Kenya listed banks

2022 Financial Results and Outlook for 2023

July 2023

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Foreword

We are delighted to launch the first edition of KPMG Kenya listed bank's results which analyses the financial results and key performance indicators for the listed commercial banks in the year ended 31 December 2022, compared to the previous year. This report provides sector leaders with succinct analysis along with insights and forward-looking views.

As the analysis depicts, the sector witnessed significant growth amidst the tough economic times the country continues to face.

In particular, we observed a 15.21 percent growth in the asset base of the listed commercial banks analysed. This was mainly a result of growth in loans and advances as well as completion of mergers and acquisitions by certain regional banks such as Equity Group and KCB Group. The growth in total assets contributed to an increase in profit before tax of 25.04 percent. Factors such as enhanced digital transformation could also have contributed to the growth.

Our analysis also shows a decrease in the cost to income ratio by 5.63 percent from the previous year which indicates that the listed commercial banks are operating at optimal productivity and effectiveness and this in turn has a positive impact on their profitability.

We expect to see more growth both organically through operational efficiency and inorganically through the anticipated acquisitions and expansions in the region in the coming years.

In addition to the analysis, this report features our insights and predictions on some of the emerging themes driving the sector.

Joseph Kariuki

Partner, Head of Banking Sector
KPMG Kenya
E: jkariuki@kpmg.co.ke

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01

Executive summary

Executive summary

Total Assets

Total assets increased from **KES 5.5 trillion** in 2021 to **KES 6.3 trillion** in 2022

Net Profit

Net Profit increased from **KES 136.5 billion** in 2021 to **KES 170.7 billion** in 2022

ROA

ROA increased from **2.34%** in 2021 to **2.57%** in 2022

Capital adequacy ratio

decreased from **18.2%** in 2021 to **17.9%** in 2022

Net interest margin

increased from **7.08%** in 2021 to **7.34%** in 2022

ROE

increased from **13.83%** in 2021to **17.24%** in 2022

Cost to income ratio

decreased from **54.3%** in 2021 to **48.6%** in 2022

Dividend payout ratio

decreased from **30%** in 2021to **24.5%** in 2022

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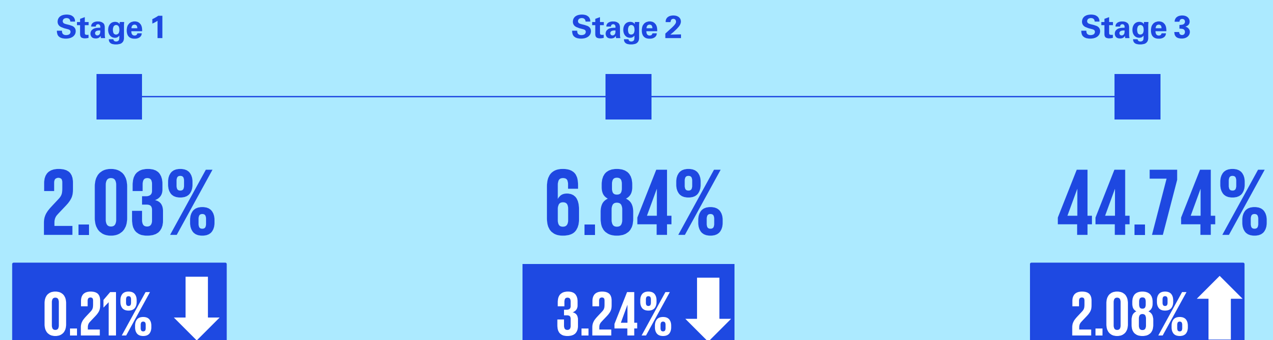
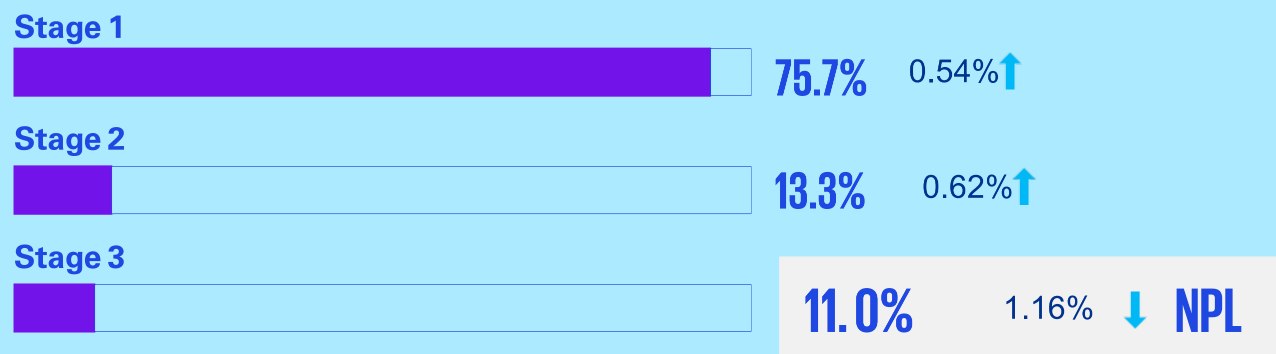
Executive summary continued

Coverage ratio on loans



Exposure subject to ECL



Net provision on loans

increased from **KES 244.5 billion** in 2021 to **KES 261.5 billion** in 2022.

NPL

decreased from **12.16 %** in 2021 to **11.00%** in 2022.

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Executive summary continued

		2022			2021		
		Highest	Average	Lowest	Highest	Average	Lowest
01	Capital Adequacy Ratio	20.70%	17.91%	12.20%	21.70%	18.24%	12.10%
02	Cost to income Ratio	87.14%	48.62%	40.80%	128.27%	54.26%	39.53%
03	Net Interest Margin	9.87%	7.34%	4.83%	9.36%	7.08%	4.28%
04	ROA	3.56%	2.57%	0.48%	5.30%	2.34%	(1.26%)
05	ROE	25.05%	17.24%	3.12%	24.89%	13.83%	(8.11%)
06	Dividend Payout Ratio	55.00%	33.36%	0.00%	59.85%	35.53%	0.00%
07	Lending Assets (in KES millions)	863,268	329,160	36,299	675,480	276,189	34,692
08	Operating Income (in KES millions)	145,935	56,959	3,039	113,386	46,298	2,365
09	Loan to Deposit ratio	92.50%	72.18%	50.00%	91.99%	68.99%	47.50%
10	Net Profit (in KES millions)	44,893	17,065	265	39,174	13,647	(682)
11	Total Assets (in KES millions)	1,554,029	629,461	56,995	1,304,913	546,355	53,210
12	NPL Ratio	21.36%	11.00%	7.70%	22.79%	12.16%	7.47%

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Interpretation statements

Profitability saw another double-digit increase of 25.04 percent, driven particularly by a growth in loan books, increased interest margins, lower loan impairment and a continued focus on cost efficiencies.

Asset growth remained robust as banks increased their asset base by 15.21 percent, which was driven by lending to customers.

Net interest margins increased by 0.26 percent, as a result of the rising interest rate environment, which helped drive profit growth.

The overall NPL ratio for the banking sector decreased by 1.16 percent and now stands at 11 percent, reflecting the conservative approach to credit risk management.

ROA (2.57 percent in 2022) increased by 0.23 percent compared with the prior year, owing to the rise in profitability being higher than the asset growth.

Cost-to-income ratios reduced by 5.63 percent compared to 2021 (54.26 percent to 48.62 percent), reflecting the continued focus on cost reductions and operating efficiency initiatives.

ROE (17.24 percent in 2022) increased by 3.4 percent compared with the prior year as profitability outpaced equity growth.

Dividend pay-out ratio decreased by 2.18 percent driven by larger payouts done by the banks in 2021, after the Covid- 19 payout holiday.

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02

Economic outlook

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Economic outlook

The global economies are faced with increased global uncertainties, that impact financial sector stability, volatile financial markets, weaker global growth outlook, continuing geopolitical tensions particularly the war in Ukraine, and continued tightening of monetary policies.

Most currencies in emerging and developing economies weakened against the U.S. Dollar, due to the tightening of U.S. monetary policy.

As a result, the MPC in June 2023, raised the Central Bank Rate (CBR) to 10.5 percent, because of sustained inflationary pressures mainly driven by driven by pressure from food and energy prices, and elevated global risks. This is expected to put pressure on the lending rates.

The banking sector has remained stable and resilient with strong liquidity and capital adequacy ratios despite the global and local economic challenges. Going forward, the banking sector is projected to remain resilient and stable. However, credit risk and Interest rate risk is expected to remain elevated in the short to medium term.

The Kenyan economy recorded a strong performance across most sectors in 2022. The growth was mainly attributed to the opening up of the economy which saw the rebound of sectors mainly the tourism and hospitality sector as well as expansion of the services sector.

According to the KPMG Kenya Budget Analysis 2023, the country experienced a slower growth in the real GDP of 4.4 percent. This was as a result of both micro and macro economic shocks such as drought experienced in the country, Russia Ukraine war and the tightening of the global financial market conditions. Drought, combined with the rising fuel prices and the depreciation of the Kenyan shilling against world major currencies contributed to rising food insecurity and increased cost of living. These challenges contributed to inflation of 7.7 percent in 2022, up from 6.1 percent in 2021.

Kenya

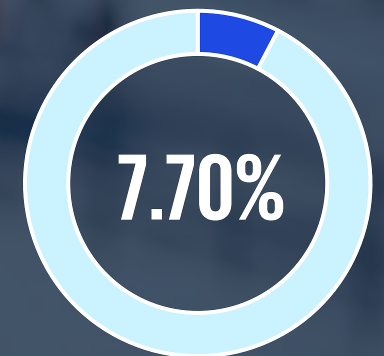
107,986

GDP (million US$)

CREDIT RATINGS

S&P	MOODY'S	FITCH
B-	B3	B

INFLATION RATE



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03

Key insights

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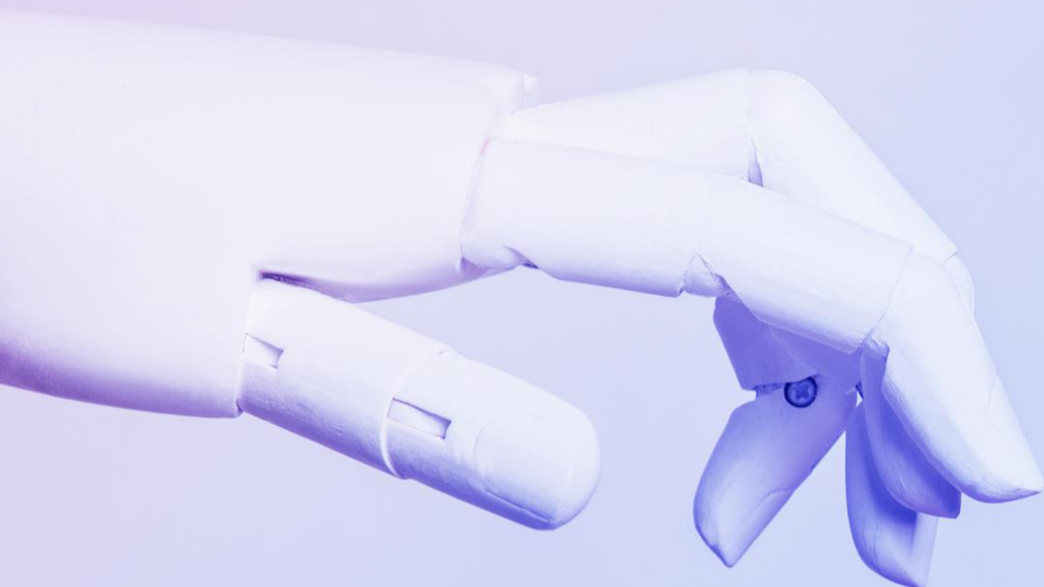

Digital transformation

Understanding the micro-economic needs of the banks is an important aspect to achieving an all-round digital transformation agenda. Digital transformation for banks influences its market perception, revenue, operational efficiency, and overall market share. There's a great need for banks in East Africa to accelerate their digital transformation journey with a strong focus on the customer and striving to offer a delightful experience to the customer.

We observe that most listed commercial banks do not have a structured approach to digital transformation, with majority of the listed banks in the East African market, having taken a modular approach to digital transformation based on the immediate need of the bank. Banks need to maintain a high level of flexibility and agility in adjusting their legacy business and operating models to meet the ever-dynamic needs of today's world.

With the rise of FinTech getting into the East Africa market to offer competing products with the banks, it is imperative for banks to find collaboration avenues to co-create and compete favourably for the same customer. Banks need to invest in having highly skilled frontline staff, equipped with timely data, insight, and customer knowledge to effectively support their customers' needs.

For a bank to understand its digital maturity, it is prudent for the bank to undertake an overall digital maturity assessment and create a structured approach towards their digital transformation journey.

Martin Kimani
Associate Director
E: mkimani@kpmg.co.ke

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Tech-forward means people-powered

Your digital future is powered by your people. We can help you connect your talent to technology in dynamic new ways, so you can accelerate adoption while igniting growth across your business.

Credit quality & sovereign risk

The economies of the East African region have largely remained resilient post the pandemic despite the uncertain global economic outlook and concerns about the stability of the global financial sector. Banks continue to closely monitor factors such as heightened inflation, exchange rate fluctuations, political stability, and regulatory policies and assess their impact on the credit quality of their portfolio.

The relief measures granted by regulators during the pandemic assisted banks to stabilize the credit quality of their portfolios and catalysed the strong credit growth recorded in 2022. Banks have continued to make adequate provisions largely driven by the rigorous approach & requirements of the IFRS 9 standard which has been in effect since 2018. Whilst the standard has led to increased provisioning requirements and posed challenges in data management, it has also enhanced credit risk management practices, improved financial transparency, and helped set the stage for adoption of internal ratings based (IRB) approaches soon.

With the increasing investments in data and analytics capabilities, banks in the region should seek to implement credit decisioning and early warning systems. These systems will help streamline the credit evaluation and management process, further improve credit quality, and contribute to the overall growth and stability of the banking sector in East Africa.

Sovereign risk remains a critical consideration in the region as the sovereign rating reflects the perceived credit risk of the country and by extension the market participants. While progress has been made in enhancing stability and creditworthiness in the region coupled with ongoing efforts in maintaining political stability, ratings downgrade ultimately lead to erosion of investor confidence. Banks with robust risk management frameworks, diversified portfolios, and proactive measures to address challenges posed by sovereign risk are better positioned to mitigate the impact and better navigate this ever-changing economic landscape.

Steve Yegon
Senior Manager
E: syegon@kpmg.co.ke

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Cyber security

The banking sector stands at the crossroads of innovation and vulnerability, as it navigates through the digital landscape. Recent cybersecurity audits have revealed some key issues that demand immediate attention

Foremost among these is the continued use of outdated software and services. Reliance on legacy systems that have been in place for many years continues to present a challenge. While these systems may have been cutting-edge at their inception, they have now become obsolete and easy targets for cyber-attacks. The risks associated with using out-of-date software are exacerbated by the lack of timely in application of critical security patches. When systems are not patched in a timely manner, it leaves them exposed to known vulnerabilities, which can be exploited by malicious entities.

Weaknesses in privileged administrative user access control have been a recurring concern. With elevated permissions, these accounts can be exploited to gain unauthorized access to sensitive data and systems. There is a need for robust policies and controls to mitigate risks associated with privileged access.

Finally, the human factor cannot be ignored. User awareness, or the lack thereof, plays a crucial role in cybersecurity. A workforce that is not educated on the best practices and the importance of cybersecurity can inadvertently become the weakest link.

It is important for the banking sector to take these findings not just as mere observations but as a call for action. Banks must adopt a proactive approach in updating software, ensuring timely patching, enforcing stringent access controls, and investing in continuous user awareness programs. Through these concerted efforts, the banking sector can strengthen its defences and safeguard the trust of its customers.

Moses Kipchirchir
Associate Director
E: mkipchirchir@kpmg.co.ke

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Cost optimization for banks

Cost to income ratio result in this survey reveal that the ratio has marginally reduced by 5.63% compared to last financial year. Multinational banks have managed their cost base better than local banks or those operating within the Eastern Africa region. This may be because of the various international cost transformation initiatives at their headquarters. However, it is important to note that the strengthening of the dollar against the various East African currencies has resulted in increased cost especially on the dollar denominated supplier payments. Keeping the ratio lower to an acceptable low will continue to remain an uphill task for banks even at a global scale.

East African banks will need to come up with various strategies to remain more efficient to improve their cost to income ratios, improve return on assets which has marginal improved and maximise shareholders return on equity that is at the verge of being eroded.

Banks can secure up to 35% cost reduction without a major strategy refresh by:

- Reducing presence in low performing customer segments and product areas.
- Reducing the cost of funding by optimising the balance sheet.
- Reducing organisational complexity, including management and governance layers.
- Creating a core organisational capability around transformation.
- Driving a cost focus through strategy and accountability.
- Digitising work from front to back office and drive enterprise-wide automation.
- Digital shift with interventions to drive behavioural change.
- Driving the simplification of the organisational model throughout the bank, focus on spans and layers, realignment of pay and rewards.
- Accelerating the migration of critical environments to the cloud, decommissioning of obsolete applications and removal of data centres.
- Rationalising operations between head offices and regions, adjustment of seat to desk ratio to 2.5:1.
- Driving 3rd party spend down through challenge of integrated supply and demand.
- Optimising of tax and legal structures.

Bernard Amukah
Partner
E: bamukah@kpmg.co.ke

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Focus on ESG

Regulatory focus on ESG has been on the rise around the world requiring Banks to integrate ESG considerations into their business practices. The Stock exchanges and Central banks within the East Africa region have been at the fore in driving this change. The Central Bank of Kenya (CBK) and the Bank of Tanzania have within the last 18 months called on the banking sector players to pay close attention to climate-related risks as part of their comprehensive risk management processes. Similarly, the Nairobi Securities Exchange (NSE) and the Dar es Salaam Stock Exchange (DSE) in Tanzania have taken actions towards pushing for ESG reporting by the listed companies in accordance with the Global Reporting Initiative (GRI) Standards.

We note that most Banks have started on their ESG journey in one form or another. Some Banks have disclosed that they have set up an ESG committee to provide oversight while others have created a C-suite position to spearhead ESG. Most of the Banks are in the process of developing their net zero strategies and making strides towards their first set of climate related disclosures aligned to the Taskforce on Climate-related Financial Disclosures (TCFD) framework. While it is true that some Banks have been publishing their annual sustainability reports for several years, there is now a noted deliberate effort towards developing ESG strategies with an aim to mainstream ESG within the business.

Finally, the recent release of the IFRS Sustainability Disclosures by the International Sustainability Standards Board (ISSB) signals a fundamental breakthrough for global ESG reporting. With an effective date of January 2024, more activity towards ESG reporting is expected across all sectors, with an initial focus on climate.

Sarah Njoroge
Senior Manager
E: snjoroge@kpmg.co.ke

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Making every step sustainable

We can help you embed ESG across
your organization, starting with a robust governance model. Which means you can drive growth as you move your business forward. Because how you grow matters.

KPI definitions and assumptions

The following parameters have been used in calculations for consistency in our analysis:

- **Total assets** are as reported in the published annual financial statements
- **Net profit** is the net profit for the year attributable to the shareholders of the banks
- **Capital adequacy ratio (CAR)** is the ratio of total capital (the sum of Tier 1 and 2 capital) to total risk weighted assets (RWAs).
- **Return on equity (ROE)** is the ratio of net profit attributable to the shareholders of the banks to average equity, where average equity is calculated by halving the sum of total equity attributable to the banks' shareholders for the current and previous year ends.
- **Return on asset (ROA)** is the ratio of net profit attributable to the shareholders of the banks to average assets, where average assets are calculated by halving the sum of total assets for the current and previous year ends.
- **Cost-to-income ratio (CIR)** is the ratio of total operating expenses (excluding impairment charges) to total operating income.
- **Dividend payout ratio (DPR)** is the ratio of Total dividends to Net profit.
- **Net interest margin (NIM)** is the ratio of net interest income (Net of interest income and expenses) to the average earning assets.
- **Loan to Deposit Ratio** is the ratio of total loans advanced to customers to total customer deposits.
- **Non performing Loans (NPL) ratio** is the ratio of the banks' non-performing loans to the total gross loans.

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In this report , we have analysed the financial results of all listed commercial banks in the country . The financial results and selected Key Performance Indicators (KPIs) for the year ended 31 December 2022 are summarised and compared with the prior year (year ended 31 December 2021).

We have also compiled our insights and predictions on some of the emerging trends in the sector.

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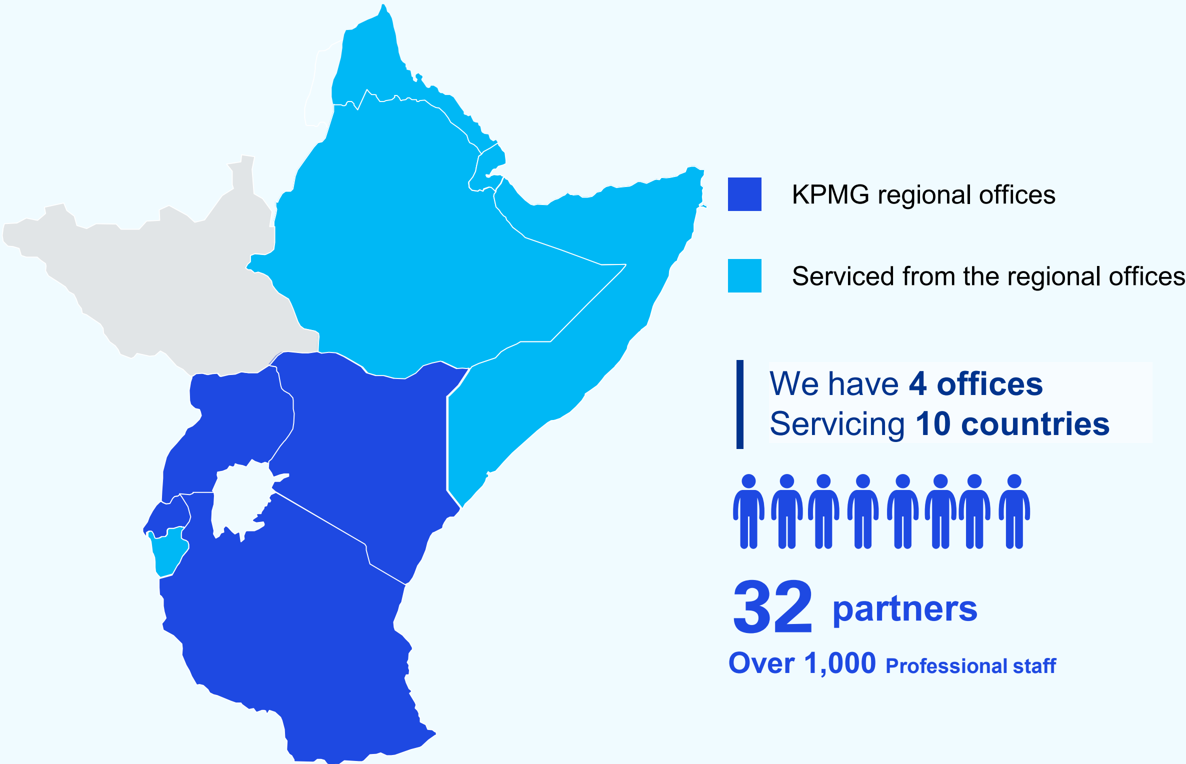
East Africa

Our East Africa practice comprises of Kenya, Uganda, Tanzania and Rwanda and additionally provides services to Eastern Democratic Republic of Congo, South Sudan, Burundi, Somalia, Ethiopia as well as Eritrea.

KPMG East Africa has 32 partners and over 1000 professional staff. The Nairobi office serves as the regional coordinating office providing the required networking and support to facilitate delivery of services on a timely basis to meet and exceed our clients' expectation.



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Contributors

Joseph Kariuki
Partner
Head of Banking Sector
E: jkariuki@kpmg.co.ke

Bernard Amukah
Partner
Governance
Risk and Compliance
E: bamukah@kpmg.co.ke

Martin Kimani
Associate Director
Technology Transformation
E: mkimani@kpmg.co.ke

Moses Kipchirchir
Associate Director
Technology Assurance
E: mkipchirchir@kpmg.co.ke

Johnson Nyika
Senior Manager
Audit
E: jnyika@kpmg.co.ke

Sarah Njoroge
Senior Manager
Governance, Risk
and Compliance
E: snjoroge@kpmg.co.ke

Steve Yegon
Senior Manager
Governance, Risk
and Compliance
E: syegon@kpmg.co.ke

Other contributors : **Catherine Mutuma, Denis Mwenda** and **Mathew Kamande**

kpmg.com/socialmedia

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