

Kenya Listed Banks H1'2021 Report, & Cytonn Weekly #36/2021

Equities

Markets Performance

During the week, the equities market was on an upward trajectory, with NSE 20 gaining by 1.9%, while both NASI and NSE 25 gained by 0.4%, taking their YTD performance to gains of 18.5%, 15.8% and 10.2% for NASI, NSE 25 and NSE 20, respectively. The equities market performance was mainly driven by gains recorded by large-cap stocks such as Equity Group, NCBA Group and Safaricom which gained by 2.2%, 1.7% and 0.8%, respectively. The gains were however weighed down by losses recorded by banking stocks such as Diamond Trust Bank (DTB-K) and ABSA Bank, which declined by 1.5% and 1.4%, respectively.

During the week, equities turnover increased by 0.7% to USD 18.2 mn, from USD 18.1 mn recorded the previous week, taking the YTD turnover to USD 862.6 mn. Foreign investors turned net buyers, with a net buying position of USD 2.2 mn, from a net selling position of USD 1.9 mn recorded the previous week, taking the YTD net selling position to USD 9.1 mn.

The market is currently trading at a price to earnings ratio (P/E) of 13.5x, 4.1% above the historical average of 12.9x, and a dividend yield of 3.2%, 0.8% points below the historical average of 4.0%. Key to note, NASI's PEG ratio currently stands at 1.5x, 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, which is currently 61.4% of the market, the market is trading at a P/E ratio of 12.1x and a PEG ratio of 1.4x. The current P/E valuation of 13.5x is 74.8% 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;



Weekly Highlight:

The Insurance Regulatory Authority (IRA), recently released the Q2'2021 Insurance Industry Report highlighting that the industry's gross premiums rose by 19.0% to Kshs 144.0 bn, from Kshs 121.0 bn recorded in Q2'2020, with the general insurance business contributing to 59.3% of the industry's premium income, an 8.5% points increase from the 50.8% contribution witnessed in Q2'2020. The general insurance business has continued to report high underwriting losses mainly attributed to increases in loss ratios as the net claims outpace net premiums.

Other key take-outs from the report include:

- i. Investment income increased significantly by 112.3% to Kshs 26.3 bn in Q2'2021, from Kshs 12.4 bn recorded in Q2'2020 for long term insurance businesses, and also increased by 42.6% for general insurance businesses to Kshs 6.3 bn, from Kshs 4.4 bn recorded in Q2'2020. The increases

can be attributed to fair value gains on quoted equity investments in the capital market as evidenced by the increases in the NASI, NSE 25 and NSE 20 which have posted YTD gains of 18.5%, 15.8% and 10.2% respectively,

- ii. The net claims for the long term insurance business increased by 15.3% to Kshs 39.4 bn, from Kshs 30.6 bn in Q2'2020, mainly driven by increased requests from individuals wishing to access their pension benefits given the reduction in their disposable income. This saw the loss ratio for the long term business increase by 3.4% points to 72.2%, from 68.8% recorded in Q2'2020,
- iii. The loss ratio for the general insurance businesses increased to 66.8% in Q2'2021, from 61.6% in Q2'2020 owing to a 15.3% increase in claims which outpaced the 6.5% increase in the net earned premium income. The increase in claims was mainly driven by the 35.7% growth in domestic fire claims to Kshs 241.6 bn, from Kshs 178.1 bn in Q2'2020. Key to note, the incurred loss ratio during the quarter of 66.8% is 2.6% points higher than the three-year industry average of 64.2%, and,
- iv. General insurance businesses recorded an underwriting loss of Kshs 1.5 bn in Q2'2021 as compared to a profit of Kshs 62.5 mn in Q2'2020. This increased loss was mainly driven by a 197.1% increase in Motor private class of general insurance loss to Kshs 2.9 bn from Kshs 1.0 bn in Q2'2021. Workmen's compensation class made the highest underwriting profit of Kshs 2.0 bn while motor private and motor commercial classes of general insurance business incurred the highest losses of Kshs 2.9 bn and Kshs 1.0 bn respectively.

In our view, the insurance sector is expected to continue to record increased investment income mainly driven by gains recorded in both the Equities and Fixed income markets. The insurance sector's profitability is however expected to be weighed down by the high loss ratios, especially in the general insurance business as the net claims outpace net premiums.

Universe of Coverage:

Company	Price as at 03/09/2021	Price as at 10/09/2021	w/w change	YTD Change	Year Open 2021	Target Price*	Dividend Yield	Upside/Downside**	P/TBv Multiple	Recommendation
I&M Group***	22.8	22.5	(1.1%)	(49.8%)	44.9	32.0	10.0%	52.2%	0.3x	Buy
ABSA Bank***	10.6	10.4	(1.4%)	9.2%	9.5	13.8	0.0%	32.7%	1.2x	Buy
Kenya Reinsurance	2.5	2.5	0.8%	9.1%	2.3	3.1	7.9%	31.0%	0.3x	Buy
Sanlam	10.5	9.9	(5.5%)	(23.7%)	13.0	12.4	0.0%	25.0%	0.9x	Buy
NCBA***	27.2	27.7	1.7%	3.9%	26.6	31.0	5.4%	17.5%	0.7x	Accumulate
KCB Group***	46.8	46.6	(0.4%)	21.4%	38.4	53.4	2.1%	16.7%	1.0x	Accumulate
Standard Chartered***	136.3	135.0	(0.9%)	(6.6%)	144.5	145.4	7.8%	15.5%	1.1x	Accumulate
Co-op Bank***	13.4	13.4	(0.4%)	6.4%	12.6	14.1	7.5%	13.1%	0.9x	Accumulate
Equity Group***	49.9	51.0	2.2%	40.7%	36.3	57.5	0.0%	12.7%	1.4x	Accumulate
Stanbic Holdings	94.0	89.3	(5.1%)	5.0%	85.0	96.6	1.9%	10.1%	0.8x	Accumulate
Liberty Holdings	8.3	7.6	(8.0%)	(0.8%)	7.7	8.4	0.0%	9.9%	0.6x	Hold
Diamond Trust Bank***	65.0	64.0	(1.5%)	(16.6%)	76.8	67.3	0.0%	5.2%	0.3x	Hold
Jubilee Holdings	360.0	359.3	(0.2%)	30.3%	275.8	330.9	2.5%	(5.4%)	0.7x	Sell
HF Group	3.7	3.8	3.6%	20.7%	3.1	3.1	0.0%	(18.2%)	0.2x	Sell
Britam	8.3	8.3	0.5%	19.1%	7.0	6.7	0.0%	(19.7%)	1.5x	Sell
CIC Group	2.8	2.8	(1.4%)	32.7%	2.1	1.8	0.0%	(35.7%)	1.0x	Sell

*Target Price as per Cytonn Analyst estimates as at H1'2021

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

***For Disclosure, these are stocks in which Cytonn and/or its affiliates are invested in

Key to note, I&M Group YTD share price change is mainly attributable to the counter trading ex-bonus issue

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 1.5x), 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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