

Unit Trust Fund Performance FY'2020, & Cytonn Weekly #18/2021

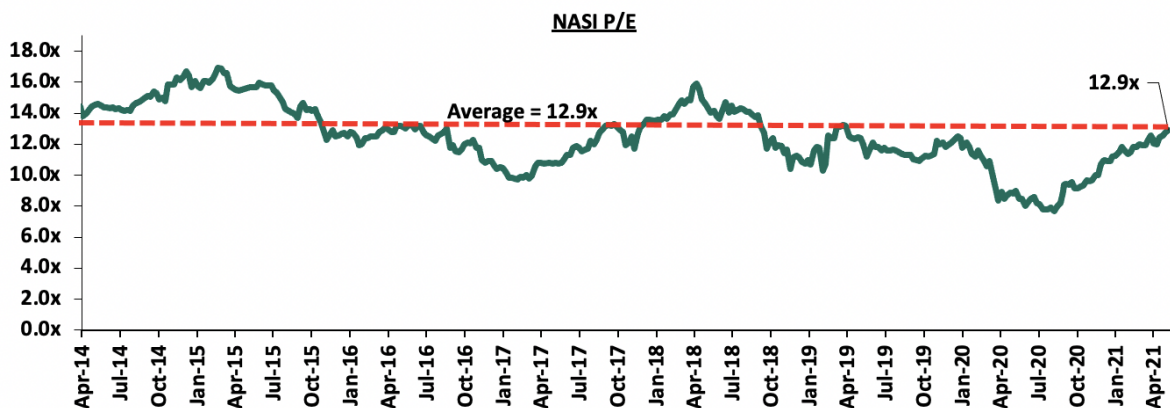
Equities

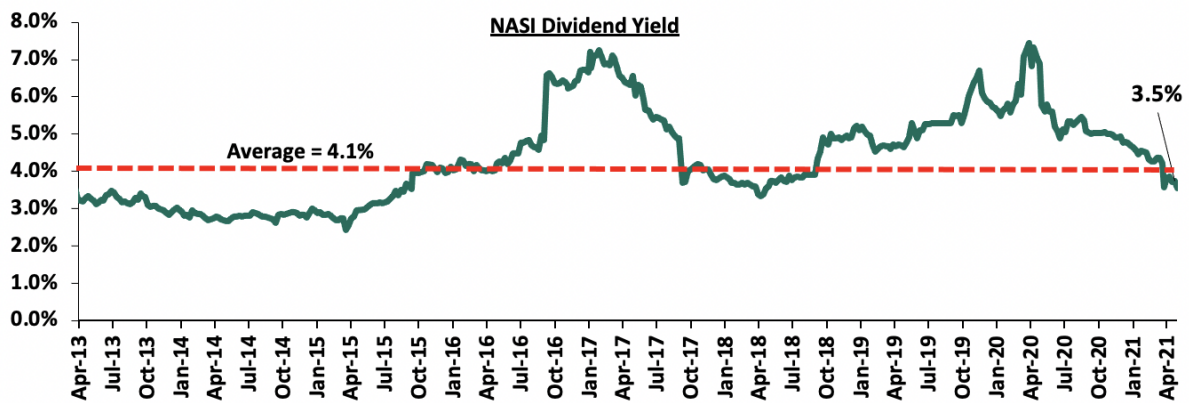
Markets Performance

During the week, the equities market recorded mixed performance, with NASI and NSE 25 gaining by 1.1% and 1.4% respectively, while NSE 20 declined marginally by 0.2%, taking their YTD performance to gains of 12.5% and 9.3% for NASI and NSE 25, respectively, and a loss of 0.5% for NSE 20. The equities market performance was driven by gains recorded by large-cap stocks such as KCB Group, Equity Group, Co-operative Bank and BAT of 4.2%, 4.1%, 3.3% and 3.0%, respectively. The gains were however weighed down by losses recorded by stocks such as Bamburi, Standard Chartered Bank, Diamond Trust Bank (DTB-K) and NCBA Group which declined by 2.5%, 1.7%, 1.5% and 1.4%, respectively.

During the week, equities turnover increased by 9.9% to USD 24.9 mn, from USD 22.7 mn recorded the previous week, taking the YTD turnover to USD 404.9 mn. Foreign investors remained net buyers, with a net buying position of USD 6.8 mn, from a net buying position of USD 8.6 mn recorded the previous week, taking the YTD net selling position to USD 2.4 mn.

The market is currently trading at a price to earnings ratio (P/E) of 12.87x, 0.3% below the historical average of 12.91x, and a dividend yield of 3.5%, 0.6% points below the historical average of 4.1%. The current NASI P/E of 12.9x is the highest it has been since March 2019. Key to note, NASI's PEG ratio currently stands at 1.4x, an indication that the market is trading at a premium to its future earnings growth. Basically, a PEG ratio greater than 1.0x indicates the market may be overvalued while a PEG ratio less than 1.0x indicates that the market is undervalued. The current P/E valuation of 12.9x is 67.1% above the most recent trough valuation 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.





Weekly Highlight:

?. CBK Credit Survey Report - Q1'2021

During the week, the Central Bank of Kenya (CBK), released the **Commercial Banks' Credit Survey Report** for the quarter ended March 2021. The quarterly Credit Officer Survey is undertaken by the CBK to identify the potential drivers of credit risk in the banking sector. For the quarter ended 31st March 2021, 38 operating commercial banks and 1 mortgage finance company participated in the Commercial Banks Credit Officer Survey. The report highlights that Profit Before Tax (PBT) for the banking sector increased by 19.7% y/y to Kshs 45.9 bn in Q1'2021, from Kshs 38.3 bn in Q1'2020, attributable to the recovery of the economy as restrictions had since been eased, especially on travel and curfew times, leading to an improved business environment. Other key take-outs from the report include:

- i. The banking sector's loan book recorded a 6.8% y/y growth, with gross loans increasing to Kshs 3.04 tn in March 2021, from Kshs 2.85 tn in March 2020. On a q/q basis, the loan book increased by 1.4% from Kshs 3.00 tn in December 2020,
- ii. The aggregate balance sheet recorded a 10.5% increase y/y to Kshs 5.5 tn in Q1'2021, from Kshs 5.0 tn in Q1'2020, attributable to a 12.1% growth in deposits to Kshs 4.1 tn in Q1'2021, from Kshs 3.7 tn in Q1'2020, coupled with a 6.8% increase in gross loans to Kshs 3.0 tn in March 2021, from Kshs 2.8 tn in March 2020. Quarterly, the balance sheet grew by 2.0% to Kshs 5.5 tn in March 2021, from Kshs 5.4 tn in December 2020,
- iii. Asset quality in the banking sector deteriorated, with the Gross NPL ratio increasing to 14.6% in Q1'2021, from 12.5% in Q1'2020 and 14.1% in Q4'2020. Some the key sectors adversely affected include Personal and Household, Real Estate, Transport and Communication, Tourism, and Trade,
- iv. The capital adequacy remained okay with the ratio increasing to 18.9%, from 18.5% recorded in March 2020 and 19.2% in December 2020. During the quarter, the total capital increased by 1.0% and the total risk weighted assets increased by 2.7% bringing the capital adequacy ratio to 18.9%, 4.4% points above the minimum statutory limit of 14.5%,
- v. IFRS 9 implementation had an adverse effect on the banking sector's capital adequacy as a result of increased provisioning due to the challenging business environment. Commercial banks have therefore injected additional capital to accommodate the expected increase in credit losses. Direct capital injection increased by 7.0% in Q1'2021, and,
- vi. Average liquidity in the banking sector increased to 56.3% in March 2021, from 51.5% in March 2020 and 54.6% in December 2020. This was 36.3% points above the minimum statutory ratio of 20.0%. The increased liquidity led to a 54.0% quarterly drop in interbank activity and was supported by a 47.0% increase in deposits, 24.0% in government securities maturities, 18.0% loan recovery and 7.0% direct capital injection.

Despite the CBK's efforts to cushion the sector against any pandemic related shocks, credit risk remained elevated and with the lock-downs in April, the situation could have worsened. As per our FY'2020 Banking Sector Report, we expect the banking sector to continue over-provisioning albeit at a slower rate than in 2020. Additionally, we expect the sector will continue to remain resilient having implemented tightened credit standards on granting of new loans coupled with the expiry of the emergency measures on loan restructuring for borrowers, and the removal of the waiver of fees on bank transfers which will, in turn, increase the sector's profitability.

B. I&M Holdings PLC Acquisition of Oriental Bank Uganda

During the week, I&M Holdings PLC announced that it has completed the 90.0% acquisition of Orient Bank Limited Uganda (OBL) share capital, after receiving all the required regulatory approvals. As highlighted in our Cytonn Weekly #50/2020, I&M Holdings was set to pay Kshs 3.6 bn for the deal; which translated to a Price to Book Value (P/Bv) of 1.1x. The valuation of 1.1x P/Bv is 0.1x lower than the 7-year average which is at 1.2x P/Bv, but higher than the last one-year average, which is at 0.7x P/Bv and the average P/Bv in the listed banking stocks of 0.8x. Additionally, I&M Holdings will take over 14 branches from OBL, taking its total branches to 80, from 66 branches as at the end of 2020. Below is a table showing the combined pro-forma financials for the banks:

Combined Pro forma Balance Sheet (Kshs bn)

Balance Sheet	I&M Holdings FY'2020	Orient Bank Ltd*	Combined Entity
Net Loans	187.4	7.7	195.1
Total Assets	358.1	23.0	381.1
Customer Deposits	262.7	18.2	280.9
Number of Branches	66	14	80

**Orient Bank Figures as at December 2019 apart from Loans and Deposits which are as reported on 3rd April 2021*

In our view, the diversification into the Ugandan market will see I&M Holdings reduce its reliance on the Kenyan Market. We believe that Uganda will continue to attract more Kenyan banks given its attractive interest rate spread which stood at 10.5% in 2018, higher than Tanzania's 9.2% and Kenya's 4.8% over the same period. Currently, banks such as KCB Group, Equity Group and DTB Group have ventured into the Ugandan market, making I&M Holdings the fourth Kenyan bank to tap into the market.

Below is a summary of the deals in the last 7-years that have either happened, been announced or expected to be concluded:

Acquirer	Bank Acquired	Book Value at Acquisition (Kshs bn)	Transaction Stake	Transaction Value (Kshs bn)	P/Bv Multiple	Date
I&M Holdings PLC	Orient Bank Limited Uganda	3.3	90.0%	3.6	1.1x	April-21
KCB Group	Banque Populaire du Rwanda	5.2	62.1%	5.7	1.1x	Nov-20*
KCB Group	ABC Tanzania	Unknown	100.0%	Undisclosed	0.4x	Nov-20*

Acquirer	Bank Acquired	Book Value at Acquisition (Kshs bn)	Transaction Stake	Transaction Value (Kshs bn)	P/Bv Multiple	Date
Co-operative Bank	Jamii Bora Bank	3.4	90.0%	1	0.3x	Aug-20
Commercial International Bank	Mayfair Bank Limited	1	51.0%	Undisclosed	N/D	May-20*
Access Bank PLC (Nigeria)	Transnational Bank PLC.	1.9	100.0%	1.4	0.7x	Feb-20*
Equity Group **	Banque Commerciale Du Congo	8.9	66.5%	10.3	1.2x	Nov-19*
KCB Group	National Bank of Kenya	7	100.0%	6.6	0.9x	Sep-19
CBA Group	NIC Group	33.5	53%:47%	23	0.7x	Sep-19
Oiko Credit	Credit Bank	3	22.8%	1	1.5x	Aug-19
CBA Group**	Jamii Bora Bank	3.4	100.0%	1.4	0.4x	Jan-19
AfricInvest Azure	Prime Bank	21.2	24.2%	5.1	1.0x	Jan-18
KCB Group	Imperial Bank	Unknown	Undisclosed	Undisclosed	N/A	Dec-18
SBM Bank Kenya	Chase Bank Ltd	Unknown	75.0%	Undisclosed	N/A	Aug-18
DTBK	Habib Bank Kenya	2.4	100.0%	1.8	0.8x	Mar-17
SBM Holdings	Fidelity Commercial Bank	1.8	100.0%	2.8	1.6x	Nov-16
M Bank	Oriental Commercial Bank	1.8	51.0%	1.3	1.4x	Jun-16
I&M Holdings	Giro Commercial Bank	3	100.0%	5	1.7x	Jun-16
Mwalimu SACCO	Equatorial Commercial Bank	1.2	75.0%	2.6	2.3x	Mar-15
Centum	K-Rep Bank	2.1	66.0%	2.5	1.8x	Jul-14
GT Bank	Fina Bank Group	3.9	70.0%	8.6	3.2x	Nov-13
Average			76.7%		1.2x	

* Announcement Date

** Deals that were dropped

Universe of Coverage

Below is a summary of our universe of coverage and the recommendations:

Company	Price at 07/5/2021	w/w change	YTD Change	Target Price*	Dividend Yield	Upside/Downside**	P/TBv Multiple	Recommendation
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Company	Price at 07/5/2021	w/w change	YTD Change	Target Price*	Dividend Yield	Upside/Downside**	P/TBv Multiple	Recommendation
I&M Holdings***	42.6	(3.3%)	(5.0%)	59.5	5.3%	45.0%	0.6x	Buy
Kenya Reinsurance	2.4	(3.2%)	3.5%	3.3	4.2%	42.3%	0.3x	Buy
Standard Chartered***	131.8	(1.7%)	(8.8%)	164.4	8.0%	32.8%	0.9x	Buy
Diamond Trust Bank***	64.3	(1.5%)	(16.3%)	84.3	0.0%	31.2%	0.3x	Buy
Liberty Holdings	7.6	2.7%	(1.6%)	9.8	0.0%	29.3%	0.6x	Buy
Stanbic Holdings	81.0	(2.4%)	(4.7%)	99.4	4.7%	27.4%	0.8x	Buy
Britam	7.0	3.9%	0.0%	8.6	0.0%	22.9%	1.3x	Buy
Sanlam	11.5	0.0%	(11.5%)	14.0	0.0%	21.7%	1.0x	Buy
NCBA***	24.6	(1.4%)	(7.5%)	28.4	6.1%	21.5%	0.6x	Buy
Equity Group***	40.8	4.1%	12.4%	49.5	0.0%	21.5%	1.3x	Buy
KCB Group***	42.0	4.2%	9.2%	49.8	2.4%	21.1%	1.0x	Buy
ABSA Bank***	8.8	(0.2%)	(8.0%)	10.2	0.0%	16.4%	1.0x	Accumulate
Co-op Bank***	12.6	3.3%	0.4%	13.6	7.9%	15.9%	0.9x	Accumulate
Jubilee Holdings	284.8	1.1%	3.3%	313.8	3.2%	13.3%	0.6x	Accumulate
HF Group	3.7	(7.3%)	17.2%	3.8	0.0%	3.3%	0.2x	Lighten
CIC Group	2.2	(0.5%)	2.8%	2.1	0.0%	(3.2%)	0.7x	Sell

We are “Neutral” on the Equities markets in the short term. With the market currently trading at a premium to its future growth (PEG Ratio at 1.4x), we believe that investors should reposition towards companies with a strong earnings growth and are trading at discounts to their intrinsic value. Additionally, we expect the recent discovery of new strains of COVID-19 coupled with the introduction of strict lockdown measures in major economies to continue dampening the economic outlook.

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