FitchRatings

Banks
Bank Holding Companies
Kenya

NCBA Group PLC

Update

Key Rating Drivers

NCBA Group PLC's and NCBA Bank Kenya Plc's Long-Term Issuer Default Ratings (IDRs) are driven by their standalone creditworthiness, as expressed by their Viability Ratings (VRs) of 'b'. NCBA Bank's Long-Term IDR is also underpinned by a limited probability of government support, as reflected in its Government Support Rating (GSR) of 'b'. The Negative Outlooks on both entities' IDRs mirror the Outlook on the sovereign rating. This reflects the concentration of their operations within Kenya and high sovereign exposure relative to capital.

NCBA Group's and NCBA Bank's National Long-Term Ratings of 'AA(ken)' are in line with those of their larger peers, KCB Group PLC and KCB Bank Lenya Limited, and two notches below Stanbic Bank Kenya Limited (AAA(ken)/Stable), as the latter benefits from shareholder support.

VRs Equalised with Group VR: The VRs of NCBA Group, a non-operating bank holding company (BHC), and NCBA Bank, its main operating bank, are the same as the group VR, based on the consolidated assessment of NCBA Group. NCBA Bank is the majority (end-1Q24: 91%) of NCBA Group's consolidated assets. NCBA Group's VR also reflects acceptable double leverage at BHC (114% at end-1Q24), and high capital and liquidity fungibility within the group.

Challenging Operating Conditions: Kenya's operating environment has been affected by high interest rates aimed at curbing inflation and by the accumulation of public-sector arrears, which led to the banking sector's non-performing loans (NPLs) ratio rising to a high 16.1% at end-4M24. Large holdings of government debt securities (end-2023: 1.9x banking sector equity) add further pressure given the Negative Outlook on the sovereign rating.

Strong Business Profile: NCBA Group is the third-largest banking group in Kenya, with a 9% market share in system total assets and deposits through its main operating subsidiary, NCBA Bank. The group operates subsidiaries in three other East African countries.

High Exposure to the Sovereign: NCBA Group's investments in Kenya's government securities represented the majority of securities holdings and were a high 197% of its Fitch Core Capital (FCC) at end-1Q24. Single-obligor and industry concentrations are also high, reflecting the size and nature of the domestic economy.

Weak Loan Quality: NCBA Group's NPLs were 11.7% of gross loans at end-1Q24 (end-2023: 10.3%) and were 56% covered by total loan loss allowances. We expect NPLs to remain high in the medium term as borrowers' debt-servicing costs increase in the high interest-rate environment.

Strong Pre-Impairment Profitability: NCBA Group's operating profit/risk-weighted assets (RWAs) ratio was 5.1% in 3M24 (annualised; 2023: 5.4%), supported by wide net interest margins, strong non-interest income and adequate operating efficiency. Cost of risk (1.6% in 3M24, annualised) is likely to increase by end-2024 as asset quality remains under pressure, although pre-impairment profit (9.1% of average loans in 3M24, annualised) provides a strong cushion against a potential rise in risk costs.

Reasonable Capitalisation: NCBA Group's FCC to regulatory RWAs ratio decreased to 17.6% at end-1Q24 (end-2023: 18.4%) but remained sound by international standards. NCBA Group's regulatory core and total capital ratios are well above the regulatory minimums.

Deposit-Funded: NCBA Group's funding profile is dominated by customer accounts (92% of total liabilities at end-1Q24) and is moderately reliant on price-sensitive term deposits. Liquidity is good, as evidenced by a reasonable loans/deposits ratio of 63% at end-1Q24.

Ratings

NCBA Group PLC	
Foreign Currency	
Long-Term IDR	B
Short-Term IDR	B
Viability Rating	b
Government Support Rating	ns
National Ratings	
National Long-Term Rating	AA(ken)
National Short-Term Rating	F1+(ken)
NCBA Bank Kenya Plc	
Foreign Currency	
Long-Term IDR	B
Short-Term IDR	B
Viability Rating	b
Government Support Rating	b
National Ratings	
National Long-Term Rating	AA(ken)
National Short-Term Rating	F1+(ken)
Sovereign Risk (Kenya)	
Long-Term Foreign-Currency IDR	B
Long-Term Local-Currency IDR	B
Country Ceiling	B
Outlooks	
Long-Term Foreign-Currency IDRs	Negative
National Long-Term Ratings	Stable
Sovereign Long-Term Foreign-Currency IDR	Negative
Sovereign Long-Term Local-Currency IDR	Negative

Applicable Criteria

Bank Rating Criteria (March 2024)

National Scale Rating Criteria (December 2020)

Related Research

Fitch Affirms NCBA Group PLC at 'B', Outlook Negative (December 2023)

Fitch Affirms Kenya at 'B'; Outlook Negative (February 2024)

Kenya's Fiscal Challenges Persist as External Risks Ease (June 2024)

African Banks Resilient to Continued Challenging Operating Conditions (November 2023)

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Rating Sensitivities

Factors that Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade

A sovereign downgrade could result in a downgrade of the Long-Term IDRs and VRs of NCBA Group and NCBA Bank. Absent a sovereign downgrade, a downgrade could result from greater-than-expected asset quality pressure, as indicated by the impaired loans ratio rising above 20%, if this results in a marked weakening in profitability and low buffers over minimum capital requirements.

A downgrade of NCBA Bank's GSR would result from a downgrade of Kenya's Long-Term IDRs.

A rise in double leverage to above 120% on a sustained basis or regulatory restrictions on NCBA Bank channelling dividends or other cash flows to its BHC would pressure NCBA Group's VR.

A downgrade of both entities' National Ratings would result from a weakening of their creditworthiness relative to that of other Kenyan issuers.

Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade

The Outlooks on the Long-Term IDRs could be revised to Stable if the Outlook on Kenya's Long-Term IDRs was revised to Stable. An upgrade of the Long-Term IDRs and VRs would require a sovereign upgrade.

An upgrade of NCBA Bank's GSR would require an upgrade of Kenya's Long-Term IDRs.

An upgrade of both entities' National Ratings would result from a strengthening of their creditworthiness relative to that of other Kenyan issuers.

Significant Changes from Last Review

Sovereign Remains on Negative Outlook

Fitch affirmed Kenya's Long-Term IDRs of 'B' with Negative Outlooks on 16 February 2024. The Negative Outlooks reflect the sovereign's large funding needs, ongoing risks to external finances, high domestic financing costs, expensive external commercial borrowing, and challenges in fiscal consolidation, despite the government's stronger commitment to narrow the budget deficit.

The ratings are supported by the authorities' fiscal consolidation plans and monetary tightening, anchored by an IMF programme, recent recovery in the macroeconomic environment and strong medium-term growth prospects. The ratings are constrained by weak governance, high interest payments, a narrow revenue base and high external debt.

Kenya has had funding support from official creditors, particularly the IMF and World Bank, and issued a USD1.5 billion Eurobond in February 2024 in order to buy back the majority of its USD2 billion Eurobond maturing on 24 June 2024. These developments contributed to the Kenyan shilling appreciating materially (by 22% since the beginning of the year) to KES128.7/USD as of 14 June 2024, which should help reduce inflation pressures.

The Kenyan banking sector has high exposure to the sovereign through government securities held for revenue and liquidity purposes, which equalled 1.9x the banking sector's equity at end-2023. This is the case for most banking sectors in sub-Saharan Africa. High sovereign exposure relative to capital leaves Kenyan banks' solvency sensitive to losses imposed on creditors in the event of a sovereign default.

Higher Interest Rates Benefitting NIMs

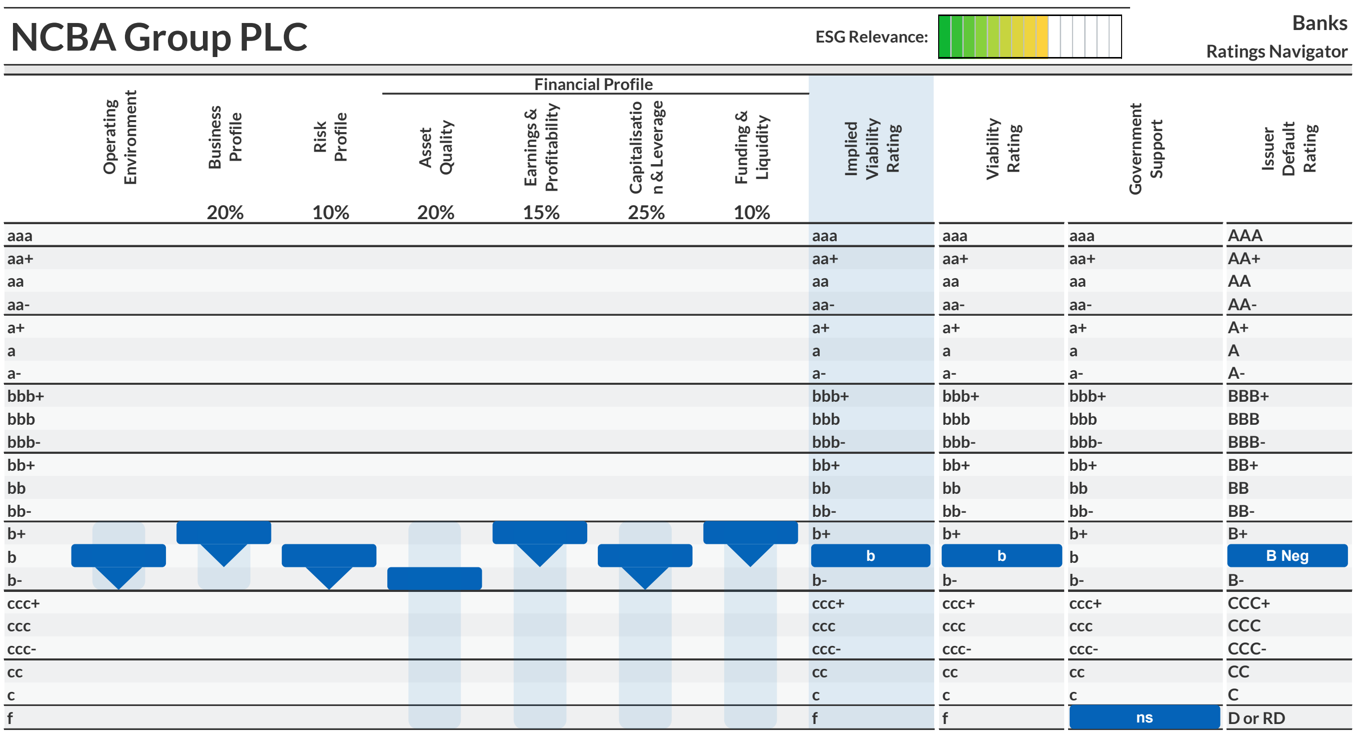
Inflation peaked at 9.2% in March 2023, and was persistently above the Central Bank of Kenya's (CBK) target band of 2.5%–7.5%, before starting to reduce in 2H23, reaching 5.1% in May 2024 due to monetary policy tightening and shilling exchange rate appreciation. The CBK maintained the central bank rate at 13% in June 2024.

High interest rates are positive for the banking sector's net interest margins as loans are predominantly extended at floating rates and reprice fairly quickly. However, higher interest rates have weighed on borrowers' debt service capacity and accentuated loan quality risks, contributing to the increase in the banking sector's regulatory NPL ratio to 16.1% at end-4M24, which is consistent with our forecast. However, the banking sector's pre-impairment operating profit (estimated at 8.5% of average loans in 2023) is strong, providing a large buffer to absorb rising impairment charges and support capitalisation despite continued loan growth.

Pending Public Sector Bills

Pending public sector bills to contractors, service providers and public sector employees (almost USD4 billion equivalent at end-2023, or 3.3% of 2023 GDP) have weakened borrowers' repayment capacity in recent years, contributing to the banking sector's high NPL ratio. The government set up a Pending Bills Verification Committee in early 2024 to evaluate the pending bills, some of which date back to July 2005. However, the National Treasury has not allocated funds for repayment of the bills in the latest supplementary budget. Fitch expects the banking sector's NPL ratio will remain heightened until these repayments begin.

Ratings Navigator



The Key Rating Driver (KRD) weightings used to determine the implied VR are shown as percentages at the top. In cases where the implied VR is adjusted upwards or downwards to arrive at the VR, the KRD associated with the adjustment reason is highlighted in red. The shaded areas indicate the benchmark-implied scores for each KRD.

Financials

Financial Statements

	31 Mar 24		31 Dec 23	31 Dec 22	31 Dec 21	31 Dec 20
	3 months	3 months	12 months	12 months	12 months	12 months
	(USDm)	(KESm)	(KESm)	(KESm)	(KESm)	(KESm)
	Unaudited	Unaudited	Audited – unqualified	Audited – unqualified	Audited – unqualified	Audited – unqualified
Summary income statement						
Net interest and dividend income	63	8,267.6	35,532.5	28,750	25,055	23,851
Net fees and commissions	35	4,653.8	16,836.7	18,084	16,956	15,960
Other operating income	23	3,055.3	9,241.3	13,228	5,722	6,133
Total operating income	121	15,976.7	61,610.5	60,062	47,733	45,944
Operating costs	61	8,088.4	28,695.8	25,077	21,535	20,752
Pre-impairment operating profit	60	7,888.3	32,914.7	34,985	26,198	25,192
Loan and other impairment charges	10	1,350.9	7,441.3	12,509	11,165	20,094
Operating profit	50	6,537.4	25,473.4	22,476	15,033	5,098
Other non-operating items (net)	n.a.	n.a.	8.5	16	2	-116
Tax	9	1,235.4	4,025.3	8,714	4,811	411
Net income	40	5,302.0	21,456.6	13,778	10,224	4,571
Other comprehensive income	-24	-3,187.9	-625.0	-2,186	-1,078	724
Fitch comprehensive income	16	2,114.1	20,831.6	11,592	9,146	5,295
Summary balance sheet						
Assets						
Gross loans	2,602	342,901.0	350,902.1	297,180	272,271	278,452
– Of which impaired	305	40,171.6	36,253.4	32,869	35,650	32,109
Loan loss allowances	170	22,395.6	20,687.7	21,147	30,807	30,945
Net loans	2,432	320,505.4	330,214.4	276,033	241,464	247,507
Interbank	451	59,498.3	28,244.8	9,748	9,870	41,664
Derivatives	n.a.	n.a.	8.4	17	97	89
Other securities and earning assets	1,657	218,387.1	250,770.1	236,690	226,252	169,159
Total earning assets	4,540	598,390.8	609,237.7	522,488	477,682	458,419
Cash and due from banks	386	50,823.7	81,832.1	54,571	78,404	34,512
Other assets	346	45,657.9	43,551.6	42,604	35,002	34,937
Total assets	5,272	694,872.4	734,621.4	619,663	591,088	527,868
Liabilities						
Customer deposits	4,158	548,067.7	579,401.9	502,677	469,890	421,505
Interbank and other short-term funding	97	12,827.0	26,680.6	5,914	14,775	6,303
Other long-term funding	38	4,982.3	6,412.0	4,207	6,097	13,320
Total funding and derivatives	4,293	565,877.0	612,494.5	512,798	490,762	441,127
Other liabilities	229	30,218.2	25,463.7	24,443	22,339	14,193
Total equity	749	98,777.2	96,663.2	82,422	77,987	72,548
Total liabilities and equity	5,272	694,872.4	734,621.4	619,663	591,088	527,868
Exchange rate		USD1 = KES131.8005	USD1 = KES156.4618	USD1 = KES123.373529	USD1 = KES113.141177	USD1 = KES109.171765

Source: Fitch Ratings, Fitch Solutions, NCBA Group

Key Ratios

	31 Mar 24	31 Dec 23	31 Dec 22	31 Dec 21	31 Dec 20
Ratios (%; annualised as appropriate)					
Profitability					
Operating profit/risk-weighted assets	5.1	5.4	5.1	3.9	1.4
Net interest income/average earning assets	5.5	6.2	5.6	5.3	5.4
Non-interest expense/gross revenue	50.6	46.6	41.9	45.2	45.3
Net income/average equity	21.8	24.2	17.1	13.7	6.5
Asset quality					
Impaired loans ratio	11.7	10.3	11.1	13.1	11.5
Growth in gross loans	-2.3	18.1	9.2	-2.2	2.6
Loan loss allowances/impaired loans	55.8	57.1	64.3	86.4	96.4
Loan impairment charges/average gross loans	1.6	2.3	4.4	4.0	7.3
Capitalisation					
Fitch Core Capital ratio	17.6	18.4	16.6	17.9	17.1
Tangible common equity/tangible assets	13.2	11.9	12.1	11.9	12.3
Net impaired loans/Fitch Core Capital	19.7	18.1	15.9	7.0	1.8
Funding and liquidity					
Gross loans/customer deposits	62.6	60.6	59.1	57.9	66.1
Customer deposits/total non-equity funding	96.9	94.6	98.0	95.8	95.6

Source: Fitch Ratings, Fitch Solutions, NCBA Group

Support Assessment

Commercial Banks: Government Support	
Typical D-SIB GSR for sovereign's rating level (assuming high propensity)	b
Actual jurisdiction D-SIB GSR	b
Government Support Rating	ns
Government ability to support D-SIBs	
Sovereign Rating	B/ Negative
Size of banking system	Neutral
Structure of banking system	Neutral
Sovereign financial flexibility (for rating level)	Neutral
Government propensity to support D-SIBs	
Resolution legislation	Neutral
Support stance	Neutral
Government propensity to support bank	
Systemic importance	Negative
Liability structure	Negative
Ownership	Neutral

The colours indicate the weighting of each KRD in the assessment.
Higher influence Moderate influence Lower influence

NCBA Group's GSR of 'no support' reflects Fitch's view that government support is unlikely to extend to a non-operating holding company given its low systemic importance and a liability structure that may be more politically acceptable to be bailed in.

NCBA Bank's GSR of 'b' is in line with Kenya's D-SIB GSR of 'b' and considers a high propensity of the authorities to provide support to the bank given its high systemic importance, but also considers Kenya's limited financial flexibility, as captured in the sovereign rating.

We believe the Kenyan authorities have a strong propensity to support NCBA Bank and the wider banking system, reflecting our view that the authorities have an incentive to maintain financial stability in order to preserve Kenya's position as a regional financial hub.

The authorities' ability to support banks is constrained by Kenya's limited financial flexibility, as captured by its Long Term IDR of 'B'. However, the ability to support banks is influenced in a positive manner by the banking system's small size (with total assets and private-sector credit at end-2023 equivalent to 50% and 25% of 2023 GDP, respectively), a moderately fragmented market structure, material foreign ownership and only moderate FC external funding.

Environmental, Social and Governance Considerations

FitchRatings **NCBA Group PLC**

Banks
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Credit-Relevant ESG Derivation

				ESG Relevance to Credit Rating
NCBA Group PLC has 5 ESG potential rating drivers NCBA Group PLC has exposure to compliance risks including fair lending practices, mis-selling, repossession/foreclosure practices, consumer data protection (data security) but this has very low impact on the rating. Governance is minimally relevant to the rating and is not currently a driver.	key driver	0	issues	5
	driver	0	issues	4
	potential driver	5	issues	3
	not a rating driver	4	issues	2
		5	issues	1

Environmental (E) Relevance Scores

General Issues	E Score	Sector-Specific Issues	Reference	E Relevance
GHG Emissions & Air Quality	1	n.a.	n.a.	5
Energy Management	1	n.a.	n.a.	4
Water & Wastewater Management	1	n.a.	n.a.	3
Waste & Hazardous Materials Management; Ecological Impacts	1	n.a.	n.a.	2
Exposure to Environmental Impacts	2	Impact of extreme weather events on assets and/or operations and corresponding risk appetite & management; catastrophe risk; credit concentrations	Business Profile (incl. Management & governance); Risk Profile; Asset Quality	1

Social (S) Relevance Scores

General Issues	S Score	Sector-Specific Issues	Reference	S Relevance
Human Rights, Community Relations, Access & Affordability	2	Services for underbanked and underserved communities: SME and community development programs; financial literacy programs	Business Profile (incl. Management & governance); Risk Profile	5
Customer Welfare - Fair Messaging, Privacy & Data Security	3	Compliance risks including fair lending practices, mis-selling, repossession/foreclosure practices, consumer data protection (data security)	Operating Environment; Business Profile (incl. Management & governance); Risk Profile	4
Labor Relations & Practices	2	Impact of labor negotiations, including board/employee compensation and composition	Business Profile (incl. Management & governance)	3
Employee Wellbeing	1	n.a.	n.a.	2
Exposure to Social Impacts	2	Shift in social or consumer preferences as a result of an institution's social positions, or social and/or political disapproval of core banking practices	Business Profile (incl. Management & governance); Financial Profile	1

Governance (G) Relevance Scores

General Issues	G Score	Sector-Specific Issues	Reference	G Relevance
Management Strategy	3	Operational implementation of strategy	Business Profile (incl. Management & governance)	5
Governance Structure	3	Board independence and effectiveness; ownership concentration; protection of creditor/stakeholder rights; legal /compliance risks; business continuity; key person risk; related party transactions	Business Profile (incl. Management & governance); Earnings & Profitability; Capitalisation & Leverage	4
Group Structure	3	Organizational structure; appropriateness relative to business model; opacity; intra-group dynamics; ownership	Business Profile (incl. Management & governance)	3
Financial Transparency	3	Quality and frequency of financial reporting and auditing processes	Business Profile (incl. Management & governance)	2
				1

How to Read This Page
ESG relevance scores range from 1 to 5 based on a 15-level color gradation. Red (5) is most relevant to the credit rating and green (1) is least relevant.

The Environmental (E), Social (S) and Governance (G) tables break out the ESG general issues and the sector-specific issues that are most relevant to each industry group. Relevance scores are assigned to each sector-specific issue, signaling the credit-relevance of the sector-specific issues to the issuer's overall credit rating. The Criteria Reference column highlights the factor(s) within which the corresponding ESG issues are captured in Fitch's credit analysis. The vertical color bars are visualizations of the frequency of occurrence of the highest constituent relevance scores. They do not represent an aggregate of the relevance scores or aggregate ESG credit relevance.

The Credit-Relevant ESG Derivation table's far right column is a visualization of the frequency of occurrence of the highest ESG relevance scores across the combined E, S and G categories. The three columns to the left of ESG Relevance to Credit Rating summarize rating relevance and impact to credit from ESG issues. The box on the far left identifies any ESG Relevance Sub-factor issues that are drivers or potential drivers of the issuer's credit rating (corresponding with scores of 3, 4 or 5) and provides a brief explanation for the relevance score. All scores of '4' and '5' are assumed to result in a negative impact unless indicated with a '+' sign for positive impact.h scores of 3, 4 or 5) and provides a brief explanation for the score.

Classification of ESG issues has been developed from Fitch's sector ratings criteria. The General Issues and Sector-Specific Issues draw on the classification standards published by the United Nations Principles for Responsible Investing (PRI), the Sustainability Accounting Standards Board (SASB), and the World Bank.

CREDIT-RELEVANT ESG SCALE

How relevant are E, S and G issues to the overall credit rating?

5	Highly relevant, a key rating driver that has a significant impact on the rating on an individual basis. Equivalent to "higher" relative importance within Navigator.
4	Relevant to rating, not a key rating driver but has an impact on the rating in combination with other factors. Equivalent to "moderate" relative importance within Navigator.
3	Minimally relevant to rating, either very low impact or actively managed in a way that results in no impact on the entity rating. Equivalent to "lower" relative importance within Navigator.
2	Irrelevant to the entity rating but relevant to the sector.
1	Irrelevant to the entity rating and irrelevant to the sector.

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' means ESG issues are credit neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit https://www.fitchratings.com/topics/esg/products#esg-relevance-scores.

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