

# Cytonn Q3'2020 Markets Review

## Equities

### Markets Performance

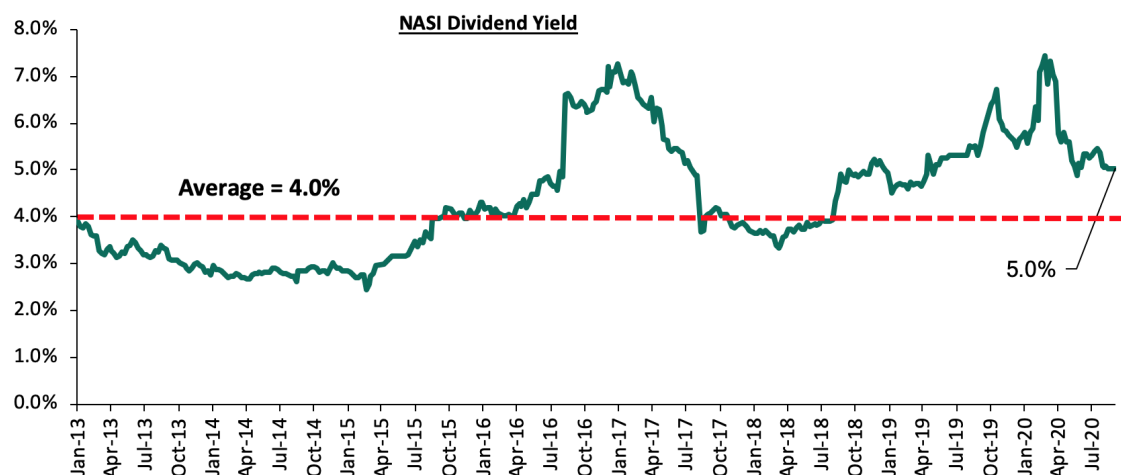
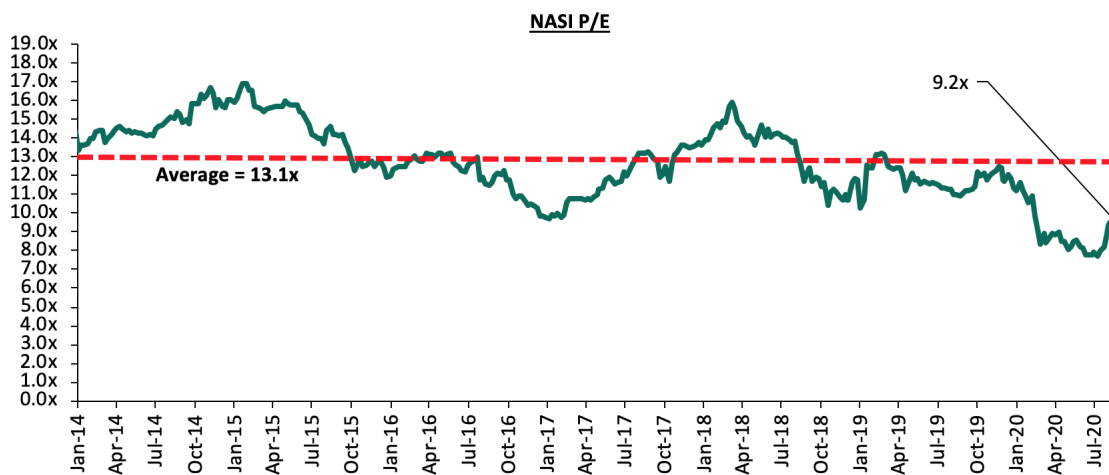
In Q3'2020, the equities market recorded mixed performance, with NASI and NSE 25 gaining by 1.6% and 1.3%, respectively, while NSE 20 declined by 4.6%. The equities market performance during the quarter was driven by gains recorded large caps such as BAT, KCB, Equity Group and EABL, which gained by 9.5%, 7.6%, 5.8% and 4.2%, respectively. The gain was however weighed down by losses recorded by other large cap stocks such as Bamburi, Diamond Trust Bank (DTB-K) and NCBA, which declined by 15.9%, 15.2% and 13.4%, respectively.

During the week, the equities market recorded mixed performances, with NSE 20 recording marginal gains of 0.3% while NASI declined by 0.1%. NSE 25 on the other hand, remained unchanged from the previous week. This week's performance takes the indices YTD performance to losses of 15.7%, 30.2%, and 20.9%, for NASI, NSE 20 and NSE 25, respectively. The NASI performance was driven by losses recorded by large-cap stocks such as ABSA, EABL and Co-operative Bank, which declined by 2.0%, 1.8% and 1.7%, respectively. The decline was however mitigated by gains recorded by other large-cap stocks such as Diamond Trust Bank and Standard Chartered Bank of 2.1% and 0.8%, respectively.

In Q3'2020, equities turnover declined by 5.4% to USD 350.4 mn from USD 370.2 mn in Q2'2020. Foreign investors remained net sellers during the quarter with a net selling position of USD 40.6 mn from a net selling position of USD 91.2 mn in Q2'2020. During the week, equities turnover declined by 55.7% to USD 14.0 mn, from USD 31.7 mn recorded the previous week, taking the YTD turnover to USD 1.2 bn. Foreign investors remained net sellers during the week, with a net selling position of USD 2.8 mn, from a net selling position of USD 3.6 mn recorded the previous week, taking the YTD net selling position to USD 257.2 mn.

The market is currently trading at a price to earnings ratio (P/E) of 9.2x, 29.4% below the 11-year historical average of 13.0x. The average dividend yield is currently at 5.0%, unchanged from the previous week and 1.0% 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 9.2x is 19.2% above the most recent valuation trough of 7.7x experienced in the first week of August 2020. The charts below indicate the historical P/E and dividend yields of the market.



During the third quarter of 2020, listed banks in Kenya released their H1'2020 results, recording a decline in their earnings growth, with their core EPS declining by 33.6%.

### Listed Banks H1'2020 Highlights:

The table below highlights the performance of the banking sector, showing the performance using several metrics, and the key take-outs of the performance.

| 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                               | (84.8%)         | 0.9%                   | (3.3%)                  | 2.5%                       | 7.3%                | 4.2%                     | 32.8%                         | 4.1%                               | 8.3%           | 17.4%                           | 81.2%                 | 8.2%         | 15.9%                    |
| KCB                                | (40.4%)         | 23.2%                  | 25.7%                   | 22.3%                      | 7.6%                | 6.0%                     | 31.0%                         | 4.3%                               | 34.6%          | 54.5%                           | 73.8%                 | 17.0%        | 16.0%                    |
| NCBA                               | (38.3%)         | 9.6%                   | 7.7%                    | 11.2%                      | 3.4%                | 28.0%                    | 47.3%                         | 61.3%                              | 9.1%           | 24.0%                           | 63.6%                 | 4.0%         | 8.9%                     |
| DTBK                               | (36.5%)         | (3.3%)                 | (9.0%)                  | 1.2%                       | 5.6%                | 5.9%                     | 25.3%                         | 24.2%                              | (0.1%)         | 9.8%                            | 75.2%                 | 5.6%         | 9.8%                     |
| SCBK                               | (31.3%)         | (6.3%)                 | (12.1%)                 | (4.6%)                     | 6.9%                | 6.6%                     | 31.9%                         | (5.2%)                             | 12.3%          | 2.1%                            | 52.4%                 | 11.9%        | 13.7%                    |
| Stanbic                            | (31.2%)         | (4.8%)                 | (3.1%)                  | (0.7%)                     | 4.5%                | (18.8%)                  | 44.0%                         | (36.7%)                            | 20.6%          | (13.4%)                         | 81.9%                 | 32.8%        | 10.9%                    |
| I&M                                | (29.5%)         | 3.4%                   | 9.4%                    | (1.4%)                     | 5.5%                | (7.1%)                   | 37.8%                         | 7.7%                               | 6.4%           | 30.1%                           | 73.1%                 | 7.2%         | 15.4%                    |
| Equity                             | (24.4%)         | 18.5%                  | 23.6%                   | 16.9%                      | 8.1%                | (13.0%)                  | 36.9%                         | (10.8%)                            | 18.6%          | 24.2%                           | 72.0%                 | 22.0%        | 17.5%                    |
| Co-op                              | (3.6%)          | 6.8%                   | (4.4%)                  | 11.6%                      | 8.4%                | (5.1%)                   | 34.3%                         | (42.5%)                            | 18.9%          | 28.8%                           | 70.8%                 | 5.7%         | 18.6%                    |
| HF Group                           | N/A             | (12.7%)                | (18.20%)                | (3.9%)                     | 4.3%                | (68.8%)                  | 22.4%                         | 42.1%                              | 15.8%          | 13.5%                           | 97.4%                 | (5.8%)       | (3.0%)                   |
| <b>H1'20 Mkt Weighted Average*</b> | <b>(33.6%)</b>  | <b>10.4%</b>           | <b>10.0%</b>            | <b>10.9%</b>               | <b>7.0%</b>         | <b>(1.1%)</b>            | <b>35.2%</b>                  | <b>(3.4%)</b>                      | <b>18.5%</b>   | <b>25.9%</b>                    | <b>71.5%</b>          | <b>14.5%</b> | <b>15.4%</b>             |

| 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 |
|-----------------------------|-----------------|------------------------|-------------------------|----------------------------|---------------------|--------------------------|-------------------------------|------------------------------------|----------------|---------------------------------|-----------------------|-------------|--------------------------|
| H1'19Mkt Weighted Average** | 9.0%            | 3.7%                   | 5.3%                    | 3.8%                       | 7.7%                | 16.5%                    | 37.2%                         | 12.7%                              | 8.6%           | 12.1%                           | 73.8%                 | 9.8%        | 19.3%                    |

\*Market-cap-weighted as at 28/08/2020

\*\*Market-cap-weighted as at 06/09/2019

### Key takeaways from the table above include:

1. For the first half of 2020, the core Earnings Per Share (EPS) declined by (33.6%) as compared to a 9.0% growth in H1'2019,
2. The sector recorded a deposit growth of 18.5% up from the 8.6% growth recorded in H1'2019. Interest expense, on the other hand, grew faster by 10.0%, compared to 5.3% in H1'2019. Cost of funds, however, declined, coming in at a weighted average of 2.9% in H1'2020, from 3.0% in H1'2019, an indication that the sector was able to mobilize cheaper deposits,
3. Average loan growth came in at 14.5%, which was faster than the 9.8% recorded in H1'2019, but slower than the 25.9% growth in government securities, an indication of the banks preference of investing in government securities compared to lending to individuals and businesses,
4. Interest income rose by 10.4%, compared to a growth of 3.7% recorded in H1'2019. The faster growth in interest income may be attributable to the 16.1% growth in loans and increased allocation to government securities. Despite the rise in interest income, the Yield on Interest Earning Assets (YIEA) declined to 9.7% from the 10.4% recorded in H1'2019, an indication of the increased allocation to lower-yielding government securities by the sector. The decline in the YIEA can also be attributed to the reduced lending rates for customers by the sector, in line with the Central Bank Rate cuts. Consequently, the Net Interest Margin (NIM) now stands at 7.0%, compared to the 7.7% recorded in H1'2019 for the listed banking sector, and,
5. Non-Funded Income declined by 1.1% y/y, slower than 16.5% growth recorded in H1'2019. The performance in NFI was on the back of declined growth in fees and commission of 3.4%, which was slower than the 12.7% growth recorded in H1'2019. The slow growth in fees and commission can be attributed to the recent waiver on fees on mobile transactions below Kshs 1,000 and the free bank-mobile money transfer. Banks with a large customer base who rely heavily on mobile money transactions are likely to take the biggest hit.

### Quarterly Highlights:

During the quarter:

- i. Equity Group disclosed it was seeking to raise up to Kshs 50.0 bn in long-term debt from international financiers in the next three years as it seeks to boost its liquidity and capital positions. This is reflective of the trend by local banks, which are increasingly seeking loans from global financiers such as the International Finance Corporation (IFC) and European Investment Bank. For more information, please see [Cytonn Weekly #29/2020](#),
- ii. I&M Holdings PLC issued a cautionary statement to its shareholders on its intention to acquire 90.0% share capital of Orient Bank Limited Uganda (OBL). The transaction will see I&M spend more than Kshs 2.0 bn in the acquisition of the Ugandan Bank, whose book value stood at Ushs 114.1 bn (Kshs 3.3 bn) in FY'2019. For more information, please see [Cytonn Weekly #30/2020](#),
- iii. Equity Group Holdings completed the 66.5% stake acquisition of the Banque Commerciale Du Congo (BCDC) at a cost of USD 95.0 mn (Kshs 10.3 bn). The acquisition was first announced by the group on 18th November 2019 and was subject to approvals from the Central Bank of Kenya (CBK), Democratic Republic of Congo's Central Bank, and the COMESA Competition Commission. Initially, the deal was to cost USD 105.0 mn (Kshs 11.4 bn), however factoring in the adverse effects of the COVID-19 pandemic on the two economies, the two parties agreed to reduce the amount to USD 95.0 mn (Kshs 10.3 bn). For more information, please see [Cytonn Weekly #33/2020](#),

- iv. Co-operative Bank Kenya completed the 90.0% acquisition of Jamii Bora Bank. As highlighted in our **Cytonn Weekly #32/2020**, the Central Bank of Kenya approved the acquisition of a 90.0% stake of Jamii Bora's shareholding by Co-operative Bank, which was to be completed on 21st August 2020 after the deal received all regulatory approvals following approval by the National Treasury on 4th August 2020. For more information, please see **Cytonn Weekly #35/2020**,
- v. The Central Bank of Kenya (CBK), directed that banks will have to get approval before declaring dividends for the current financial year, in a bid to ensure that the banks have enough capital that will enable them to respond appropriately to the COVID-19 pandemic. The CBK has given guidance to lenders asking them to revise their ICAAP (Internal Capital Adequacy Assessment Process) based on the pandemic. For more information, please see **Cytonn Weekly #35/2020**,
- vi. The Capital Markets Authority (CMA) granted African Diaspora Asset Managers (ADAM) Ltd a fund Manager's License. In the statement by CMA, the fund manager will offer financial products and services such as asset management, wealth management, unit trusts, discretionary portfolio management, etc. and will target clients in the Kenyan markets as well as Africans in the diaspora. This will bring the total number of licensed fund managers to 25. For more information, please see **Cytonn Weekly #37/2020**,
- vii. The Capital Markets Authority (CMA) published guidelines to Collective Investments Schemes on the valuation, performance measurement and reporting. CMA highlighted that given the inconsistencies in the performance measurement and presentation by the fund managers, there was a need for standardization by the Collective Investment Schemes in order to enhance the comparability and consistency of the information presented across the sector. The guidance will be applicable to all approved Collective Investment Schemes and will take effect on 1st January 2021. For more information, please see **Cytonn Weekly #38/2020**

### Weekly Highlights:

During the week, Jubilee Holdings Limited disclosed that it had entered into an agreement with Allianz Africa Holding, one of the world's leading insurers and asset managers, to establish a strategic partnership in regards to Jubilee's short-term insurance business operations in its countries of operations. In the **press release**, Jubilee discloses that Allianz will acquire a controlling stake ranging from 51.0% - 66.0% in each of Jubilee's operating subsidiaries engaged in short-term general insurance in Kenya, Uganda, Tanzania, Burundi and Mauritius. The total net consideration for the transaction will be Kshs 10.8 bn of which Kshs 7.8 bn will be received by Jubilee Holdings. Key to note, the transaction does not include Jubilee's Life business or Medical Insurance Business in Kenya, Uganda and Tanzania. Following the transaction, Jubilee will be a minority stake holder in each of the acquired subsidiaries. As of H1'2020, the general insurance subsidiaries contributed Kshs 4.0 bn to the group's total assets, and as such, this transaction will translate to a trading multiple of 2.7x Price to Book. The proposed transaction will be subject to Jubilee's shareholders' approval, regulatory approval in the 5 countries i.e. Kenya, Tanzania, Uganda, Burundi and Mauritius as well as the completion of the restructuring of the Ugandan and Tanzanian entities. In our view, the partnership is a commendable move by Jubilee as this will see the group broaden its insurance markets across Africa and also leverage on Allianz's expertise in the insurance industry. Additionally, we believe that the Kshs 7.8 bn receivable by Jubilee from the transaction will see Jubilee invest the cash in the expansion of its business in line with its corporate strategy of offering innovative, affordable and technically advanced products to the market.

### Universe of Coverage:

| Company                      | Price at 25/09/2020 | Price at 02/10/2020 | w/w change | q/q change | YTD Change | Year Open | Target Price* | Dividend Yield | Upside/Downside** | P/TBv Multiple | Recommendation |
|------------------------------|---------------------|---------------------|------------|------------|------------|-----------|---------------|----------------|-------------------|----------------|----------------|
| <b>Diamond Trust Bank***</b> | 60.0                | 61.3                | 2.1%       | (15.2%)    | (43.8%)    | 109.0     | 119.4         | 3.9%           | 98.9%             | <b>0.3x</b>    | <b>Buy</b>     |

| Company               | Price at 25/09/2020 | Price at 02/10/2020 | w/w change | q/q change | YTD Change | Year Open | Target Price* | Dividend Yield | Upside/Downside** | P/TBv Multiple | Recommendation |
|-----------------------|---------------------|---------------------|------------|------------|------------|-----------|---------------|----------------|-------------------|----------------|----------------|
| Kenya Reinsurance     | 2.3                 | 2.4                 | 3.0%       | 12.1%      | (20.8%)    | 3.0       | 4.0           | 4.6%           | 71.3%             | 0.2x           | Buy            |
| Sanlam                | 13.1                | 12.5                | (4.6%)     | (3.7%)     | (27.3%)    | 17.2      | 18.4          | 0.0%           | 47.2%             | 1.2x           | Buy            |
| I&M Holdings***       | 44.4                | 43.6                | (1.9%)     | (11.5%)    | (19.4%)    | 54.0      | 57.8          | 5.1%           | 37.8%             | 0.7x           | Buy            |
| NCBA***               | 23.1                | 22.7                | (1.7%)     | (13.4%)    | (38.5%)    | 36.9      | 30.7          | 1.0%           | 36.5%             | 0.6x           | Buy            |
| KCB Group***          | 38.9                | 38.5                | (1.0%)     | 7.6%       | (28.7%)    | 54.0      | 46.4          | 9.9%           | 30.4%             | 0.8x           | Buy            |
| Standard Chartered*** | 159.8               | 161.0               | 0.8%       | (5.7%)     | (20.5%)    | 202.5     | 197.2         | 7.8%           | 30.3%             | 1.2x           | Buy            |
| Co-op Bank***         | 11.9                | 11.7                | (1.7%)     | (2.5%)     | (28.4%)    | 16.4      | 14.2          | 8.4%           | 29.8%             | 0.8x           | Buy            |
| Equity Group***       | 36.1                | 36.0                | (0.4%)     | 5.8%       | (32.8%)    | 53.5      | 44.5          | 5.9%           | 29.7%             | 0.9x           | Buy            |
| Liberty Holdings      | 7.8                 | 7.6                 | (2.1%)     | (5.0%)     | (26.4%)    | 10.4      | 9.8           | 0.0%           | 28.6%             | 0.6x           | Buy            |
| ABSA Bank***          | 10.0                | 9.8                 | (2.0%)     | (1.8%)     | (26.6%)    | 13.4      | 10.8          | 12.0%          | 22.2%             | 1.2x           | Buy            |
| Britam                | 7.2                 | 7.4                 | 2.5%       | (2.1%)     | (17.6%)    | 9.0       | 8.6           | 3.3%           | 19.2%             | 0.8x           | Accumulate     |
| Stanbic Holdings      | 76.0                | 80.0                | 5.3%       | (3.3%)     | (26.8%)    | 109.3     | 84.9          | 9.0%           | 15.1%             | 0.6x           | Accumulate     |
| Jubilee Holdings      | 220.0               | 291.8               | 32.6%      | 0.0%       | (16.9%)    | 351.0     | 313.8         | 3.6%           | 11.1%             | 0.5x           | Accumulate     |
| HF Group              | 4.0                 | 4.0                 | (0.5%)     | (10.0%)    | (38.2%)    | 6.5       | 4.1           | 0.0%           | 2.8%              | 0.2x           | Lighten        |
| CIC Group             | 2.1                 | 2.2                 | 5.8%       | (7.9%)     | (18.3%)    | 2.7       | 2.1           | 0.0%           | (4.1%)            | 0.7x           | Sell           |

\*Target Prices as per Cytonn Analyst estimates

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

\*\*\*For disclosure, there are banks 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.*

Liason House, StateHouse Avenue  
The Chancery, Valley Road  
www.cytonn.com  
Generated By Cytonn Report

A product of Cytonn Technologies