

HF Group – FY17 Earnings Update

“ Surprise Bonus Issue”

HF Group FY17 net earnings plunged 86.1% y/y to KES 126.2M on the back of a tough business environment given the prevailing rate cap and the long electioneering period in 2017. The lender slashed dividend to KES 0.35 (-30.0% y/y) yet recommended an unanticipated bonus share issue of 1 share for every 10 held at close of business on 27th April, 2018 for both. Net interest income dipped 17.1% y/y to KES 7.2B while non funded income soared 78.2% y/y to KES 1.3B.

Total operating profit dipped 55.5% y/y to KES 910.6M due to a 29.1% y/y rise in operating expenses to KES 3.4B, and a 24.3% y/y dip in net interest income to KES 3.0B despite a 78.2% y/y surge in non-funded income to KES 1.3B.

The surge in non-funded income was a result of a 1183.5% y/y rise in foreign exchange income to KES 50.2M and a 154.6% y/y surge in other income to KES 1.1B despite a 37.6% y/y drop in gross fees and commission to KES 200.4M, showing the lenders efforts to diversify revenue streams.

Loan loss provision expense posted a decline of 17.6%y/y to KES 576.2M contradicting a 32.6% y/y rise in gross non performing loans to KES 8.2B. The banks quality of loan book saw NPLs close at 16.0% compared to an industry average of 10.6% (+490 bps y/y) a worrisome trend for the lender.

Total interest expense decreased 11.1% y/y to KES 4.2B in line with a marginal decrease of customer deposits at 3.75y/y to KES 36.7B and a 86.6% y/y plunge in deposits due to banks and financial institutions to KES 83.7M. This is a clear indicator of the lenders struggle to attract deposits.

Loans and advances also dropped 8.9% y/y to KES 49.6B the effect of which saw the interest income dip 17.1% y/y to KES 7.1B caused by the tough business environment in 2017 and stringent lending with the looming rate cap.

Future Outlook

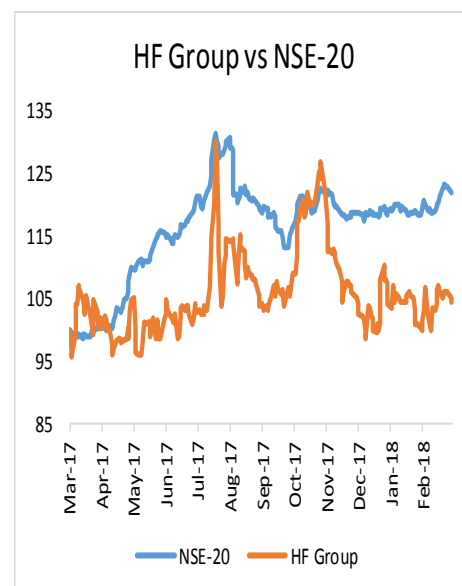
The lender has been struggling to change its negative earnings story with profits going down 6150bps y/y. Given the high competitive environment in the banking sector, management will have to come up with clear, well laid out strategies to change the numbers going forward. We are hopeful that a repeal on the rate cap will help boost the lenders top line.

The counter is currently trading at KES 8.95, 24.0x P/E, 0.3x P/B, and a dividend yield of 3.9%.

Bloomberg Ticker : HFCL KN
Reuters Ticker: HFCK.NR

Share Statistics	
Current Price (KES)	8.95
Issued shares (M)	338.8
Market cap (USD M)	40.9
Year end	Dec
Foreign ownership (%)	26.29
Free float (%)	78.35
Av daily trading vol (USDk)	7.4

Price Trend



Source: Bloomberg

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Financials

	FY16	1Q17	2Q17	3Q17	4Q17	FY17	% chg y/y	% chg q/q
	KES '000	KES '000	KES '000	KES '000	KES '000	KES '000		
Income Statement								
Interest Income	8,607,499	1,850,057	1,829,870	1,773,285	1,679,414	7,132,626	-17.1%	-5.3%
Interest Expense	4,673,384	1,052,453	1,068,260	1,149,113	886,432	4,156,258	-11.1%	-22.9%
Net Interest Income	3,934,115	797,604	761,610	624,172	792,982	2,976,368	-24.3%	27.0%
Foreign Exchange Income	3,913	24,134	14,052	5,428	6,607	50,221	1183.4%	21.7%
Gross Fees and Commission	321,233	52,464	68,276	82,220	-2,480	200,480	-37.6%	-103.0%
Other Income	430,403	96,251	169,305	132,436	697,760	1,095,752	154.6%	426.9%
Non Interest Income	755,549	172,849	251,633	220,084	701,887	1,346,453	78.2%	218.9%
Total Operating Income	4,689,664	970,453	1,013,243	844,256	1,494,869	4,322,821	-7.8%	77.1%
Total Operating Expenses	2,642,618	640,314	731,365	745,530	1,294,987	3,412,196	29.1%	73.7%
Loan Loss Provision Expense	699,166	200,749	180,117	98,012	97,325	576,203	-17.6%	-0.7%
Operating Profit	2,047,046	330,139	281,878	98,726	199,882	910,625	-55.5%	
Profit Before Tax and exceptional items	1,347,880	129,390	101,761	716	102,528	334,395	-75.2%	
Current Tax	459,824	41,052	31,087	-	113,269	185,408	-59.7%	
Profit After Tax	905,829	88,338	70,674	716	-33,512	126,216	-86.1%	
EPS (KES)	2.59	1.01	-0.10	-0.10	-0.45	0.37	-85.6%	
DPS (KES)	0.50					0.35	-30.0%	
Balance Sheet								
Total Shareholders' Equity	11,289,262	11,380,009	11,304,186	11,300,885	11,449,535	11,449,535	1.4%	1.3%
Deposits due to Banks & Financial Institutions	624,701	832,243	81,827	302,248	83,682	83,682	-86.6%	-72.3%
Customer Deposits	38,082,325	38,257,115	37,357,722	33,619,068	36,660,591	36,660,591	-3.7%	9.0%
Total Liabilities	60,640,878	60,526,916	60,318,666	59,486,878	56,091,581	56,091,581	-7.5%	-5.7%
Total Equity and Liabilities	71,930,140	71,906,925	71,622,852	70,787,763	67,541,116	67,541,116	-6.1%	-4.6%
Cash and CBK Balances	3,372,363	3,745,896	3,112,410	5,829,218	3,270,722	3,270,722	-3.0%	-43.9%
Balances due from Banks & Financial Institutions	1,659,112	832,243	3,613,678	4,539,031	2,301,262	2,301,262	38.7%	-49.3%
Government and Other Securities	4,085,550	4,249,727	3,434,773	730,608	2,287,296	2,287,296	-44.0%	213.1%
Net Loans and Advances	54,469,605	54,598,316	54,469,605	51,194,205	49,639,639	49,639,639	-8.9%	-3.0%
Fixed Assets	1,458,087	1,435,212	1,372,061	1,360,600	1,517,380	1,517,380	4.1%	11.5%
Total Assets	71,930,140	71,906,926	71,622,852	70,787,763	67,541,116	67,541,116	-6.1%	-4.6%
Key Ratios								
Gross NPL (KES M)	6,193,462	7,783,590	7,914,856	8,104,752	107,415	8,212,167	32.6%	
Interest In Suspense (KES M)	1,017,611	1,113,363	1,151,481	1,413,209	-152,166	1,261,043	23.9%	
Total NPL (KES M)	5,175,851	6,670,227	6,763,375	6,691,543	259,581	6,951,124	34.3%	
Loan Loss Provision (KES M)	1,298,340	1,436,766	1,697,679	1,571,083	158,021	1,729,104	33.2%	
Net NPL	3,877,511	5,233,461	5,065,696	5,120,460	101,560	5,222,020	34.7%	
NPL Ratio	11.1%	13.9%	14.1%	15.4%	0.2%	16.0%	490bps	
Coverage Ratio	21.0%	18.5%	21.4%	19.4%	147.1%	21.1%	10bps	
Cost of Risk	1.3%	1.5%	1.3%	0.8%	0.8%	1.2%	-10bps	
Loan to Deposits	143.0%	142.7%	145.8%	152.3%	135.4%	135.4%	-760bps	
Yield on Interest Earning Assets	14.3%	12.4%	11.9%	12.6%	12.4%	13.2%	-110bps	
Cost of Funds	12.1%	10.8%	11.4%	13.6%	9.6%	11.3%	-80bps	
NIM	2.2%	1.6%	0.5%	-1.0%	2.7%	1.8%	-40bps	
Non Funded/Total Income	16.1%	17.8%	24.8%	26.1%	47.0%	31.1%	1500bps	
Cost to Income Ratio	56.3%	66.0%	72.2%	88.3%	86.6%	78.9%	22600bps	
ROE	8.0%	3.1%	2.5%	0.0%	-1.2%	1.1%	-690bps	
ROA	1.3%	0.5%	0.4%	0.0%	-0.2%	0.2%	-110bps	
Core Capital/TRWA	15.7%	15.7%	14.6%	15.0%	15.8%	15.8%	10bps	
Total Capital/TRWA	17.4%	17.3%	16.1%	16.5%	17.2%	17.2%	-20bps	
Liquidity Ratio	26.9%	21.4%	26.4%	26.0%	20.7%	20.7%	-620bps	
P/E (x)						24.0		
P/B (x)						0.3		
Dividend Yield						3.9%		

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