Cytonn Monthly - May 2021

Equities

Markets Performance

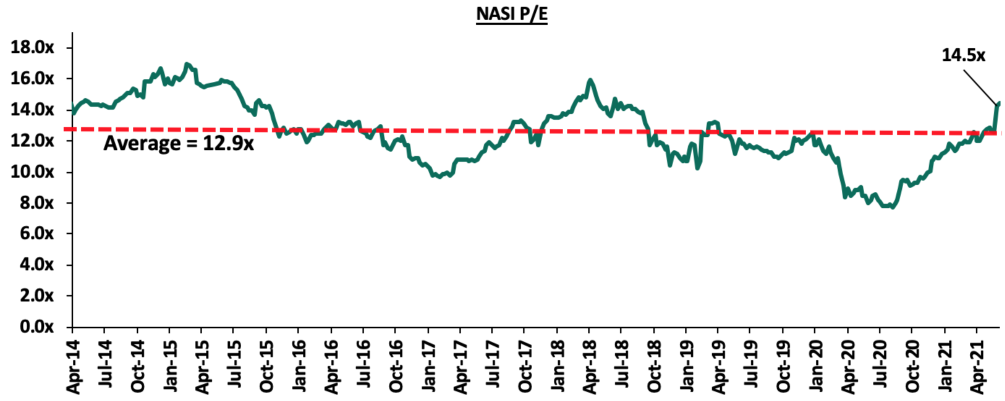
During the month of May, the equities market recorded mixed performance, with NASI and NSE 20 gaining by 0.5% and 0.3%, respectively, while NSE 25 declined by 0.1%. The equities market performance was driven by gains recorded by large cap stocks such as EABL, ABSA Bank Kenya, Equity Group and KCB Group, which gained by 9.1%, 8.0%, 7.8%, and 5.1% respectively. The gains were however weighed down by losses recorded by stocks such as Bamburi, Diamond Trust Bank Kenya (DTB-K) and Standard Chartered Bank Kenya, which declined by 10.5%, 8.0%, and 3.0%, respectively.

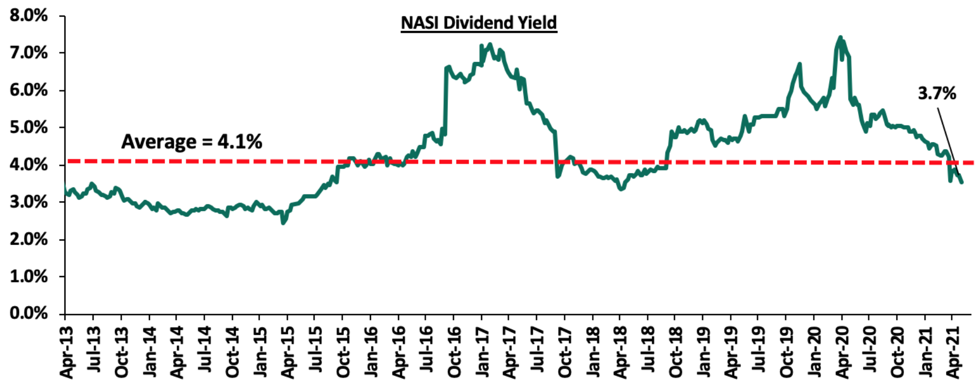
During the week, the equities market recorded mixed performance, with the NSE 20 gaining by 2.5%, while NASI and NSE 25 declined by 1.6% and 0.6%, respectively, taking their YTD performance to gains of 1.9%, 11.7% and 8.3% for NSE 20, NASI and NSE 25, respectively. The equities market performance was mainly driven by gains recorded by large-cap stocks such as Bamburi, ABSA Bank Kenya and NCBA Group of 9.5%, 2.7%, and 2.6%, respectively. The gains were however weighed down by losses recorded by large-cap stocks such as Safaricom which declined by 3.2%.

Equities turnover increased by 44.3% during the month to USD 131.9 mn, from USD 91.4 mn recorded in April 2021. Foreign investors remained net sellers during the month, with a net selling position of USD 7.3 mn, compared to April’s net selling position of USD 0.3 mn.

During the week, equities turnover decreased by 53.6% to USD 21.5 mn, from USD 46.3 mn recorded the previous week, taking the YTD turnover to USD 530.8 mn. Foreign investors turned net sellers, with a net selling position of USD 1.7 mn, from a net buying position of USD 7.2 mn recorded the previous week, taking the YTD net selling position to USD 17.5 mn.

The market is currently trading at a price to earnings ratio (P/E) of 14.5x, 12.0% above the historical average of 12.9x, and a dividend yield of 3.7%, 0.4% points below the historical average of 4.1%. Key to note, NASI’s PEG ratio currently stands at 1.6x, 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. Excluding Safaricom, the market is trading at a P/E ratio of 12.6x and a PEG ratio of 1.4x. The current P/E valuation of 14.5x is 87.8% 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.





Monthly Highlights:

- **Safaricom Plc announced that the Ethiopian Communications Authority (ECA) had approved a bid for an Ethiopia Telco License which was submitted by a consortium consisting of Safaricom, Vodacom Group Ltd, Vodafone Group Plc (UK), CDC Group Plc and Sumitomo Corporation. The consortium's financial bid of USD 850.0 mn (Kshs 91.8 bn) will allow the consortium to operate a telecommunications network in Ethiopia, but will not include a license to operate mobile money. For more information, please see Cytonn Weekly#21/2021,**

- In May 2021, Equity Group disclosed that it had acquired an additional 7.7% stake valued at Kshs 996.0 mn, in Equity bank Congo (EBC) from the German Sovereign Wealth Fund (KfW). The acquisition raised the total ownership in EBC to 94.3%, indicating that they are currently valuing the company at Kshs 14.2 bn. This follows the recent acquisition of 66.5% stake in Banque Commerciale Du Congo (BCDC) by Equity Group at a cost of Kshs 10.2 bn in August 2020. For more information, please see Cytonn Weekly#20/2021,
- KCB Group disclosed that it had made an offer to the Banque Populaire du Rwanda Plc (BPR) shareholders to raise its acquisition stake in the bank from 62.1% to 100.0%. As highlighted in our Cytonn Weekly #48/2020, the 62.1% BPR acquisition would see KCB pay a cash consideration based on the net asset value of the BPR at completion of the transaction using a price to book multiple of 1.1x. According to the latest BPR financials, the bank had a book value of Rwf 47.3 bn (Kshs 5.1 bn), and thus at the trading multiple of 1.1x, we expect KCB Group to pay Kshs 5.6 bn. Collectively, KCB will spend a total of USD 56.9 mn (Kshs 6.1 bn) in the acquisition of Banque Populaire du Rwanda Plc (BPR) Rwanda and African Banking Corporation (ABC) Tanzania. For more information on the acquisition, see our Cytonn Weekly #19/2021,
- I&M Holdings PLC announced that it 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. 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. For more information, please see Cytonn Weekly

#18/2021, and,

- 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. The report highlighted 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. For more information, please see Cytonn Weekly #18/2021.

Earnings Releases:

During the month, the listed banks released their Q1'2021 financial results. The table below highlights the performance of the banks, showing their 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
Stanbic	23.1%	0.5%	(7.3%)	5.0%	6.1%	19.3%	46.7%	(8.5%)	10.6%	42.3%	69.5%	(2.4%)	13.2%
KCB	1.8%	8.7%	1.8%	11.1%	8.4%	(20.0%)	27.4%	(26.5%)	1.2%	4.7%	79.7%	7.8%	13.9%
SCBK	18.9%	(9.0%)	(30.2%)	(2.8%)	6.7%	11.1%	35.1%	11.7%	8.9%	7.8%	44.4%	(6.1%)	11.3%
Equity	63.8%	31.9%	42.4%	28.4%	7.6%	30.7%	42.3%	21.5%	58.2%	16.1%	61.7%	28.6%	18.9%
Co-op	(3.7%)	27.6%	19.8%	30.7%	8.6%	(9.2%)	32.0%	(15.7%)	16.0%	43.4%	75.7%	8.0%	12.3%
DTB-K	0.5%	4.8%	2.9%	6.2%	5.3%	(1.9%)	23.9%	(20.5%)	10.6%	7.9%	68.2%	2.3%	5.7%
ABSA	23.7%	(0.3%)	17.6%	5.9%	7.0%	(3.9%)	32.0%	7.4%	7.7%	1.1%	84.9%	7.5%	13.6%
NCBA	73.8%	8.1%	(5.7%)	19.9%	5.9%	(3.3%)	44.3%	(8.1%)	11.2%	15.1%	56.0%	(1.1%)	8.1%
I&M	13.5%	10.2%	(5.2%)	23.4%	5.4%	(17.7%)	29.7%	(5.3%)	9.3%	89.5%	73.4%	5.6%	13.3%
HF	N/A	(18.7%)	(19.0%)	(18.3%)	4.1%	(46.7%)	22.0%	(36.2%)	(2.1%)	13.4%	96.2%	(6.9%)	(20.4%)
Q1'21 Mkt Weighted Average*	**28.6%**	**14.7%**	**13.1%**	**17.3%**	**7.4%**	**3.3%**	**35.4%**	**(2.5%)**	**22.0%**	**18.2%**	**69.1%**	**11.1%**	**14.1%**
Q1'20 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%**

***Market cap weighted as at 04/06/2021**

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

Key takeaways from the table above include:

i. The listed banks recorded a 28.6% weighted average growth in core Earnings per Share (EPS), compared to a weighted average decline of 7.4% in Q1'2020 for the entire listed banking sector. The performance is largely skewed by the strong performance from NCBA and equity bank,
ii. The Banks have recorded a weighted average deposit growth of 22.0%, faster than the 14.3% growth recorded in Q1'2020,
iii. Interest expense grew at a faster pace of 13.1%, compared to the 11.4% growth in Q1'2020 while cost of funds declined, coming in at a weighted average of 2.5% in Q1'2021, from 3.0% in Q1'2020, owing to the faster growth in average interest-bearing liabilities, an indication that the listed banks were able to mobilize cheaper deposits,
iv. Average loan growth came in at 11.1%, lower than the 14.1% growth recorded in Q1'2020. The loan growth was also slower than the 18.2% growth in government securities, an indication of the banks' preference of investing in Government securities as opposed to lending due to the elevated credit risk occasioned with the pandemic. The faster growth in government securities could also be attributed to cautious lending by banks in a bid to reduce cost of risk as well as mitigate further deterioration of the asset quality,
v. Interest income grew by 14.7%, compared to a growth of 8.2% recorded in Q1'2020. Notably, the Yield on Interest Earning Assets (YIEA) increased to 10.2%, from the 9.8% recorded in Q1'2020, an indication of the increased allocation to higher-yielding government securities by the sector during the period. Consequently, the Net Interest Margin (NIM) now stands at 7.4%, 0.2% points higher than the 7.2% recorded in Q1'2020 for the whole listed banking sector, and,

vi. Non-Funded Income grew by 3.3%, compared to the 15.9% growth recorded in Q1'2020. This can be attributable to a slower growth in the fees and commission which declined by 2.5% compared to a growth of 24.5% in Q1'2020.

Below are links to the various Earnings notes for the Listed Banks;

i. Equity Group Q1'2021 Earnings Note,
ii. KCB Group Q1'2021 Earnings Note,
iii. Co-operative Bank Q1'2021 Earnings Note,
iv. NCBA Group Q1'2021 Earnings Note,
v. Diamond Trust Bank (DTB-K) Q1'2021 Earnings Note,
vi. ABSA Bank Q1'2021 Earnings Note,
vii. I&M Holdings Q1'2021 Earnings Note,
viii. Standard Chartered Bank Kenya Q1'2021 Earnings Note,
ix. Stanbic Bank Q1'2021 Earnings Note, and,
x. HF Group Q1'2021 Earnings Note.

Weekly Highlight:

On 31st May 2021, Nation Media Group (NMG) issued a share buyback circular to shareholders, proposing to buy back of up to 10.0% (20.7 mn shares) of its issued and paid-up share capital in accordance with Part XVI, Section 447 of the Companies Act, 2015 of the laws of Kenya. This would reduce the company's outstanding shares to 186.7 mn shares, from 207.4 mn shares. Key to note, NMG is the first company in the Nairobi Securities Exchange (NSE) to undertake a share repurchase program. The proposed buyback, which will be through the open market, shall be proposed to the company's Annual General Meeting (AGM) that will be held on 25th June 2021 and will be subject to shareholders' approval. The buyback is expected to run from 28th June 2021 to 24th September 2021. The board proposed a minimum buying price of Kshs 2.50, equivalent to the par value of an ordinary share and a maximum buyback price of Kshs 25.00 per share. NMG has gained 47.7% Year to Date to Kshs 22.6 from Kshs 15.3 recorded on 4th January 2021. NMG's profit declined by 94.4% in FY'2020 to Kshs 47.9 mn, from Kshs 862.6 mn recorded in FY'2019 driven by a 26.5% decline in advertising revenue to Kshs 4.4 bn in FY'2020, from Kshs 6.0 bn in FY'2019 coupled with a 23.4% decline in circulation revenue to Kshs 1.8 bn in FY'2020, from Kshs 2.4 bn in FY'2019. Total revenue declined 24.7% to Kshs 5.7 bn in FY'2020 from Kshs 7.2 bn in FY'2019.

Share buybacks have historically led to share price rallies in the stock market due to market perceptions of management's confidence in the company coupled with reduction in the supply of outstanding shares in the market. We therefore expect the share price of NMG to gain further, to a target price of Kshs 25.0, which is the maximum buying price that the firm will be buying back its shares. We also expect NMG's shareholders to approve the share buyback, which will make NMG the first company in the NSE to conduct a share repurchase. More buybacks in the NSE are likely to follow, especially for companies whose prices and valuations are at historical lows. The Capital Markets Authority (CMA) issued guidelines on share buy-backs in June 2020, with the guidelines being in the process of being revised following public participation. In our view, the move by the CMA to issue guidelines on the share buybacks is commendable, and we expect more listed companies to follow NMG's suit and initiate share repurchases if the valuations remain low. For more information on the buyback, please see our Note on Nation Media Group's Share Buyback.

Universe of Coverage

Below is a summary of our universe of coverage and the recommendations. We are currently reviewing our target prices for the Banking Sector coverage:

Company	Price at 28/5/2021	Price at 4/6/2021	w/w change	m/m change	YTD Change	Year Open 2021	Target Price*	Dividend Yield	Upside/ Downside**	P/TBv Multiple	Recommendation
Kenya Reinsurance	2.3	2.5	8.2%	(6.9%)	8.2%	2.3	3.3	4.0%	36.0%	**0.3x**	**Buy**
Jubilee Holdings	280.0	280.0	0.0%	(0.9%)	1.5%	275.8	330.9	3.2%	21.4%	**0.6x**	**Buy**
Liberty Holdings	7.0	7.0	(0.6%)	(4.9%)	(9.1%)	7.7	8.4	0.0%	20.0%	**0.5x**	**Buy**
Sanlam	11.0	10.5	(4.5%)	(4.3%)	(19.2%)	13.0	12.4	0.0%	18.1%	**0.9x**	**Accumulate**
Britam	7.2	7.1	(1.7%)	7.7%	1.7%	7.0	6.7	0.0%	(5.9%)	**1.3x**	**Sell**
CIC Group	2.1	2.1	(3.3%)	(4.6%)	(1.9%)	2.1	1.8	0.0%	(13.0%)	**0.7x**	**Sell**

***Target Price as per Cytonn Analyst estimates**
****Upside/ (Downside) is adjusted for Dividend Yield**
*****For Disclosure, these are stocks in which Cytonn and/or its affiliates are invested in**
We are currently reviewing our target prices for the Banking Sector coverage

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 1.6x), 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.