Cytonn INVESTMENTS

Cytonn Weekly Update

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Fixed Income Update

The government released the Budget Policy Statement indicating an increase in the budget from KES 1.2 trillion in the year 2011/2015 to KES 1.9 trillion for 2015/2016 financial Year. Road, railway, energy and airport projects are set to be the biggest winners. There was an increase in the allocation to fund Infrastructure development to KES 675 billion, up from KES 560 billion.

The budget will be funded by tax collections of KES 1.2 trillion

supported by appropriations in aid of KES 100 billion, with the deficit being covered by debt. The Treasury plans to borrow KES 187 billion from the domestic market and KES 287 billion from international investors. We anticipate high demand from foreign investors given the successful issuance of the first Eurobond and deflationary fears in the Eurozone, which have kept rates depressed, making Kenyan Bonds more attractive.

In other news, the Central Bank of Kenya?s 91-day Treasury Bills were oversubscribed at 139.8% subscription rate with an increase in the T-bill rate from 8.529% in the previous auction to 8.601%. The 182 and 364-day T-bills were undersubscribed at 87% subscription for each. In our view, these auctions signal investor?s expectations of a rise in rates and hence are non-committal towards longer dated Paper.

Equity Market Update

East African bourses topped in Sub - Saharan African performance in full-year 2014, with the NSE coming in third after Tanzania and Uganda. The NSE in full-year 2014 returned 19.2%, while Tanzania and Uganda markets traded 22.7% and 14.1% higher respectively. In USD terms, however, most markets had negative returns. The worst performers were Ghana, Nigeria and Zimbabwe. The Greenback saw large gains during Q4 2014, eroding any USD losses that local bourses had made.

The Strong economic growth prospects will continue to support corporate earnings, pro-business policies and benign macro-environment ? supported by lower oil prices?will have a positive impact on both consumer and business spending expenditure therefore we expect the equity markets to continue with mid double-digit growth.

In other news, following the introduction of the Capital Gains Tax (CGT), there has been confusion in the market regarding its implementation. Stockbrokers have now moved to court to have the various controversial clauses redressed. Some of the stock brokerage firms have cited cumbersomeness in filing of the tax as part of the challenges of the new law. The Capital Gains Tax was reintroduced after 3 decades as part of the Finance Act 2014, and is charged at 5%.

Real Estate Update

Kenya?s only listed mortgage lender, Housing Finance (HF) is set to raise additional capital of KES 3.5 billion (USD 38.29 million) in a rights issue at KES 30 per share. The funds raised from the issue, one for every two shares held, are set to increase the financier?s lending capacity. This offer runs from 19th February to 13th March, 2015. The issue will propel Housing Finance as the premier lender for mortgages, financing and facilitating developers and buyers of property in the real estate sector.

The HF issue comes at a time when Kenya?s housing needs are estimated at 210,000 new units as compared to the current 50,000 units actually built. Furthermore, Kenya?s middle class has shown a high appetite for new housing units consequently increasing demand above the current supply. This has strongly contributed to Cytonn?s keen focus in investment opportunities in Kenya?s thriving real estate sector.

Private Equity Update

Egyptian Private Equity firm Qalaa Holdings, formerly Citadel Holdings will invest US$70 million to hasten the movement of rail cargo from the port of Mombasa, Kenya, into the East African markets. Qalaa?s investment will go into assisting Rift Valley Railways (RVR) in handling cargo at the port. Qalaa currently holds 85% of RVR, the operator of the Kenya-Uganda railway. At the moment, roughly 90% of the 23.5 million tonnes of cargo in Mombasa is ferried by road. It is interesting, however, to note that as Qalaa?s plans to spend heavily on RVR,it is yet to be seen how this works out given that the government of Kenya has begun the construction of a parallel Standard Gauge Railway. Undoubtedly, Qalaa?s investment highlights the confidence investors have in Kenya as well as the abundant opportunities available for PE investment in Kenya.

African IPOs expected to rise by 25% in 2015, as per a new report by Law Firm Baker & McKenzie. Firms in the real estate, financial and energy sectors were expected to be most active and most new listings would be on markets in Egypt, Kenya, Morocco, Nigeria, South Africa and Tunisia, the law firm said.

Listings are expected to be primarily driven by Private Equity exiting investments. Improved corporate governance, better regulation and expanding economies were creating a more sound footing for African capital markets, and will contribute to the deepening of the Capital Markets in these countries.

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