H12026 Banking Sector Analysis

H12026 Kenyan Banking Sector Analysis: Resilient Earnings Amid a Shift Toward Credit, Efficiency & Diversification-Led Growth

Kenya's banking sector delivered a solid H1 2026 performance, supported by improving macroeconomic conditions, improving private-sector credit growth and resilient balance sheets. Earnings remained robust as banks benefited from lower funding costs, disciplined cost management and continued diversification into non-funded income and geographically. The period also saw important structural developments, including the listing of Family Bank and progress towards Nedbank's proposed acquisition of a 66% stake in NCBA.

Banking sector recorded **PBT growth of 16%**, with earnings increasingly supported by loan growth, resilient margins, improved operating efficiency and stronger non-funded income. Balance-sheet expansion also remained healthy, with industry assets, deposits and gross loans growing by **13%, 14% and 12%**, respectively, pointing to a continued recovery in financial intermediation. Asset quality improved with Gross NPLs declining by 6% to KES 688.2Bn in H126.

The sector is, however, entering a new phase of growth. As yields on investment securities moderate, banks are increasingly shifting towards credit-led growth and revenue diversification. The ability to expand loan books while maintaining asset quality, improve cost efficiency and scale fee-generating businesses will increasingly determine earnings resilience across institutions. This is already creating greater performance dispersion, with banks combining strong credit underwriting, diversified revenue streams and efficient operating models better positioned to sustain returns.

Looking ahead, the operating environment is likely to become more demanding, shaped by:

- Greater reliance on loan growth, NFI expansion and operating efficiency
- Persistent asset-quality risks as credit deployment accelerates
- Sensitivity to geopolitical developments, energy prices and inflation

The increase in the minimum core capital requirement to KES 10Bn by 2032 will add another layer of structural change, encouraging capital raising, consolidation and strategic partnerships across the industry. This is likely to reshape the competitive landscape, particularly for smaller institutions that may face increasing pressure to strengthen their capital bases.

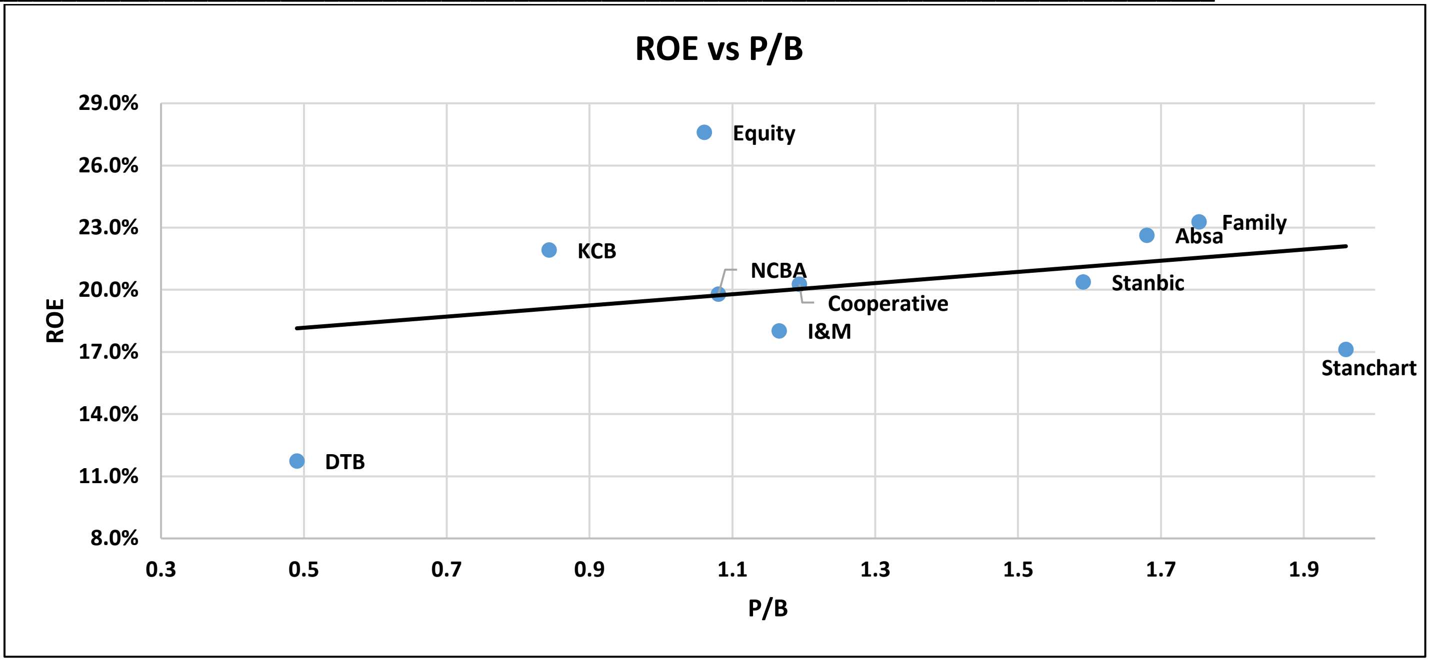
Overall, while some of the cyclical tailwinds that supported the sector's recent re-rating are moderating, the underlying banking story remains resilient. We expect the next phase of sector performance to be driven less by falling funding costs and expanding securities yields, and more by quality loan growth, NFI diversification, regional expansion, cost efficiency and disciplined risk management. Well-capitalized and diversified banks with strong asset quality should be better positioned to sustain profitability as the sector moves into a more normalized and competitive operating environment.

1) Investment Thesis & Sector View

Resilient sector with reasonable valuations

The Kenyan banking sector remains constructive but increasingly selective. While the broad rerating phase has largely played out, opportunities persist in fundamentally sound counters trading at reasonable valuations with clear earnings catalysts.

Valuation opportunities still exist in the banking sector and thus can be best assessed through the relationship between P/B and ROaE, which highlights how efficiently the market prices profitability. Using the trendline as a benchmark, the banks are classified into distinct valuation quadrants:



Source: Comp Fin, KCB IB

Equity and KCB Group emerge as the most compelling investment opportunities, combining industry-leading profitability with relatively modest valuation multiples. Their positions above the valuation trend line suggest that the market has yet to fully reflect their earnings quality and growth potential.

Meanwhile, NCBA Group, Stanbic Bank, I&M & Co-operative Bank trade close to the trend line, indicating that their current valuations are broadly aligned with their profitability and implying balanced risk-return profiles.

Conversely, **Standard Chartered Kenya** trades at the highest P/B multiple despite generating comparatively lower returns on equity, suggesting that its valuation premium may constrain further upside. **DTB** remains the cheapest bank on a P/B basis but also posts the lowest ROaE, limiting its near-term appeal unless profitability improves materially.

Classification:

- **STARS (Profitability not fully priced)**: Attractive opportunities, combining high ROaE with relatively low P/B ratios suggesting strong profitability that is not fully priced in. They give the highest return per unit of assets. (KCB Group, Equity Group).

- **DIAMONDS (Premium Quality):** Delivers strong profitability (High ROaE) supported by a premium valuation. While its high ROE justifies the premium, much of earnings strength appears to be reflected in the current share price, suggesting limited scope for further valuation re-rating. (Absa Kenya, Family Bank).

- **PYRAMIDS (Fairly Valued)**: These banks trade close to the valuation trend line, indicating that their market valuations broadly reflect their profitability. Future upside is therefore likely to be driven by earnings growth rather than multiple expansion (NCBA, Stanbic, Coop, I&M).

- **CROSSES (Premium Valuation):** The bank trades at a significant premium relative to its profitability, suggesting that much of its earnings outlook is already priced in. Unless profitability improves materially, further upside may be limited (Stanchart).

- **YANKEES (Deep undervaluation)**: These are characterized by low P/B ratios and weak ROaE, indicating underperformance and limited attractiveness from a valuation and returns perspective. (DTB)

Valuation Overview & Market Positioning

Stock	18th Sept 2026	52-week low	52-week high	EPS	P/B	P/E	BVPS	ROE	Trailing Div	Dividend Yield	Recommendation
Cooperative	34.80	13.80	39.95	5.04	1.19x	6.90x	29.15	**20.27%**	2.50	7.18%	**BUY**
Equity	98.50	41.20	109.00	19.07	1.06x	5.17x	92.84	**27.60%**	5.75	5.84%	**BUY**
KCB	87.00	35.00	101.00	20.80	0.78x	4.18x	111.08	**21.92%**	7.00	8.05%	**Neutral**
I&M	80.00	29.50	82.50	34.70	1.17x	7.41x	68.62	**18.02%**	3.75	4.69%	**HOLD**
Stanbic	278.00	147.00	300.00	11.18	1.59x	8.01x	174.70	**20.38%**	22.35	8.04%	**HOLD**
NCBA	86.25	48.00	100.00	14.20	1.08x	6.07x	79.82	**19.79%**	7.10	8.23%	**BUY**
Stanchart	330.75	260.00	370.00	32.47	1.96x	10.67x	168.83	**17.12%**	31.00	9.37%	**ACCUMULATE**
Absa	31.10	15.00	36.50	4.22	1.68x	7.37x	18.51	**22.63%**	2.05	6.59%	**HOLD**
DTB	179.50	66.00	198.50	33.65	0.49x	5.33x	366.18	**10.43%**	9.00	5.01%	**BUY**

Source: NSE, KCB IB

**Cut off date for prices as of 18th September*

The sector exhibits pockets of selective opportunities, with certain counters delivering solid profitability and consistent dividend payouts, while others appear more fairly valued.

- **Profitability & Shareholder Returns:** Profitability remains robust across the sector, with Equity, Absa & KCB leading in ROaE, while Co-operative & NCBA continue to deliver strong returns.
- Dividend yields remain attractive (5%–10%), with Standard Chartered, NCBA and Stanbic standing out as top income plays, underscoring strong cash generation.

Investment Positioning & Recommendations

- **BUY** – Equity, Cooperative, NCBA: Strong returns, low valuation, and clear upside.
- **Speculative Buy-** DTB: Deep value given low P/B, but weaker ROaE tempers conviction.
- **ACCUMULATE** – Stanchart: Higher valuations but strong income appeal.
- **HOLD** – Stanbic, I&M, Absa: Fairly valued with limited upside.

Sector Outlook & Investment View: The sector presents a valuation disconnect, with strong fundamentals not fully reflected in pricing. However, performance will be shaped by a pause in monetary easing, compressed loan yields, and lingering asset quality risks. Going forward, returns will be driven by credit growth, efficiency, and risk management.

The Kenyan banking sector remains profitable and reasonably valued. Banks with strong returns, discounted valuations, and scalable models, such as Equity, KCB, and Co-operative, are best positioned to deliver sustainable long-term returns.

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Listed Banks Dividend History

Bank	2021	2022	2023	2024	2025	Div Payout Ratio	Div Cover	2026 Interim Div
ABSA Bank	1.10	1.35	1.55	1.75	2.05	49%	2.06	0.50
Co-operative Bank	1.00	1.50	1.50	1.50	2.50	50%	2.02	Nil
DTB Kenya	3.00	5.00	6.00	7.00	9.00	27%	3.74	Nil
Equity Group	3.00	4.00	4.00	4.25	5.75	30%	3.32	Nil
I&M Group	1.50	2.25	2.55	3.00	3.75	35%	2.88	Nil
KCB	3.00	2.00	Nil	3.00	7.00	34%	2.97	3.00
Stanbic	9.00	12.60	15.35	20.74	22.35	64%	1.55	1.64
Standard Chartered	19.00	22.00	29.00	45.00	31.00	95%	1.05	8.50
NCBA	3.00	4.25	4.75	5.50	7.10	50%	2.00	3.75

Source: Financials, KCB IB

- Kenyan banks have maintained an upward dividend trajectory, with most banks increasing DPS over the past five years.
- Stanbic and Standard Chartered lead in absolute dividends, while KCB, NCBA and I&M have also shown consistent growth.
- Payout ratios range from 27%–95%, highlighting differing distribution policies and dividend sustainability.

H12026 Listed Banks Performance Snapshot

H12026	KCB	Equity	Co-op	NCBA	I&M	DTB	Stanbic	SCB	Absa	Family	HFCB
PAT Growth	14.5%	31.5%	28.0%	12.2%	22.4%	35.8%	1.3%	(16.8%)	(9.8%)	61.8%	59.8%
NII Growth	7.0%	16.8%	13.0%	20.4%	22.5%	26.4%	5.5%	(19.8%)	(5.4%)	40.7%	29.4%
NFI Growth	15.4%	35.9%	11.6%	7.6%	24.5%	6.6%	(9.0%)	15.9%	(10.2%)	(14.2%)	37.4%
Operating Income	9.5%	24.6%	12.5%	15.1%	23.0%	20.9%	1.6%	(8.8%)	(6.8%)	22.1%	31.7%
Loan Growth	13.3%	18.9%	18.1%	20.1%	15.0%	13.7%	24.7%	11.1%	8.2%	12.6%	11.5%
Deposit Growth	15.1%	21.4%	13.4%	11.0%	17.7%	10.6%	23.0%	6.4%	5.4%	27.1%	29.7%
NIM	8.4%	7.8%	9.2%	7.9%	8.8%	7.4%	8.4%	10.3%	9.5%	9.5%	7.0%
ROE	21.4%	27.6%	20.3%	19.8%	18.0%	11.7%	20.4%	17.1%	22.6%	23.3%	10.3%
Profit Margin	34.1%	36.5%	35.8%	30.5%	30.2%	27.5%	33.5%	33.4%	35.9%	30.6%	26.2%
NPL Ratio	14.5%	10.2%	14.2%	10.8%	8.4%	12.2%	7.3%	5.1%	10.2%	14.7%	21.4%
NPL Coverage	78.8%	71.6%	68.9%	67.4%	74.8%	58.2%	86.6%	84.3%	69.1%	66.2%	80.5%
Cost-to-Income	44.4%	48.6%	46.0%	47.9%	44.4%	46.0%	48.5%	49.9%	41.2%	53.1%	60.6%
Cost of Risk	0.8%	0.6%	0.7%	1.4%	1.6%	1.3%	0.3%	0.3%	0.9%	0.8%	0.6%

Source: Financials, KCB IB

- Kenyan listed banks delivered strong earnings in H1 2026, supported by accelerating credit growth, resilient net interest income and improved non-funded income.
- Loan growth accelerated by an average of 15.2%, while PAT increased by an average of 21.9%.
- Asset quality also improved, with the NPL ratio average declining to 11.7%, alongside stronger NPL coverage.

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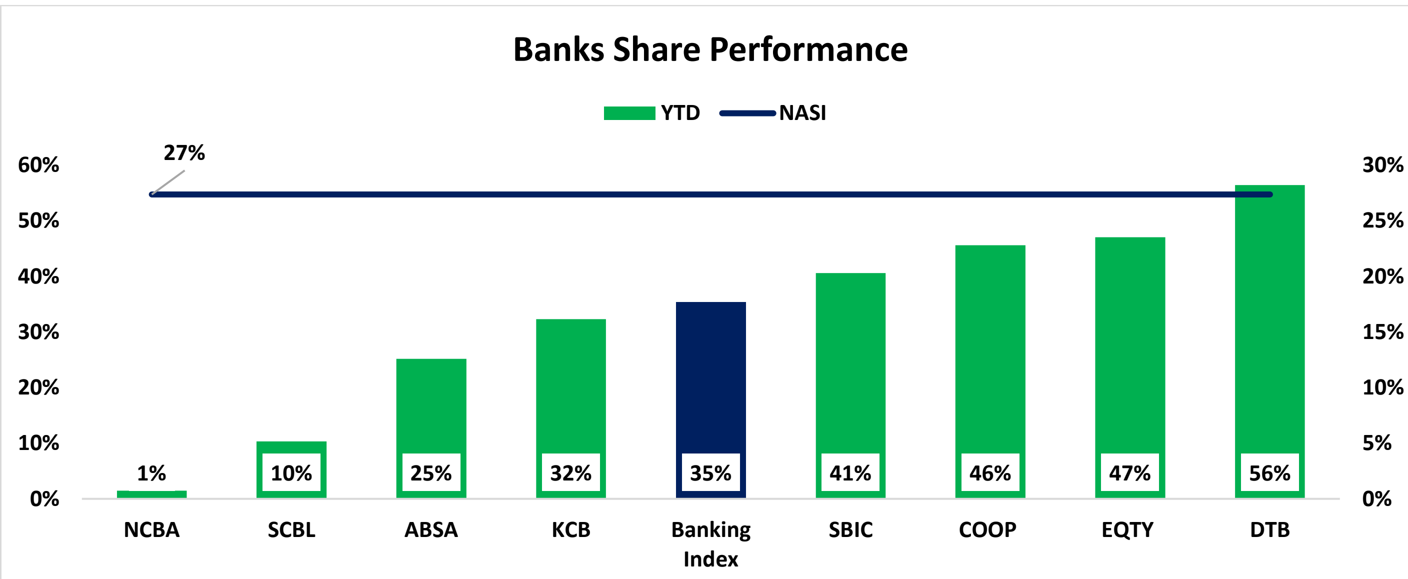
Market Performance & Sentiment: Rally sustained by positive earnings amidst volatility

The Nairobi Securities Exchange (NSE) delivered a strong first half, with NASI rising by 20% by June and 27% YTD, lifting market capitalization to KES 3.76Tn. The rally, which carried over from late 2025, was supported by robust corporate earnings and stable macroeconomic conditions.

The NSE Banking Sector Index outperformed, gaining 25% by June and 35% YTD, driven by strong H1 2026 earnings, balance-sheet expansion, lower funding costs, resilient margins and improving asset quality. Momentum was further supported by local absorption of foreign exits and structural developments, including approval of the WSA Banking Sector Index ETF and the listing of Family Bank.

However, the rally moderated amid geopolitical risks, shifting rate expectations and profit-taking. Despite these headwinds, strong banking fundamentals have kept the sector at the forefront of the market's performance heading into H2 2026.



Source: NSE, KCB IB

2) Macro & Operating Environment Context: Supportive but increasingly complex backdrop

H12026 featured a high volume of moving parts. Key operational positives included stable currency and a welcome expansion in private sector credit growth. However, macro performance remained heavily exposed to external geopolitical shocks, particularly ongoing Middle East tensions, which slowed overall domestic expansion, leaving GDP growth projections modest at around 5.0%.

Concurrently, a resurgence in inflation during the second quarter triggered a hawkish hold. The CBK paused its monetary easing cycle, holding the CBR at 8.75%. While lending rates initially eased in H1, their future path remains highly dependent on central bank action. Emerging external vulnerabilities and the halt in policy easing point toward a far more nuanced and defensive operating landscape for the remainder of 2026.

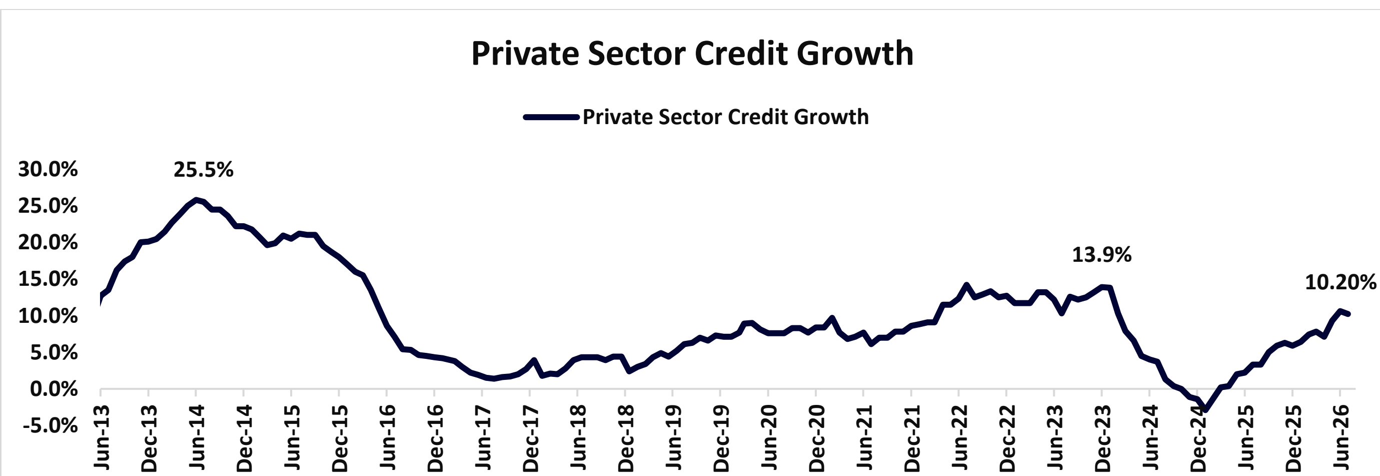
- **Currency Stability**: KES remained stable in H12026, trading within a range of 129-133 against the US Dollar. This stability was underpinned by a proactive reserve accumulation by CBK and strong remittance inflows. YTD, the currency remained broadly flat, depreciating by a marginal 0.4%, signaling sustained short-term stability. We expect the exchange rate to hover around these current levels for the remainder of the year.

Implication: Reduced FX volatility has reduced currency translation gains and FX spreads, reinforcing a necessary return to core banking income, mainly interest income and fee-based transactions. However, underlying pressures remain. Elevated external public debt servicing, a widening current account deficit, and high sensitivity to global commodity prices leave the currency exposed to unexpected depreciation shocks, particularly if geopolitical friction drags on.

- **Inflation Control:** Headline inflation averaged 5.6% YTD before and edged upward to 6.6% in August 2026 from July 2026. While this keeps inflation within the CBK's statutory target band of 2.5%–7.5%, it sits uncomfortably above the regulator's preferred 5.0% midpoint. Price pressures have been primarily driven by supply-side shocks rather than domestic demand, specifically a 15.7% surge in transport inflation fueled by rising global oil prices and localized agricultural supply constraints.

  Implication: With inflation sitting above the preferred midpoint, the CBK is likely to anchor interest rates at the current levels for longer to curb second-round inflationary effects. For commercial banks, this means decline in funding costs enjoyed during the early part of the easing cycle will moderate in H2'2026. Net interest margins (NIMs) could face compression if liability repricing hits a floor while asset repricing lags.

- **Credit Growth**: Credit to the private sector experienced a robust rebound, climbing to 10.2% by mid-year. This recovery was unlocked by healthier market liquidity, a trailing decline in commercial lending rates (which fell to an average of 14.4% by July), and a gradual recovery in consumer demand. Sector asset quality showed signs of structural repair, with the industry NPL ratio tapering down to 14.6% offering banks the breathing room needed for cautious portfolio expansion.



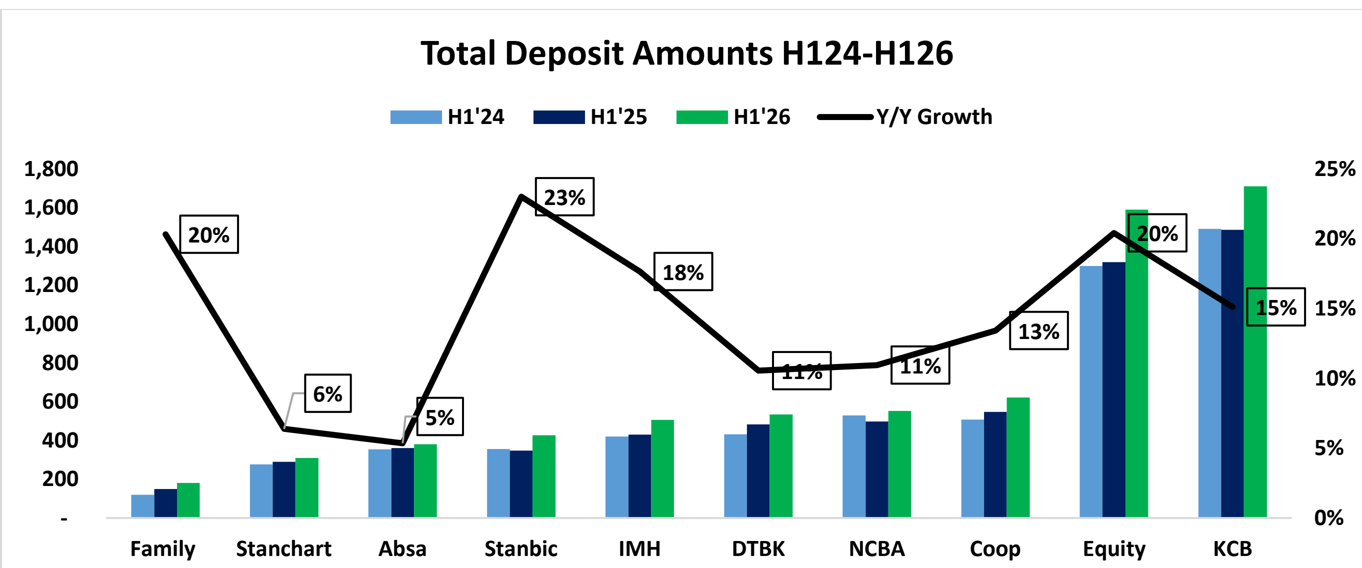
Source: NSE, KCB IB

- **Implication:** Going forward, we anticipate a measured acceleration in credit uptake. This will be led by tier-1 banks deploying advanced risk-based lending models to safely price risk. However, credit expansion will remain highly defensive. Global hawkishness, volatile fuel costs, and a projected El Niño weather patterns later in the year threaten to re-ignite domestic inflation pressures. Should these risks force the CBK to pivot back toward rate hikes, higher borrowing costs will abruptly slow down the private sector's credit rebound and potentially trigger a reversal in recent NPL improvements.

3) Balance Sheet Strength: Solid expansion anchored on strong deposit growth, prudent lending, and ample liquidity buffers.

The Kenyan banking sector remains anchored by dominant players, highlighting strong market concentration and scale advantages.

- **Sustained asset growth driven by scale and improving credit demand:** The banking sector's asset base expanded by 13% y/y to **KES 8.9Tr,** supported by resilient deposit mobilization and a gradual recovery in lending activity. KCB Group maintained its lead with assets growing 17% to KES 2.3Tr, while Equity Group followed closely at KES 2.2Tr, reinforcing the dominance of tier-one banks and the benefits of scale in driving growth.
- **In Sector Trends**, **Liquidity build-up outpaces lending as banks remain cautious:** Gross loans increased by 12% y/y to KES 4.6Tr, reflecting improving lending for most of the year, while customer deposits grew by a faster 14% y/y to KES 6.7Tr, underscoring sustained liquidity build-up across the sector.
- **Strong deposit mobilization supports low-cost funding strategy**: Deposit mobilization remained resilient across our coverage, with nearly all banks recording positive growth. HFCB led the pack with a 30% expansion, while KCB Group and Equity Group continued to dominate in absolute terms, with deposits standing at KES 1.7Tr (Up 15% y/y) and KES 1.6Tr (Up 20% y/y), respectively.



Source: NSE, KCB IB

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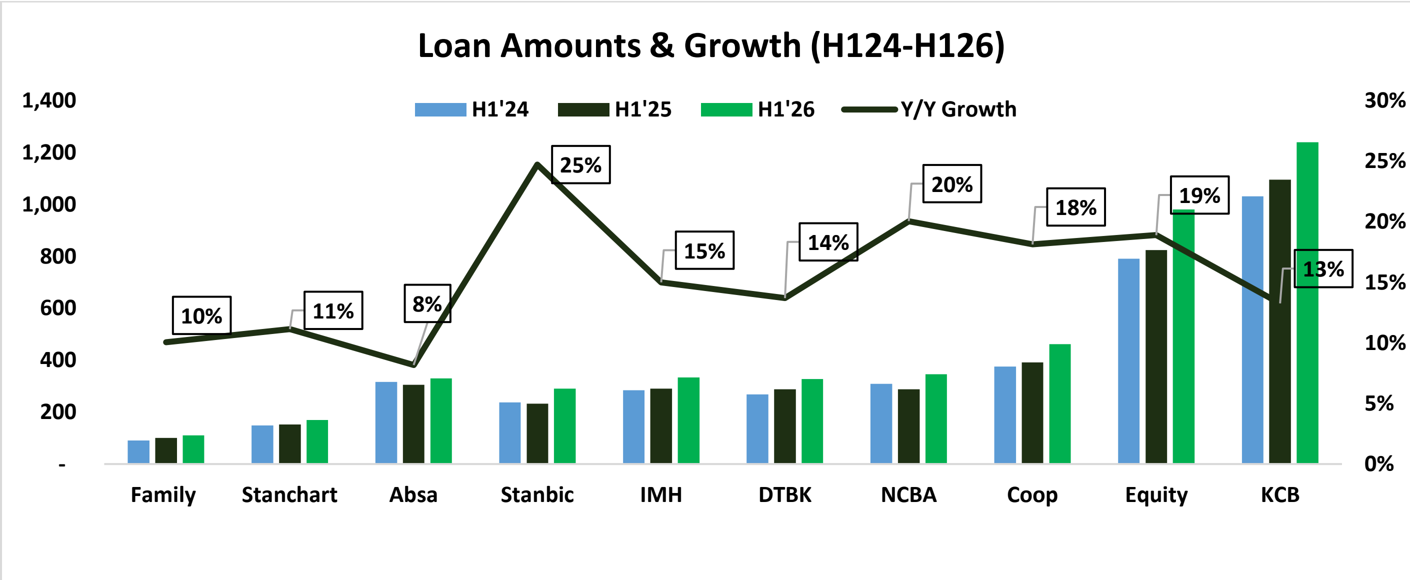
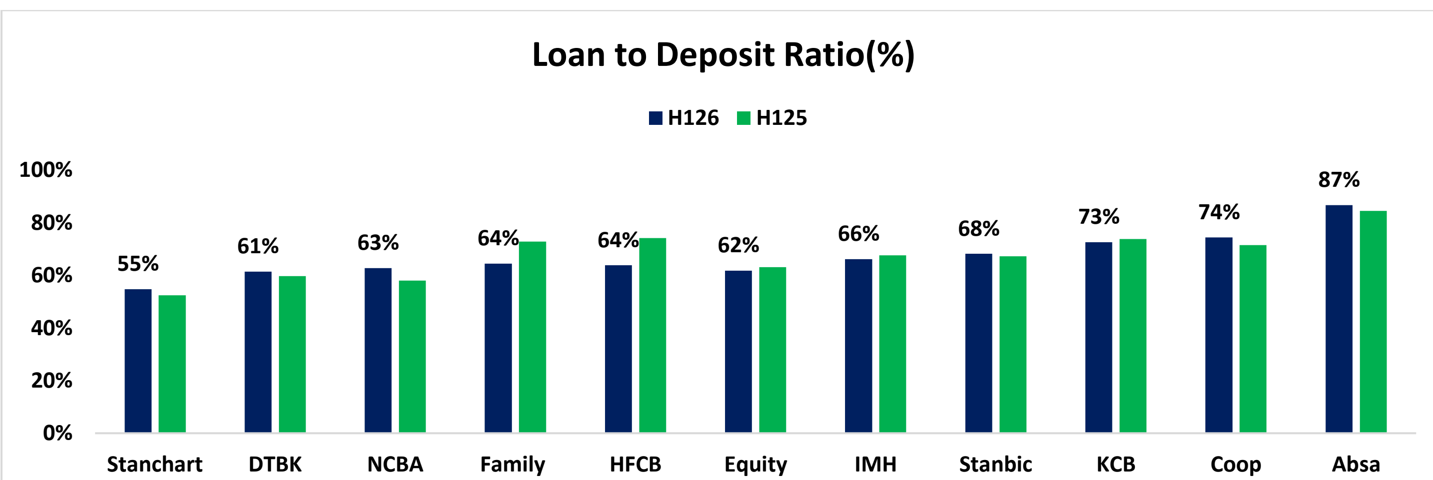


Source: NSE, KCB IB

- **Gradual recovery in lending as credit demand picks up:** Loan growth across listed banks under coverage averaged 15% y/y, outpacing the broader sector's average of 12%. This signals a continuing recovery in private sector credit demand following interest rate easing. While KCB Group and Equity Group remained the largest lenders in absolute terms, supported by their massive scale and regional diversification, peer growth was broad-based. Stanbic (Up 25% y/y) and NCBA (Up 20% y/y) significantly outperformed the market, signaling a more proactive shift toward credit expansion, while Absa and Standard Chartered reported the trailing growth rates within the coverage universe.

- **Loan-Deposit reflects balanced liquidity positions supporting sustainable credit growth:** Loan-Deposit Ratios remained broadly stable across the sector, reflecting prudent liquidity management. Absa and Cooperative maintained relatively higher LDRs.



Source: Comp Fin, KCB IB

- **Capital & Liquidity Positioning: Strong buffers and ample liquidity underpin sector resilience**

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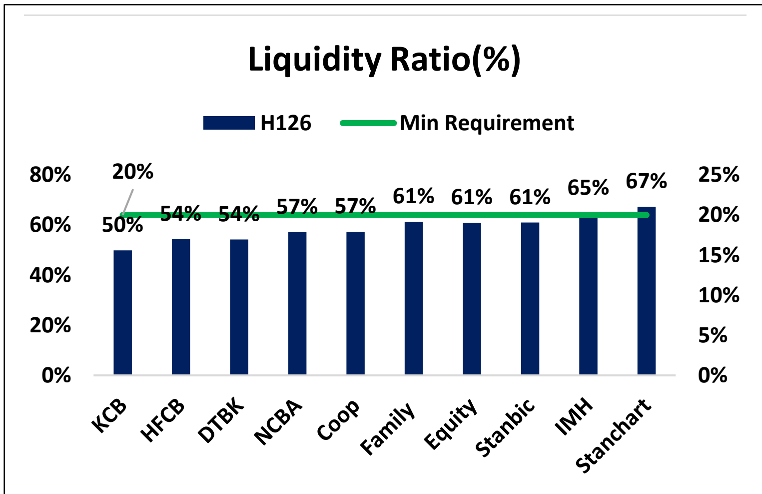
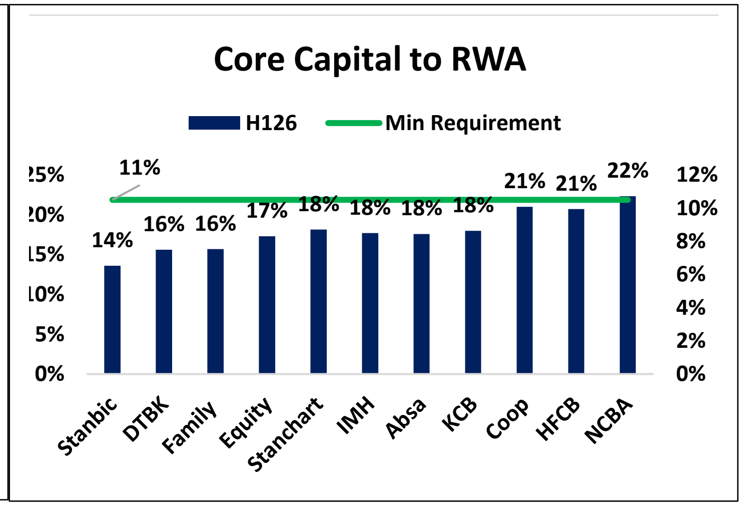
All banks under coverage maintain robust capital positions, comfortably exceeding the statutory minimum. This provides strong solvency cushions to absorb lingering credit risks. Liquidity remains an undeniable sector fortress, with the average liquidity ratio standing at 61.2%, more than three times the 20.0% regulatory minimum requirement.

However, the deployable context is changing. With the CBK introducing its public-comment framework for Domestic Systemically Important Banks (D-SIBs), Tier-1 lenders face impending requirements for additional Common Equity Tier 1 (CET1) capital surcharges of 0.5% to 2.5%. This makes preserving high-quality liquid assets and strong baseline capital a strategic necessity rather than just a compliance checkbox, balancing strong stability with the efficiency required to pivot into risk assets.





Source: Comp Fin, KCB IB

Balance sheet Outlook:

Accelerating credit deployment as rates ease: With yields on investment securities moderating, the banking sector is increasingly shifting towards credit-led growth to sustain earnings and support returns. Loan-book expansion is becoming a more important earnings driver. Industry data reflects this transition, with gross loans surpassing KES 4.6Tr in June, pointing to stronger private-sector credit growth.

However, asset quality remains a key constraint. While the industry's gross NPL ratio has gradually improved, elevated levels of bad debt continue to weigh on profitability through provisioning costs and sluggish recovery process. The remainder of 2026 is likely to highlight a growing divergence across banks, institutions able to scale digital and retail lending while maintaining disciplined underwriting should be better positioned to translate loan growth into sustainable earnings, while those facing weaker asset quality could see a larger portion of incremental income absorbed by provisions.

Ultimately, cost efficiency, disciplined credit underwriting and risk-adjusted pricing will remain critical to protecting margins and sustaining profitability.

4) Earnings & Profitability Analysis: Margin resilience and diversification anchor earnings

➢ Net Interest Income (NII): Lower funding costs cushion pressure on asset yields

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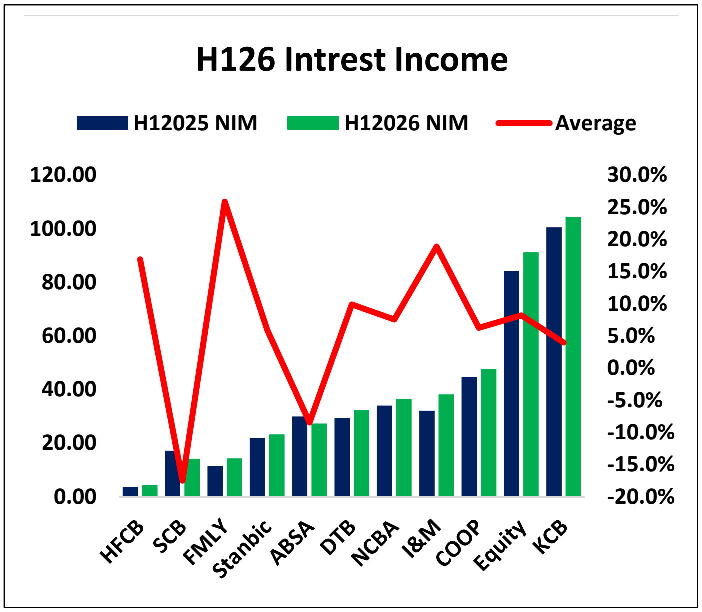
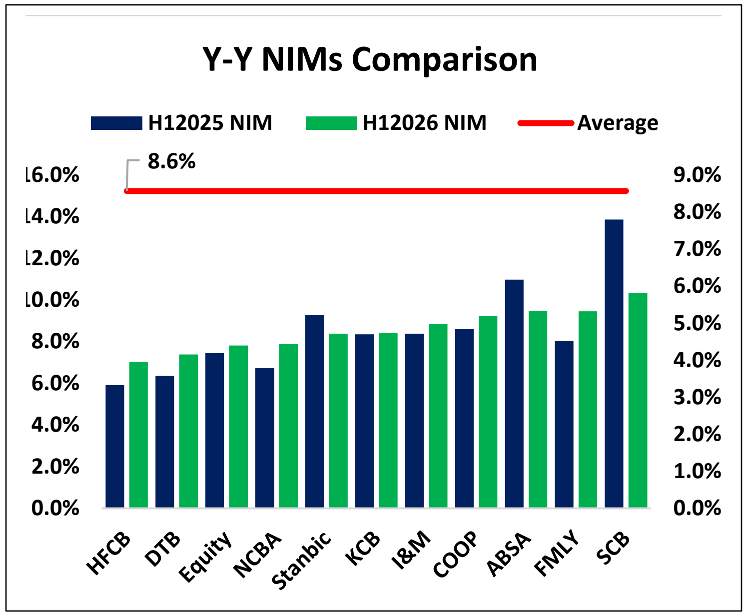
Net Interest Income (NII) remained resilient across covered banks with gross interest income rising 6.0% y/y, supported by a contraction in interest expenses that offset moderated asset yields. Net Interest Margins (NIMs) stayed broadly stable as proactive deposit repricing and liability management shielded lenders from the impact of an easing monetary cycle.

Only select banks such as Standard Chartered & Absa registered slowdown in gross interest income.





Source: Comp Fin, KCB IB

➢ **Non-Funded Income (NFI): Diversification supports earnings**

NFI remained a key earnings buffer, averagely contributing 29% among the listed banks in our coverage. Growth was supported by diversification into transaction-based income, bancassurance, and wealth management. Equity recorded notable gains in NFI, increasing by 35.9%. I&M and HFCB also recorded significant growth in the NFI implying growing diversification among the lenders. However, Stanbic lagged, mostly on the back of slowdown in other fees and commissions and other income. Absa also recorded a decline of 10% attributable to reduced FX trading income and other income.

➢ **Non-Funded Income Composition: Distinct revenue models drive earnings variability**

An analysis of **NFI** composition highlights stark variations in business models across the covered banking sector:

- **Retail & Digital Leaders:** NCBA and Cooperative Bank lead in credit-linked non-funded income, generating the highest proportion of revenue from Fees & commissions on loans. Meanwhile, Equity and KCB show a heavy reliance on other fees (transactional income), heavily supported by their extensive retail footprints and robust agency banking networks.
- **Corporate & Treasury Giants:** Stanbic, Stanchart, and Absa maintain a distinct corporate focus. Their NFI profiles feature substantial contributions from both other fees and FX trading income, underscoring their strengths in corporate transaction banking and foreign exchange market-making.

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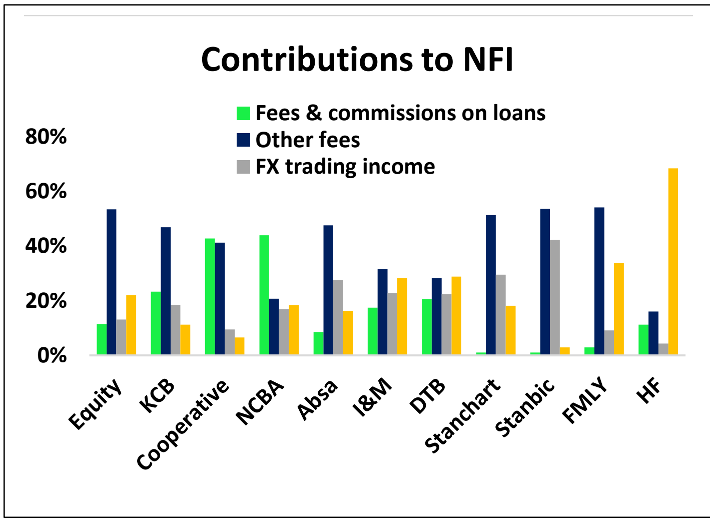
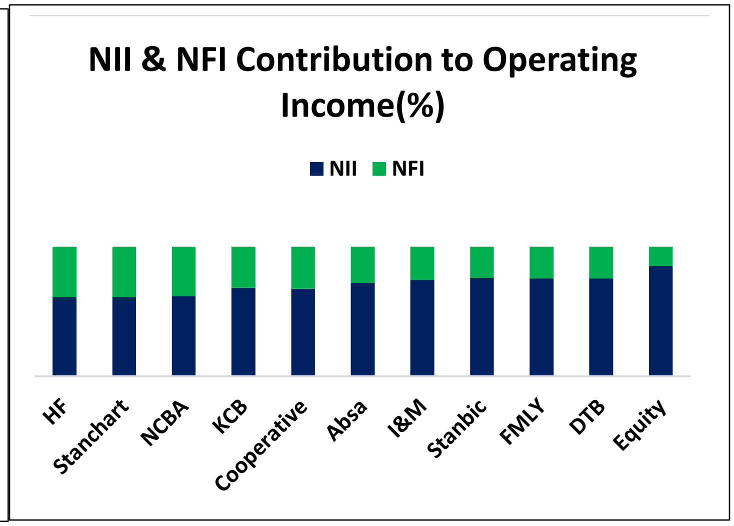
- **Diversified Players**: I&M and DTB exhibit a highly balanced revenue mix, spreading their earnings relatively evenly across loan fees, transactional fees, FX trading, and other income streams.

- **Niche & Alternative Structuring:** Family Bank is anchored predominantly by transactional other fees, whereas HFCB presents a highly unique profile dominated heavily by Other Income, reflecting alternative real estate-driven revenue structure. The performance reflects its ongoing corporate transformation out of a pure mortgage model into a Tier II commercial bank.



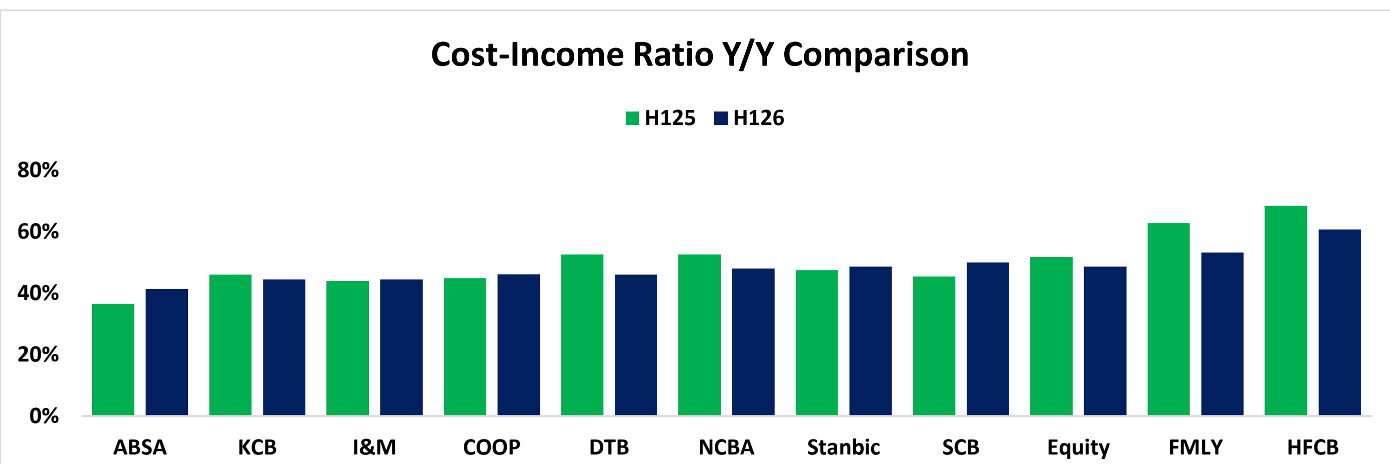


Source: Comp Fin, KCB IB

Despite lenders improving their diversification to non-funded income, lending remains the core anchor in the banking revenue. The sector remains largely funded-income driven, with NII contributing 61%–85% of operating income.

➢ **Efficiency: Cost discipline drives improved operational efficiency**

Efficiency improved across most banks, with reduced cost-to-income ratios reflecting better cost management. Family Bank, DTB and NCBA led in efficiency gains, while Absa and Standard Chartered recorded higher ratios with decline in revenue.



Source: Comp Fin, KCB IB

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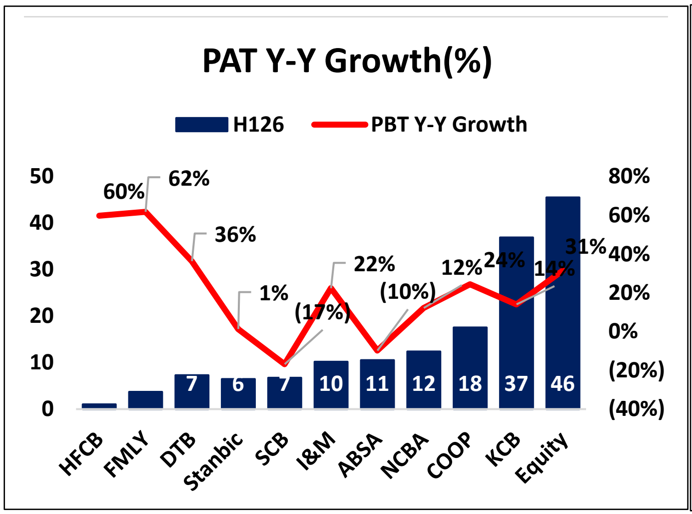
➢ **Profitability Trends: Earnings growth sustained**

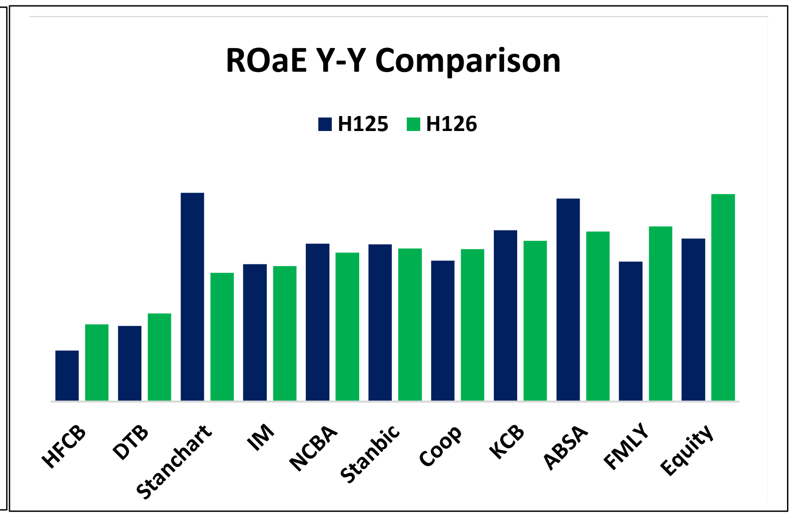
Profitability improved across most listed lenders in H1 2026, primarily supported by resilient Net Interest Income (NII) as falling funding costs outpaced asset yield compression. The performance was further boosted by private-sector credit acceleration, which hit a high of 10.6% in June. Growth in non-funded income also supported the increase in the bottom-line.

Tier 1 Leaders: Within the large-cap banking segment, performance was highly divergent. Equity Group, Co-operative, and Diamond Trust emerged as the clear outperformers, posting PAT growth well above 20%. KCB Group also registered solid expansion, growing its PAT by 14%. Conversely, Stanbic Holdings flattened out with near-zero growth.

Tier 2 Outliers: Listed small and mid-sized lenders showcased substantial upside volatility. Both HF Group and Family Bank recorded massive bottom-line expansion, with PAT surging by 60% and 62% Y/Y, respectively.

Underperformers: Standard Chartered Bank Kenya and **Absa Bank Kenya** experienced a visible contraction in earnings. This deterioration was primarily driven by margin compression on their funded portfolios.





Source: Comp Fin, KCB IB

ROaE Dynamic: Sector-wide return metrics held relatively steady, maintaining an ROaE of approximately 19%, tracking closely to 2025 levels. However, structural shifts are visible: Stanchart's and Absa's return profiles contracted due to compressed profitability, while Equity surged forward to reclaim the top industry position, printing an exceptional ROaE of 27% in H1 2026.

Strategic Outlook: Transition to volume-driven growth amid rising macro risks

Going into the second half of 2026, the sector's operating framework is becoming increasingly intricate. Headline inflation has rebounded to 6.6%, structurally forced upward by rising food and transport costs amidst geopolitical tensions. This consumer-level shock, paired with sticky global commodity prices linked to geopolitical tensions in the Middle East, has halted monetary easing cycle. As a result, banks will see a ceiling placed on further funding cost reduction benefits, sustaining immediate pressure on interest margins.

Nonetheless, the sector exhibits structural resilience. Future earnings expansion will transition from price-driven to volume-driven growth, heavily reliant on prudent loan book extensions into recovering private sectors. Incremental optimization will be carried by structural efficiency gains out of digital delivery transformations, alongside aggressive write-offs and recoveries targeting sticky legacy asset quality issues.

While NFI may struggle to find massive organic growth catalysts in the absence of historical foreign exchange volatility, underlying cross-border diversification and regional subsidiary matrices will offer critical defensive buffers to top-line performance. Diversification into other revenue line items such as Bancassurance, asset management and insurance will support further upside.

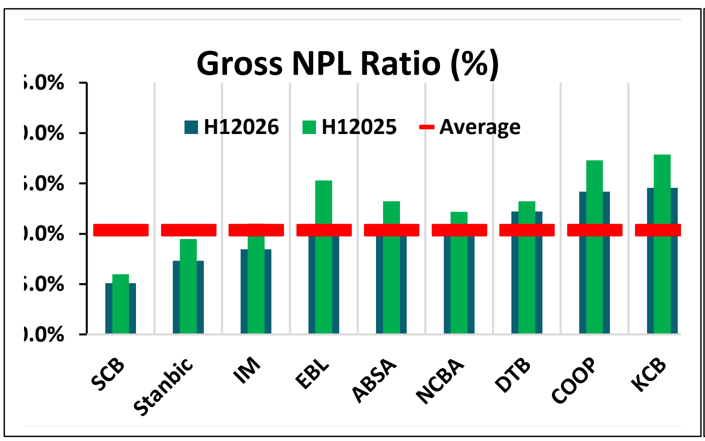
5) Asset Quality: Fragile Recovery Amid Renewed Global Headwinds

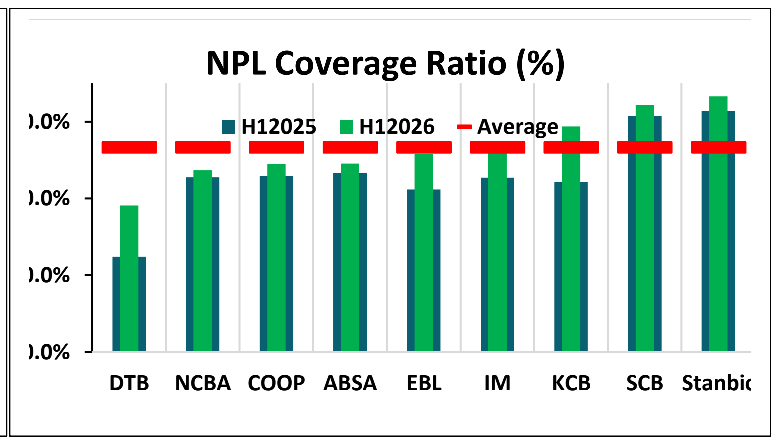
Asset quality showed a gradual but fragile trajectory in **H12026**, with average sector Non-Performing Loan (**NPL**) ratios hovering around 14.6%. The temporary reprieve brought by an earlier accommodative monetary stance has slowed. Renewed macroeconomic friction, triggered by global developments, threatens to usher in a "higher-for-longer" interest rate environment.

Historically, the initial deterioration in asset quality was driven by compounding domestic factors:

- High benchmark lending rates
- Protracted government payment delays to contractors
- Sustained borrower cash flow stress

While the sector recently saw marginal improvements owing to active loan book clean-ups and restructured facilities, the pace of recovery is still fragile. Furthermore, Kenya's structural NPL levels remain elevated compared to regional peers.





Source: Comp Fin, KCB IB

Bank-Level Performance: Asset quality trends diverge sharply across the banking sector, directly reflecting individual risk appetites and corporate sector exposures.

High NPL Tier 1 Banks: KCB and Co-operative registered the highest NPL ratios among tier-1 peers, breaking past the 14.0% mark in H12026. However, both institutions show signs of stabilization through aggressive recoveries and tightened underwriting controls, having improved from the highest levels of 17.9% and 17.3%, for KCB and Co-operative, respectively.

Defensive & Conservative Banks: Stanbic and Standard Chartered maintained exceptionally robust asset quality. Their NPL profiles sit comfortably below the sector average due to highly conservative corporate lending frameworks and a focus on premium, low-risk borrowers.

Outliers & Legacy Strains: Among all listed banking institutions, HFCB continues to carry the heaviest NPL burden. This is primarily a function of legacy defaults embedded in its historical mortgage lending portfolio, though ongoing internal balance sheet clean-ups are slowly reversing the damage.

Provisions & Risk Buffers: To counter looming defaults, Kenyan banks have aggressively fortified their financial safety nets using the IFRS 9 forward-looking framework. While provisioning expenses spiked alongside initial NPL defaults, NPL coverage ratios remained resilient through H12026. Notably, Stanbic and SCB led the market with coverage ratios exceeding 80%, while DTB trailed significantly below the sector average at under 50%. This proactive buffering ensures that the tier-1 banking segment maintains sufficient capital runways to absorb any potential credit shocks.

Outlook & Market Sentiments:

The forward-looking outlook for the remainder of 2026 has tilted hawkish. The Fed's interest rate hike signals a sharp reversal in global liquidity. This external tightening severely constrains the domestic central bank's ability to maintain an accommodative stance.

Simultaneously, geopolitical friction continues to inject volatility into global supply chains, driving international crude oil prices higher. The elevated energy prices run the risk of feeding directly into domestic inflation. Commercial banks thus face a dual threat of imported inflationary pressures and potential elevation of borrowing costs.

Consequently, while the sector's asset quality clean-up offers cushion, credit risks are expected to remain firmly elevated through the next fiscal quarters. Banks will likely adopt a highly defensive lending posture to protect their balance sheets from a renewed wave of defaults.

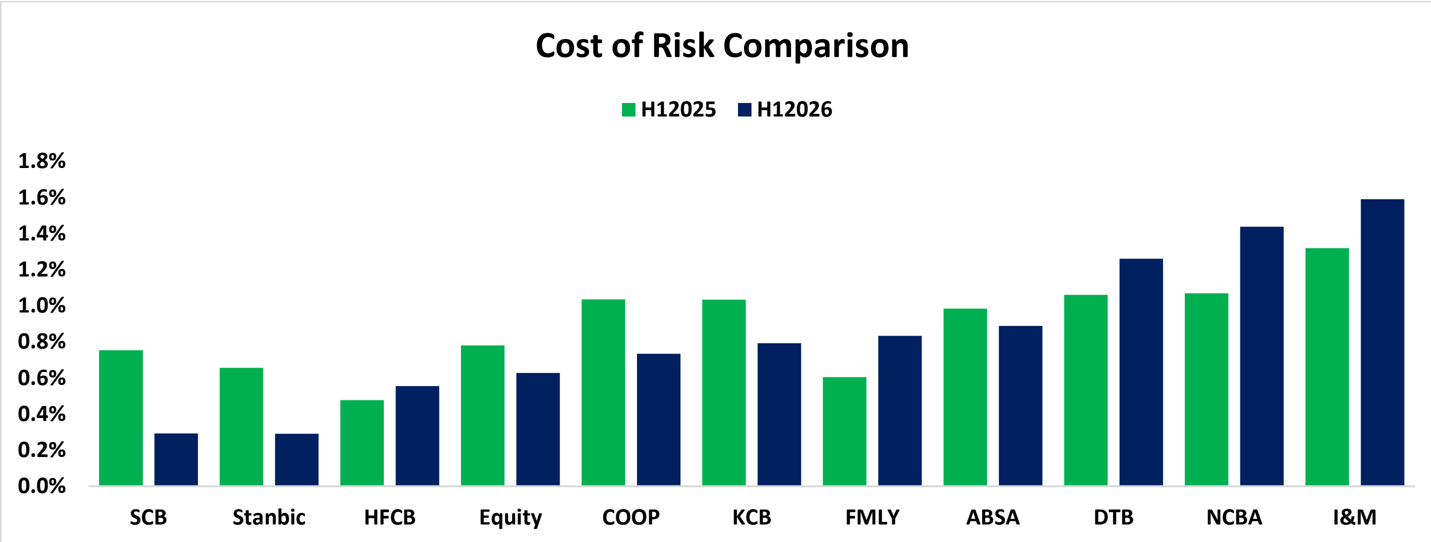
Cost of Risk Dynamics: Divergent Paths Amid Shifting Monetary Landscapes

The sector transitioned into a lower risk phase, with cost of risk declining as borrower stress eases. Leading banks such as Stanchart and Stanbic recorded notable improvements, while others like NCBA and I&M maintained higher provisions to address exposures. Overall, the shift reflects improving credit conditions and stronger risk management.

The sector's cost of risk trajectory reflects a bifurcated credit environment in H12026, heavily influenced by individual bank asset quality clean-ups and uneven borrower recovery. While some institutions capitalized on the tail-end of the accommodative domestic stance, others built additional buffers to insulate against brewing macroeconomic shocks.

Analysis of individual bank performance reveals distinct strategies:

- **Market Leaders:** SCB and Stanbic recorded the most significant improvements. Both banks shift successfully reduced their cost of risk from H12026, because of prime-borrower portfolios.
- **Proactive Provisioning:** In contrast, I&M, NCBA, and DTB escalated their risk pricing. I&M recorded the highest CoR in the peer group, climbing to nearly 1.6%, followed closely by NCBA at 1.4% and DTB at 1.3%. This upward reflects deliberate, heightened provisions to safely manage legacy and emerging corporate exposures.
- **Mid Adjustments:** Family Bank and HFCB saw mild expansions in their risk costs, while COOP, KCB, and Equity benefited from normalizing credit environments, dropping their CoR indicators significantly below H12025 levels.



Source: Comp Fin, KCB IB

Cost Dynamics Outlook: The asset quality and provisioning outlook for the remainder of 2026 remains cautiously defensive, as improving domestic conditions are increasingly offset by renewed global and fiscal risks. While recent loan-book clean-ups have provided some relief, pressure on borrowers is likely to persist.

Key risks include:

- **Tighter global financial conditions:** The **Fed hike** could constrain the scope for further domestic monetary easing, while keeping funding and liquidity conditions relatively tight.
- **Higher and volatile oil prices:** Escalating **Middle East tensions** pose a risk of renewed oil-price pressures, which could raise operating costs, weaken household purchasing power and constrain borrowers' debt-servicing capacity.
- **Fiscal payment delays:** Delayed government payments to contractors and suppliers continue to create liquidity pressure across the private sector, increasing the risk of working-capital stress and loan delinquencies.

We expect banks to remain focused on proactive loan restructuring, tighter underwriting and prudent provisioning. Further improvement in asset quality will increasingly depend on banks' risk-management discipline and ability to selectively grow high-quality credit, rather than broad-based macroeconomic support.

6) Key Strategic Trends: Structural shift toward scale, efficiency, digitalization, and capital strength

The banking sector in 2026 is undergoing a major structural shift. Strategy has moved beyond simple banking toward becoming regional financial conglomerates driven by digital infrastructure and a race for capital.

Some of the key strategic trends involve:

- **Regional Diversification:** Regional operations are increasingly driving profitability and diversification. Equity derives almost 50% of PBT from subsidiaries, while KCB's regional expansion, particularly in the DRC, strengthens its position.
- **New Capital Requirements (The Business Laws, Amendment, Act, 2024):** Regulatory and strategic shifts are set to reshape the competitive landscape. Following legislative revisions that repealed the strict annual interim milestones, the deadline for commercial banks to increase their minimum core capital to KES 10Bn has been extended to 2032. This adjusted timeline

provides a longer, more flexible compliance window to prevent disruption in credit access for the wider economy. Nevertheless, the ultimate mandate continues to drive market consolidation, capital raising, and strategic partnerships. This trend is already evident through increased M&A activity, capital injections from parent companies, and rights issues. Growing interest from regional players, particularly from South Africa and Nigeria, further reinforces Kenya's position as a key financial hub.

- **Digital Transformation:** Over 98% of transactions are now processed through digital channels. Banks are investing in AI-driven lending, fraud detection, and API ecosystems to enhance efficiency and customer experience.
- **Revenue Diversification Beyond Traditional Banking:** Banks are expanding into non-funded income streams to reduce reliance on traditional lending. Equity has strengthened its presence in insurance, while KCB continues to grow its investment banking and asset management businesses. Standard Chartered is leveraging digital platforms such as *Shilingi* to drive transactional revenue, and Absa is expanding its footprint in wealth management and advisory services to enhance income diversification.
- **Structural consolidation**

Let's dive into deeper analysis for individual banks under our coverage;

Stock	18th Sept 2026	EPS	P/B	P/E	BVPS	ROaE	Trailing Div	Dividend Yield	Target Price	Upside (%)	Recommendation
Cooperative	34.80	5.04	1.19x	6.90x	29.15	**20.27%**	2.50	7.18%	42.03	27.96%	**BUY**
Equity	98.50	19.07	1.06x	5.17x	92.84	**27.60%**	5.75	5.84%	125.48	33.23%	**BUY**
I&M	80.00	34.70	1.17x	7.41x	68.62	**18.02%**	3.75	4.69%	79.00	3.44%	**HOLD**
Stanbic	278.00	11.18	1.59x	8.01x	174.70	**20.38%**	22.35	8.04%	281.47	9.29%	**HOLD**
NCBA	86.25	14.20	1.08x	6.07x	79.82	**19.79%**	7.10	8.23%	107.10	32.41%	**BUY**
Stanchart	330.75	32.47	1.96x	10.67x	168.83	**17.12%**	31.00	9.37%	348.96	14.88%	**ACCUMULATE**
Absa	31.10	4.22	1.68x	7.37x	18.51	**22.63%**	2.05	6.59%	33.93	15.69%	**HOLD**
DTB	179.50	33.65	0.49x	5.33x	366.18	**10.43%**	9.00	5.01%	213.75	24.09%	**BUY**

Source: NSE, KCB IB

Banking Sector Analysis

A. Equity Group-BUY:(TP-KES 125.48, CP- 98.50, Upside-33.2%)

- Equity Group delivered a strong H12026 performance, reinforcing its position as one of the region's highest-quality banking franchises.
- **PAT** increased 31.5% y/y to KES 45.5Bn, supported by a 16.8% increase in NII and a 35.9% growth in NFI. Operating income rose 24.6% to KES 124.9Bn, highlighting the Group's strong revenue generation and diversified income base.
- **Asset quality** improved materially, with the gross NPL ratio declining to 10.2% from 15.3%, while gross NPLs fell 22.2% y/y to KES 108.4Bn. The improvement provides greater capacity for balance sheet expansion as credit demand recovers.
- **Profitability** metrics strengthened, with ROaE improving to 27.6% from 21.7%, while NIM expanded to 7.8% from 7.5%, supported by lower funding costs and improved asset yields.
- **Regional Diversification & Expansion**: The diversified regional footprint remains a key earnings strength, with revenue contribution between Equity Kenya and the regional subsidiaries broadly balanced at 50:50.
- **Valuation** remains reasonable relative to the Group's growth and profitability profile, with the stock trading at 5.2x P/E and 1.1x P/B.

- The trailing dividend yield of 5.8% further enhances the income proposition. With a 30%-50% dividend payout policy and approximately 30% payout in 2025, there remains meaningful headroom for dividend growth as subsidiaries mature and increasingly contribute distributable earnings.

- We maintain a positive long-term view on the stock, supported by **strong earnings momentum**, **improving asset quality, high profitability, attractive valuation, and growing earnings diversification**.

- It remains well suited to investors seeking quality, stability, income, and long-term compounding potential.

B. Standard Chartered Bank (ACCUMULATE:TP-348.9, CP-330.75, Upside-14.4%) Dividend Anchor

- Standard Chartered Kenya delivered a weaker H1'2026 performance, with PAT declining 16.8% y/y to KES 6.7Bn, primarily due to a sharp contraction in NII.
- **NFI** provided earnings support, increasing 15.9% y/y to KES 7.9Bn, partially offsetting the decline in core interest income and highlighting the bank's ability to diversify.
- **Asset quality** remained a key strength, with the gross NPL ratio improving to 5.1% from 6.0%, while NPL coverage increased to 84.3%.
- **The balance sheet** remained resilient, with loans and advances growing 11.1% y/y to KES 169.2Bn, ahead of the 6.4% increase in customer deposits to KES 309.1Bn.
- **Profitability** came under pressure, with ROaE declining to 17.1% from 27.8% and NIM narrowing to 10.3% from 13.9%, reflecting lower asset yields.
- The bank maintained its strong shareholder distribution profile, declaring an interim dividend of **KES 8.50 per share, up 6.3% y/y**. The continued dividend growth provides meaningful income support despite the weaker earnings performance and remains a key component of the investment case.
- At approximately 10.7x P/E and 2.0x P/B, the stock trades at a premium to most local banking peers, limiting near-term valuation upside. However, this premium is partly justified by the bank's strong asset quality and consistent dividend track record.
- We maintain an **ACCUMULATE** recommendation. While near-term earnings remain constrained by pressure on NII and margins, the stock's strong **dividend yield**, **resilient balance sheet, improving asset quality, and defensive earnings profile provide downside support.**

C. Co-operative Bank: BUY (TP-42.0, CP-34.8, Upside-28.0%): Defensive Income Play

- Co-operative Bank delivered a strong H1'2026 performance, with PAT rising 28.0% y/y to KES 18.0Bn, supported by a 13.0% increase in NII to KES 33.2Bn and an 11.6% growth in non-funded income to KES 15.8Bn.
- The bank continues to demonstrate resilient fundamentals, supported by its strong domestic franchise, improving asset quality, healthy loan growth, and growing contributions from its banking and non-banking subsidiaries.
- Co-operative Bank's diversified business model provides additional earnings resilience, with continued growth in both interest and non-funded income. Increasing contributions from the Group's subsidiaries should further support revenue diversification and reduce reliance on traditional banking income.
- Valuation remains attractive, with the stock trading at approximately 6.9x P/E and 1.2x P/B, which we view as reasonable given its strong profitability, earnings growth, and improving fundamentals.
- The 7.2% trailing dividend yield further enhances the investment case, particularly following the introduction of an interim dividend in 2025.
- We issue a **BUY** recommendation, supported by strong earnings momentum, improving asset quality, resilient loan growth, attractive valuation, and a consistent dividend profile.

D. Stanbic Bank – HOLD (TP-281.5, CP-278.0, HOLD-9.3%): Offer income & Stability

- Stanbic Holdings delivered a resilient H1'2026 performance, with PAT increasing marginally by 1.0% y/y to KES 6.6Bn, supported by 4.1% growth in Net Interest Income (NII), although this was largely offset by a 0.1% decline in non-funded income.
- Operating income rose 2.5% to KES 19.2Bn, while operating expenses increased 5.3% to KES 9.9Bn,

reflecting continued investment in the Group's operations.

- **Loans and advances** grew by 16.7% y/y to KES 360.2Bn, while **deposits** increased by a robust 33.4% to KES 467.5Bn. The strong deposit growth provides a solid funding base for continued credit expansion and positions the bank to benefit from an improvement in credit demand.
- **Asset quality** remained sound, with the NPL ratio broadly stable at 7.3%, comparing favorably with the wider banking sector. Loan loss provisions also declined by 45.6% y/y, providing support to earnings and reflecting improved credit risk conditions.
- Shareholder returns were weaker, with the Board declaring an interim dividend of KES 1.64 per share, down 56.8% from KES 3.80 in H1'2025. The reduction tempers the bank's near-term income appeal, despite its historically strong dividend track record.
- Profitability remained relatively strong, with ROE at 18.2%, although the limited growth in earnings highlights the near-term challenge of converting strong balance-sheet expansion into higher profitability.
- At 1.6x P/B, the stock trades at a modest premium to the sector, limiting room for near-term valuation expansion.
- We maintain a **HOLD** recommendation. Stanbic offers a combination of strong balance-sheet growth, sound asset quality, resilient profitability, and a well-established dividend track record. However, the muted earnings growth, higher operating costs, and significant decline in the interim dividend limit near-term upside.

E. NCBA Group – BUY (TP-107.1, CP-86.3 Upside-32.4%)

- NCBA Group recorded strong H1'2026 performance, with PAT increasing 12.2% y/y to KES 12.4Bn, supported by a 20.4% increase in Net Interest Income (NII) and 7.6% growth in non-funded income.
- **Operating efficiency and asset quality** continued to improve, with the cost-to-income ratio declining to 47.9% from 52.5%, while the NPL ratio improved to 10.8%.
- ROaE remained strong at 19.8%, underscoring the Group's ability to generate attractive returns despite the challenging operating environment.
- Shareholder returns strengthened, with the Group increasing its interim dividend by 50.0% y/y to KES **3.75 per share**. The higher interim payout, alongside a trailing 12-month DPS of KES 7.10, translates to an attractive dividend yield of approximately 7.7% and provides scope for further income growth.
- Valuation remains attractive relative to the Group's profitability and growth profile, with the stock trading at approximately 6.1x P/E and 1.0x P/B. The combination of strong returns, improving efficiency, earnings resilience, and a high dividend yield provides an attractive risk-reward profile.
- The Group also offers additional long-term growth potential through its diversified regional and non-banking businesses. Continued loan growth, lower funding costs, improving asset quality, and stronger subsidiary contributions should support earnings expansion. The acquisition of a 66% controlling stake by Nedbank also introduces a strategic partner with the potential to strengthen NCBA's regional footprint, capabilities, and long-term growth prospects.

F. I&M Holdings – HOLD (TP-79.0, CP-80.0, Upside-3.4%)

- I&M delivered an impressive H1'2026 performance, with PAT rising 22.4% y/y to KES 10.2Bn, supported by broad-based growth in both funded and non-funded income. NII increased 22.5% to KES 25.0Bn, while non-funded income grew 24.5% to KES 8.7Bn.
- Subsidiaries remain an important earnings driver, contributing approximately **33%** of Group PBT, with continued growth across the regional and non-banking businesses supporting earnings diversification.
- Fundamentals remain positive, with improving asset quality, healthy deposit mobilization and strong earnings momentum. ROaE stood at 18.0%, broadly in line with peers, while continued earnings growth should support further improvement in dividend payouts.
- At 7.4x P/E and 1.2x P/B, the stock is trading close to our fair value following its recent rally. With only 2.7% upside to our target price plus dividend yield, we see limited scope for near-term re-rating despite the strong underlying performance.
- We maintain a **HOLD** recommendation. I&M remains fundamentally sound, but the current valuation largely

reflects its improved earnings outlook. Further upside will depend on sustained earnings growth, stronger subsidiary contributions and continued improvement in asset quality, while cost growth and the pace of credit expansion remain key risks to monitor.

G. Absa Bank Kenya – HOLD (TP-33.9, CP-31.1, Upside-15.7%)

- Absa Bank Kenya delivered a weaker H1'2026 performance, with PAT declining 9.8% y/y to KES 10.5Bn, as NII fell 5.4% to KES 21.1Bn and non-funded income declined 10.2% to KES 8.2Bn. Operating income consequently fell 6.8% to KES 29.3Bn.
- Lower funding costs provided some support, with total interest expense declining 17.7% y/y to KES 6.2Bn, driven by a 19.8% reduction in interest expense on customer deposits. However, this was insufficient to offset pressure on asset yields, with NIM declining to 9.5% from 11.0%.
- The balance sheet remains resilient, with loans growing 8.2%, while asset quality continued to improve. The bank's diversified non-banking businesses, including Bancassurance, Asset Management and Custody, provide additional earnings diversification and offer potential for a recovery in non-funded income.
- Shareholder returns remain attractive, with the interim dividend increasing 150%, supporting a trailing dividend yield of approximately 6.0%. However, ROaE has weakened alongside the decline in earnings.
- At approximately 7.4x P/E and 1.7x P/B, the stock trades at a premium valuation relative to its current earnings trajectory.
- We maintain a **HOLD** recommendation. **The attractive dividend and resilient balance sheet provide downside support, but weak core income growth, margin compression and elevated valuation constrain the near-term investment case. A stronger recovery in loan growth, stabilization of NIM and renewed growth in non-funded income would be key catalysts for a more positive view.**

H. DTB –Buy (TP-213.75, CP-179.5, Upside- 24.1%)

- DTB delivered a strong H1'2026 performance, with PAT rising 35.8% y/y to KES 7.3Bn, supported by a 26.4% increase in NII to KES 20.0Bn and 6.6% growth in non-funded income to KES 6.5Bn.
- Lower funding costs further supported earnings, with interest expense declining 9.5% to KES 12.2Bn, while the 13.7% growth in loans and improvement in NIM to 7.4% demonstrates strong operating momentum and improving balance-sheet utilization
- Asset quality also strengthened, with NPL coverage improving to 58.2% from 44.8%, providing a stronger buffer against potential credit losses. ROaE improved to 11.7% from 10.1%, with further upside expected as profitability and capital efficiency improve.
- Valuation remains the key attraction, with DTB trading at approximately 5.1x P/E and 0.4x P/B, despite its improving earnings and return profile. The 26.7% payout ratio also provides significant headroom for future dividend growth as profitability strengthens.
- The bank is well positioned to benefit from lower funding costs, improving credit demand and the easing interest-rate environment, while its relatively low P/B valuation provides scope for a re-rating as returns improve.
- We maintain an **ACCUMULATE** recommendation. The combination of strong earnings momentum, improving asset quality, deep-value valuation and significant balance-sheet capacity for growth offers an attractive risk-reward profile. Continued improvement in ROaE and profitability provides a clear pathway for further value creation and potential re-rating.

H12026 Banking Sector Analysis

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