

Cytonn H1'2020 Markets Review

Equities

Markets Performance

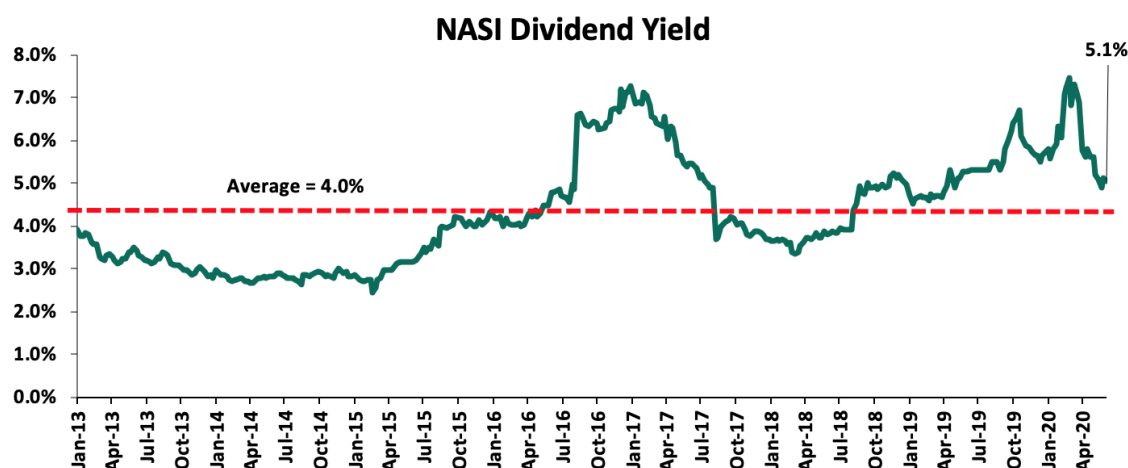
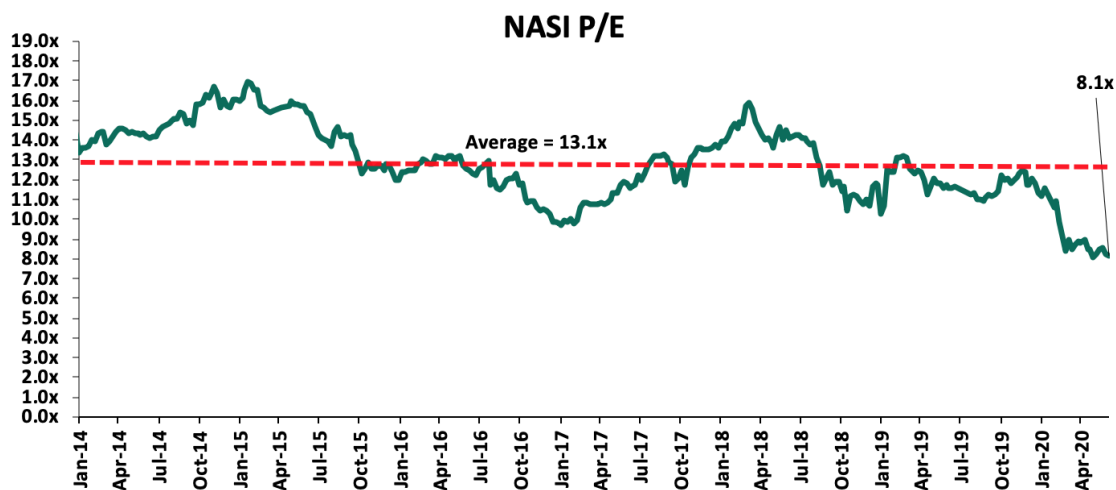
In H1'2020, the equities market was on a downward trend, with NASI, NSE 20 and NSE 25 declining by 17.3%, 26.8% and 21.5%, respectively. The equities market performance during the first half was driven by losses recorded by large caps such as:

No	Company	Loss In Percentage
1	Bamburi	65.0%
2	BAT	36.5%
3	Equity Group	35.1%
4	DTBK	35.1%
5	KCB	32.7%
6	NCBA	28.0%
7	Co-operative bank	25.7%
8	ABSA	25.1%

During the week, the equities market recorded mixed performances, with NASI and NSE 20 recording gains of 1.3% and 0.4%, respectively, while NSE 25 declined by 0.4%, taking their YTD performance to losses of 16.1%, 26.7%, and 21.5%, for NASI, NSE 20 and NSE 25, respectively. The NASI performance was driven by gains recorded by large-cap stocks such as Safaricom, Bamburi and SCBK, which gained by 4.0%, 2.8% and 1.3%, respectively. The gain was however weighed down by losses recorded by other large-cap stocks such as Equity Bank, EABL, KCB, BAT and Co-operative bank of 6.3%, 4.4%, 3.7%, 3.1% and 2.4%, respectively. For the last twelve months (LTM), NASI, NSE 25 and NSE 20 have declined by 8.0%, 10.3% and 26.2%, respectively.

In H1'2020, equities turnover increased by 5.0% to USD 808.8 mn from USD 770.2 mn in H1'2019. Foreign investors turned net sellers in H1'2020 with a net selling position of USD 216.5 mn from a net buying position of USD 23.3 mn in H1'2019. During the week, equities turnover declined by 44.8% to USD 14.4 mn, from USD 26.1 mn recorded the previous week, taking the YTD turnover to USD 816.0 mn. Foreign investors remained net sellers during the week, with a net selling position of USD 4.3 mn, from a net selling position of USD 12.3 mn recorded the previous week, taking the YTD net selling position to USD 218.1 mn.

The market is currently trading at a price to earnings ratio (P/E) of 8.1x, 37.9% below the historical average of 13.1x. The average dividend yield is currently at 5.1%, unchanged from the previous week, and 1.1% points above the historical average of 4.0%. With the market trading at valuations below the historical average, we believe there are pockets of value in the market for investors with higher risk tolerance and are willing to wait out the pandemic. The current P/E valuation of 8.1x is 1.1% above the most recent valuation trough of 8.0x



During the first half of 2020, banks released their FY'2019 and Q1'2020 results, recording earnings growth and loss of 8.9% and (7.4%) in their core EPS in FY'2019 and Q1'2020, respectively.

Listed Banks Q1'2020 Highlights:

Kenyan listed banks released their Q1'2020 results, recording a 7.4% average decline in core Earnings per Share (EPS) compared to a growth of 12.2% in Q1'2019. The performance for Kenyan listed banks in Q1'2020 is summarized below:

Bank	Core EPS Growth	Interest Income Growth	Interest Expense Growth	Net Interest Income Growth	Net Interest Margin	Non-Funded Income Growth	NFI to Total Operating Income	Growth in Total Fees & Commissions	Deposit Growth	Growth in Government Securities	Loan to Deposit Ratio	Loan Growth	Return on Average Equity
ABSA	17.0%	2.8%	(1.9%)	4.5%	7.4%	9.1%	15.8%	(0.2%)	6.6%	7.2%	85.0%	12.4%	17.0%
KCB	8.4%	20.4%	26.6%	18.5%	8.1%	30.5%	34.4%	33.6%	34.1%	52.0%	74.8%	19.3%	20.0%
DTBK	3.7%	(2.4%)	(9.0%)	2.9%	5.7%	3.4%	25.4%	9.6%	(0.9%)	1.9%	73.8%	6.7%	12.6%
COOP	(0.3%)	4.5%	(4.4%)	8.5%	8.2%	19.0%	39.9%	28.3%	6.9%	11.5%	81.3%	9.8%	18.5%
Equity	(14.1%)	14.3%	26.7%	10.6%	8.2%	15.8%	41.9%	12.5%	16.5%	14.2%	75.9%	24.1%	20.7%
SCBK	(16.6%)	(4.3%)	(1.3%)	(5.1%)	7.2%	(6.5%)	32.1%	(5.2%)	4.6%	(13.7%)	51.5%	6.8%	15.8%
NCBA ***	(26.8%)	6.8%	8.3%	5.5%	3.3%	25.9%	49.7%	49.7%	9.9%	66.2%	63.0%	2.2%	10.7%
I&M	(29.7%)	5.7%	7.1%	4.6%	5.8%	7.4%	38.8%	12.9%	8.8%	(2.6%)	76.0%	8.3%	17.5%
Stanbic	(33.5%)	(7.1%)	0.5%	(11.0%)	5.5%	(29.2%)	43.2%	(37.6%)	6.4%	(19.9%)	79.8%	11.8%	14.1%
HF	N/A	(7.8%)	(20.9%)	13.7%	4.5%	(2.0%)	30.4%	(3.7%)	11.8%	39.3%	101.1%	(8.5%)	0.5%
Q1'2020 Mkt Weighted Average*	(7.4%)	8.2%	11.4%	7.4%	7.2%	15.9%	22.7%	24.5%	14.3%	14.9%	74.1%	14.1%	17.2%

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Q1'2019 Mkt Weighted Average**	12.2%	3.6%	2.5%	4.5%	8.0%	10.7%	36.0%	11.2%	11.0%	16.1%	74.0%	7.7%	19.2%

*Market cap-weighted as at 02/06/2020

**Market cap weighted as at 31/05/2019

***The financial statements of the bank have been prepared on a prospective basis (assuming a continuation of CBA), representing Q1'2020 results of NCBA bank (merged bank) with prior year comparatives (Q1'2019) being those of CBA bank. Hence, the results are not comparable on a like for like basis. As such, we have used proforma-combined financials for the two entities.

Key take-outs from the above table include:

1. Listed Kenyan banks recorded a 7.4% average decline in core Earnings per Share (EPS) compared to a growth of 12.2% in Q1'2019, the depressed earnings recorded in the listed banking sector is partly attributed to the tough operating environment occasioned by the ongoing Coronavirus pandemic, which saw total operating expenses increase by 25.6%, outpacing the 10.3% increase recorded on total operating income,
2. Listed Banks recorded a deposit growth of 14.3%, faster than the 11.0% growth recorded in Q1'2019. Interest expenses, on the other hand, rose by 11.4%, faster than 2.5%, recorded in Q1'2019. The cost of funds, however, declined coming in at a weighted average of 3.1% in Q1'2020 down from 3.5% in Q1'2019 owing to the faster 12.2% growth average interest-bearing liabilities indicating that the listed banks were able to mobilize cheaper deposits,
3. Average loan growth came in at 14.1%, which was faster than the 7.7% recorded in Q1'2019, with the growth in loans being accelerated following the repeal of interest rate cap in November 2019, coupled with increased demand in funding, as businesses demand working capital to operate in the tough operating environment as a result of the pandemic,
4. Interest income rose by 8.2%, compared to a growth of 3.6% recorded in Q1'2019. The faster growth in interest income may be attributable to the 14.1% growth in loans and increased allocation to government securities. The net interest income increased by 7.4% slower than the 10.7% rise in average interest-earning assets. Consequently, the Net Interest Margin (NIM) declined to 7.2%, compared to the 8.0% recorded in Q1'2019 for the whole listed banking sector, and,
5. Non-Funded Income grew by 15.9% y/y, faster than 10.7% recorded in Q1'2019. The growth in NFI was supported by the 24.5% average increase in total fee and commission income, which was faster than the 11.2% growth recorded in Q1'2019. For more information, please see our Q1'2020 Listed Banks Report.

Half-Year Highlights:

During the first half of 2020:

- i. The Central Bank of Kenya gave a go-ahead to Nigerian lender, Access Bank PLC to acquire a 100% stake in Transnational Bank PLC for an undisclosed amount, with Access Bank PLC targeting to enhance its corporate and retail banking business in Kenya through the acquisition. For more information see our [Cytonn Weekly #03/2020](#),
- ii. Barclays Bank of Kenya officially commenced trading on the Nairobi Securities Exchange (NSE) as ABSA Bank Kenya Plc, after the bourse temporarily suspended the trading of the lender's shares to allow the settlement of outstanding obligations as well as a change of its trading ticker code, as the lender finalized its brand transition. For more information see our [Cytonn Weekly #07/2020](#),
- iii. The Central Bank of Kenya (CBK) announced the acquisition of a 51.0% stake in Mayfair Bank Limited by Egyptian lender, Commercial International Bank (CIB), effective 1st May 2020 for an undisclosed amount following CBK's approval on 7th April 2020. For more information, please see [Cytonn Weekly #17/2020](#),
- iv. NCBA Group, the third-largest bank by assets in Kenya, with an asset base of Kshs 509.6 bn as at March 2020, announced it would withhold the final dividend payment of Kshs 1.5 per share, to shareholders totalling to Kshs 2.2 bn for FY'2019. For more information, please see [Cytonn](#)

Weekly #17/2020,

- v. Global rating agency Moody's changed the outlook for KCB, Equity and Co-operative Bank to "Negative" from "Stable" but affirmed all three banks' local currency deposit ratings at B2, citing the link between their rating and that of the state due to the top banks' large exposure to government securities, which poses a risk to their credit profile. For more information, please see Cytonn Weekly #20/2020
- vi. Equity Group announced it had mutually agreed with Atlas Mara to call off plans to acquire banking assets in four countries in exchange for shares in Equity Group. For more information, please see Cytonn Weekly #26/2020,
- vii. Jamii Bora Bank (JBB), disclosed Co-operative bank had offered an initial Kshs 1.0 bn for a 90.0% stake in Jamii Bora Bank, effectively valuing Jamii Bora Bank at Kshs 1.1 bn. For more information, please see Cytonn Weekly #26/2020, and,
- viii. The Board of Directors for Equity Group withdrew their recommendation to pay a first and final dividend of Kshs 2.50 per share for FY'2019 and instead recommended to shareholders that no dividend be paid for FY2019. For more information, please see Cytonn Monthly- May 2020.

Universe of Coverage:

Company	Price at 26/06/2020	Price at 03/07/2020	w/w change	q/q change	YTD Change	Year Open	Target Price*	Dividend Yield	Upside/Downside**	P/TBv Multiple	Recommendation
Diamond Trust Bank***	70.0	70.0	0.0%	(19.6%)	(35.8%)	109.0	175.0	3.9%	153.9%	0.4x	Buy
Kenya Reinsurance	2.2	2.2	0.0%	(9.3%)	(26.7%)	3.0	4.6	5.0%	112.2%	0.2x	Buy
KCB Group***	36.4	35.1	(3.7%)	3.9%	(35.1%)	54.0	56.2	10.0%	70.3%	0.9x	Buy
I&M Holdings***	50.0	49.4	(1.3%)	(1.5%)	(8.6%)	54.0	76.3	5.2%	59.8%	0.8x	Buy
Co-op Bank***	12.5	12.2	(2.4%)	(5.4%)	(25.4%)	16.4	18.0	8.2%	55.7%	1.0x	Buy
Equity Group***	35.1	32.9	(6.3%)	2.2%	(38.6%)	53.5	50.7	0.0%	54.3%	1.2x	Buy
Stanbic Holdings	82.0	80.3	(2.1%)	(8.4%)	(26.5%)	109.3	111.2	8.8%	47.4%	1.0x	Buy
ABSA Bank***	10.1	10.1	(0.5%)	(1.0%)	(24.7%)	13.4	13.2	10.9%	42.3%	1.3x	Buy
Jubilee Holdings	250.0	250.0	0.0%	(9.3%)	(28.8%)	351.0	334.8	3.6%	37.5%	0.9x	Buy
NCBA***	27.1	26.5	(2.0%)	(6.5%)	(28.1%)	36.9	35.6	0.9%	35.3%	0.8x	Buy
Sanlam	13.7	13.7	0.0%	(10.0%)	(20.6%)	17.2	18.4	0.0%	34.8%	1.3x	Buy
Standard Chartered***	167.0	169.3	1.3%	(4.6%)	(16.4%)	202.5	202.7	7.4%	27.1%	1.5x	Buy
Liberty Holdings	7.2	8.0	11.4%	(5.0%)	(22.3%)	10.4	9.8	0.0%	22.3%	0.7x	Buy
Britam	7.8	7.6	(2.6%)	17.2%	(15.6%)	9.0	7.6	3.3%	3.3%	0.7x	Lighten
CIC Group	2.3	2.3	(1.7%)	4.1%	(15.7%)	2.7	2.1	0.0%	(7.1%)	0.8x	Sell
HF Group	4.5	4.5	0.2%	5.5%	(29.7%)	6.5	4.0	0.0%	(11.9%)	0.2x	Sell

*Target Prices as per Cytonn Analyst estimates

**Upside/ (Downside) is adjusted for Dividend Yield

***Companies in which Cytonn and/or its affiliates are invested in

We are "Neutral" on equities for investors because, despite the sustained price declines, which have seen the market P/E decline to below its historical average presenting investors with attractive valuations in the market, the economic outlook remains grim.

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