Kes 4.4 bn, in line with the 1.4% contraction of the loan book. NFI to total income therefore declined from 39.1% to 34.7%.

Operating expenses grew 9.4% to Kes 32.5 Bn, driven by a 13% increase in staff costs. The group managed to reduce its cost-to-income ratio from 52.9% to 50.7% as it continues to reap from increased use of alternative channels. Transactions from agents and mobile increased by 21% and 141% respectively while ATM and branch transactions reduced by 19% and 14% respectively. Through the Equitel's platform, Equity's market share of total mobile transactions increased from 13.1% from December 2015 to 16.0% as at September 2016.

The group's ROE reduced from 25.5% to 21.5% against our projection of 23%.

Below is a summary of the key metrics from the results;

	FY 2015	FY 2016
Loan book growth	26.02%	-1.4%
Earnings growth	2.36%	-4.2%
ROE	25.5%	21.5%
Yield on interest earning assets	12.8%	14.5%
Cost of deposits	2.65%	2.78%
NIMs	10.5%	11.0%
CTI (excluding provisioning)	52.9%	50.7%
Non funded / total income	39.1%	34.7%
NPL Coverage	50.7%	41.9%
Loan to deposit	89.3%	78.9%
Core capital to RWA	18.7%	18.7%
Total capital to RWA	20.2%	19.7%
Liquidity ratio	33.2%	47.6%

Outlook

Based on Q4 performance, we expect a 14% decline in interest income due to reduced yield on interest bearing assets and we project average NIMs of between 8% to 9%, which is 100 bps lower than management projections. We also expect the group to focus on growing their regional loan book, based on management's loan book growth projections.

We expect the group to focus on growing their non-funded income, but overall we expect a net profit decline of within 10% for 2017 and a decline in ROE to levels of 19-20%, against management expectation of above 22%. Our projections are based on a prevailing interest rate cap.

Equity maintained a dividend of Kes 2.00 per share, giving a dividend yield of 7.0% on the current price. This represented a payout ratio of 45.7%. Despite the low growth outlook, management decided to retain excess cash, expressing confidence of a turnaround in the operating environment.

We maintain our Kes 30.40 per share target price which represents a 5.7% upside from the current cum dividend price of Kes 28.75. Equity currently has a dividend yield of 7.0% and is trading at a trailing P/B of 1.28x against 0.86x industry average.

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