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Bank of Kigali

Bank of Kigali: Poor Q1 20 results on higher cost of risk; reiterate Hold

Bank of Kigali **HOLD**

Faith Mwangi
Equity Research Analyst, Financials (East Africa)

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EARNINGS REPORT

- Profit outlook remains dim with net income expected to decline 30-40% in FY 20
- Management concerned about corporate business outlook and intends to maintain coverage levels above the 100% mark
- Reiterate Hold on recovery post-Covid-19 supported by large market share, access to government-related business

Bank of Kigali (Hold, TP RWF309) released poor Q1 20 results with net income declining 17% yoy and a 7% cost of risk impacting earnings negatively. Management is concerned about the outlook of the corporate business and intends to maintain coverage levels above the 100% mark. Still, compared with the East African banks that we cover, Bank of Kigali is one of the most prudent banks on provision coverage. The bank's pre-provision profit grew 23% yoy on low cost growth (+1% yoy) and saw a 14% yoy rise in operating income. According to management, the bank expects muted cost growth going forward with only targeted infrastructure investments being made over the next three years. Non-interest revenue growth was low at just 1% yoy with the bank failing to deliver growth from the insurance business, which had earlier recorded a strong growth trajectory that we had expected to be maintained for at least 3-4 years.

Bank of Kigali is trading at a current PB of 1.0x against a Q1 20 annualised ROE of 11.2%. We maintain our Hold recommendation on expected fall in earnings in FY 20 by an estimated 30-40%. However, a recovery after the Covid-19 pandemic will be supported by the bank’s large market share, access to government-related business and the government's plans to invest significantly in infrastructure.

Outlook

1. Management expects net income to decline 30-40% yoy in FY 20.
2. Management expects some economic recovery in Q4 20 with the government currently laying out plans for stimulating the economy.
3. Outlook on loan growth is expected to still be positive yoy, but weakness in asset quality is already showing in the corporate book, which is expected to result in higher cost of risk.
4. Non-funded income to remain flat in FY 20 on account of reduced transactions charges due to regulatory changes.
5. Net interest margin is expected to decline to 10% from 11.5% in FY 19 as management will be offering loans at much cheaper rates during the Covid-19 pandemic.

6. Cost/income target at 40% for FY 20, but investments in infrastructure will remain the key cost factor.

Key positives

1. Loan and deposit growth was 13% yoy and 22% yoy, respectively, which was supported by higher liquidity in the market within the quarter. Management expects some minimal loan book growth in the coming quarters, but is optimistic of economic recovery in Q4 20. The bank's large market share of 30%, 33% and 30% in assets, loans and deposits, respectively is likely to give the bank a head start post-Covid-19 crisis.

2. Modest cost growth of 1% yoy. Staff costs declined 6% yoy with management keen on encouraging clients to use alternative channels to minimise the need for higher head count. General expenses grew 15% yoy and management expects the only cost factor going forward will be investments in infrastructure.

Key negatives

1. Cost of risk jumped to 7% (from 2.7% in FY 19) after management downgraded the outlook on the corporate book. The bank has a coverage ratio of 121%, which we consider as healthy, but management is still keen on accelerating provision coverage on account of the Covid-19 impact. The bank is targeting to restructure about 40% of the loan book, which in our view, warrants the high coverage levels.

2. Non-interest income grew just 1% on weakness in the insurance business. We had expected the bank to deliver higher growth from the insurance business as it booked new clients through its network. We had also expected a high growth momentum for at least three years and hence, it is disappointing to see the lacklustre performance this early in the game.

Risks: Continued Covid-19 restrictions would adversely affect business operations and the economy.

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