Unit Trust Funds Performance, Q1'2021, & Cytonn Weekly #41/2021

Focus of the Week

Unit Trust Funds (UTFs) are collective investment schemes that pool funds from different investors and are managed by professional fund managers. The fund managers invest the pooled funds in a portfolio of securities with the aim of generating returns to meet the specific objectives of the fund. Following the release of the Capital Markets Authority (CMA) Quarterly Statistical Bulletin – Q2’2021, we analyze the performance of Unit Trust Funds, as the total Assets Under Management (AUM) have been steadily increasing and they are among the most popular investment options in the Kenyan market. We will further analyze the performance of Money Market Funds, a product under Unit Trust Funds. In our previous focus on Unit Trust Funds, we looked at the FY’2020 Performance by Unit Trust Fund Managers. In this topical, we focus on the Q1’2021 performance of Unit Trust Funds where we shall analyze the following:

i. Performance of the Unit Trust Funds Industry,
ii. Performance of Money Market Funds,
iii. Comparing Unit Trust Funds AUM Growth with other Markets, and,
iv. Conclusion

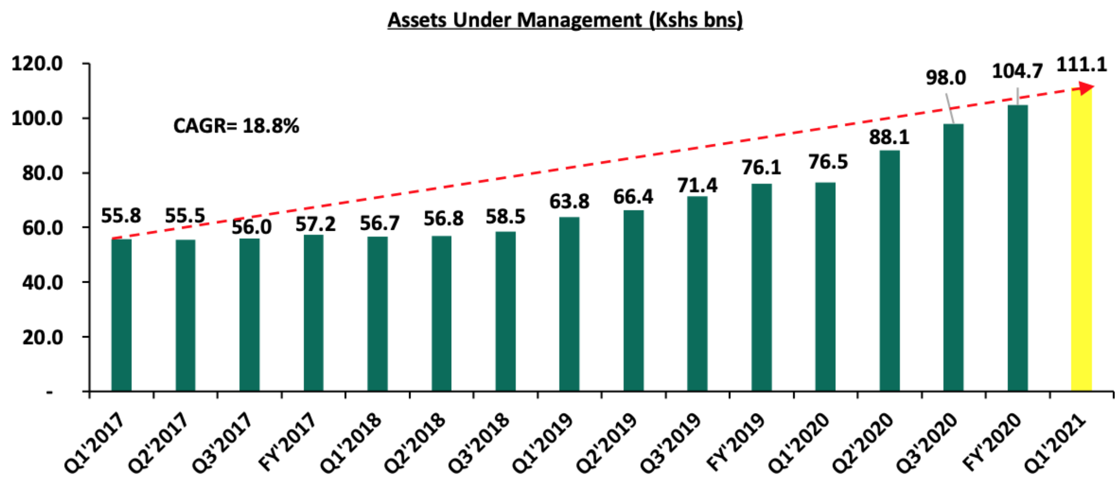
Section I: Performance of the Unit Trust Funds Industry

Unit Trust Funds are investment schemes that pool funds from investors and are managed by professional Fund Managers. The fund manager invests the pooled funds with the aim of generating returns in line with the specific objectives of the fund. The Unit Trust Funds earn returns in the form of dividends, interest income, rent and/or capital gains depending on the underlying security. The main types of Unit Trust Funds include:

i. Money Market Funds – These are funds that invests in fixed income securities such as fixed deposits, treasury bills and bonds, commercial papers, etc. They are very liquid, have stable returns, and, they are suitable for risk averse investors,
ii. Equity Funds – These are funds which largely invest in listed securities and seek to offer superior returns over the medium to long-term by maximizing capital gains and dividend income. The funds invest in various sectors to reduce concentration of risk and maintain some portion of the fund’s cash in liquid fixed income investments to maintain liquidity and pay investors if need be without losing value,
iii. Balanced Funds – These are funds whose investments are diversified across the Equities and the Fixed Income market. The Balanced Fund offers investors long-term growth as well as reasonable levels of stability of income,
iv. Fixed Income Funds – These are funds which invest in interest-bearing securities, which include treasury bills, treasury bonds, preference shares, corporate bonds, loan stock, approved securities, notes and liquid assets consistent with the portfolio’s investment objective, and,
v. Sector Specific Funds – These are funds that invest primarily in a particular sector or industry. The funds provide a greater measure of diversification within a given sector than may be

otherwise possible for the other funds. They are specifically approved by the capital Markets Authority as they are not invested as per the set rules and regulations.

As per the Capital Markets Authority (CMA) Quarterly Statistical Bulletin – Q2'2021, the industry's overall Assets Under Management (AUM) grew by 6.1% to Kshs 111.1 bn as at the end of Q1'2021, from Kshs 104.7 bn as at the end of FY'2020. Assets Under Management of the Unit Trust Funds have grown at a 4-year CAGR of 18.8% to Kshs 111.1 bn in Q1'2021, from Kshs 55.8 bn recorded in Q1'2017.



This growth can be largely attributable to:

- Low Investments minimums: Unit Trust Funds have become relatively affordable to retail investors, with a majority of the Collective Investment Schemes' (CIS) in the market requiring an initial investment ranging between Kshs 100.0 - Kshs 10,000.0,

- Increased Investor Knowledge: There has been a drive towards investor education which has meant that more people are aware and have a deeper understanding of the investment subject. As a result, their confidence has been boosted and more of them are investing,
- Diversified product offering: Unit Trust Funds are also advantageous in terms of offering investors the opportunity of diversifying their portfolios by providing them with access to a wider range of investment securities through pooling of funds, which would have not been accessible if they invested on their own,
- Efficiency and ease of access to cash/High Liquidity: Funds invested in UTFs are invested as portfolios with different assets and the fund managers always maintain a cash buffer, they are relatively liquid and investors can get their cash on demand. Unit trusts are highly liquid, as it is easy to sell and buy units without depending on demand and supply at the time of investment or exit, and,
- Adoption of Fintech: Digitization and automation within the industry has enhanced liquidity, enabling investors to receive their funds within 3 to 5 working days if they are withdrawing to their bank accounts, and immediate access to funds when withdrawing via M-PESA. According to the Central Bank of Kenya, more and more individuals are transacting through mobile money services as evidenced by the increase in the total number of registered mobile money accounts to 68.1 mn in August 2021 from 66.6 mn recorded in January 2021. Fintech has increased the efficiency of processing both payments and investments for fund managers.

According to the Capital Markets Authority, as at the end of Q1'2021, there were 25 approved Collective Investment Schemes in Kenya. Out of the 25, however, only 19 were active while 6 were inactive. During the period under review, total Assets Under Management grew by 6.1% to Kshs 111.1 bn in Q1'2021, from Kshs 104.7 bn as at the end of FY'2020. The table below outlines the performance of the Fund Managers:

Assets Under Management (AUM) for the Approved and Active Collective Investment Schemes

No.	Fund Managers	FY'2020 AUM (Kshs mns)	FY'2020 Market Share	Q1'2021 AUM (Kshs mns)	Q1'2021 Market Share	AUM Growth FY'2020 – Q1'2021
1	CIC Asset Managers	42,988.1	41.1%	44,761.7	40.3%	4.1%
2	Britam	12,304.8	11.8%	14,150.3	12.7%	15.0%
3	NCBA Unit Trust Scheme	12,543.2	12.0%	13,609.4	12.3%	8.5%
4	ICEA Lion	11,521.0	11.0%	11,843.3	10.7%	2.8%
5	Sanlam Investments	6,279.8	6.0%	6,758.7	6.1%	7.6%
6	Old Mutual	6,131.3	5.9%	6,168.5	5.6%	0.6%
7	Dry Associates	2,360.9	2.3%	2,581.9	2.3%	9.4%
8	Madison Asset Managers	1,928.6	1.8%	1,896.8	1.7%	(1.7%)
9	African Alliance Kenya	1,813.3	1.7%	1,827.7	1.7%	0.8%
10	Nabo Capital (Centum)	1,654.8	1.6%	1,778.7	1.6%	7.5%
11	Zimele Asset Managers	1,420.4	1.4%	1,454.5	1.3%	2.4%
12	Co-op Trust Investment Services Limited	1,007.1	1.0%	1,371.9	1.2%	36.2%
13	Cytonn Asset Managers	819.5	0.8%	960.2	0.9%	17.2%
14	Apollo Asset Managers	587.3	0.6%	685.8	0.6%	16.8%
15	Genghis Capital	700.0	0.7%	645.5	0.6%	(7.8%)
16	Equity Investment Bank	310.8	0.3%	297.9	0.3%	(4.1%)
17	Alphafrica Asset Managers	208.1	0.2%	216.4	0.2%	4.0%
18	Amana Capital	135.4	0.1%	75.6	0.1%	(44.2%)
19	Wanafunzi Investments	0.5	0.0%	0.6	0.0%	0.0%
20	Metropolitan Cannon Asset Managers	-	-	-	-	-
21	FCB Capital Limited	-	-	-	-	-
22	Fusion Investment Management Ltd	-	-	-	-	-
23	Standard Chartered Investment Services	-	-	-	-	-
24	Natbank Trustee & Investment Services	-	-	-	-	-
25	ABSA Asset Management Ltd	-	-	-	-	-
	Total	104,714.9	100.0%	111,085.3	100.0%	6.1%

Source: Capital Markets Authority: Quarterly Statistical Bulletin, Q2'2021

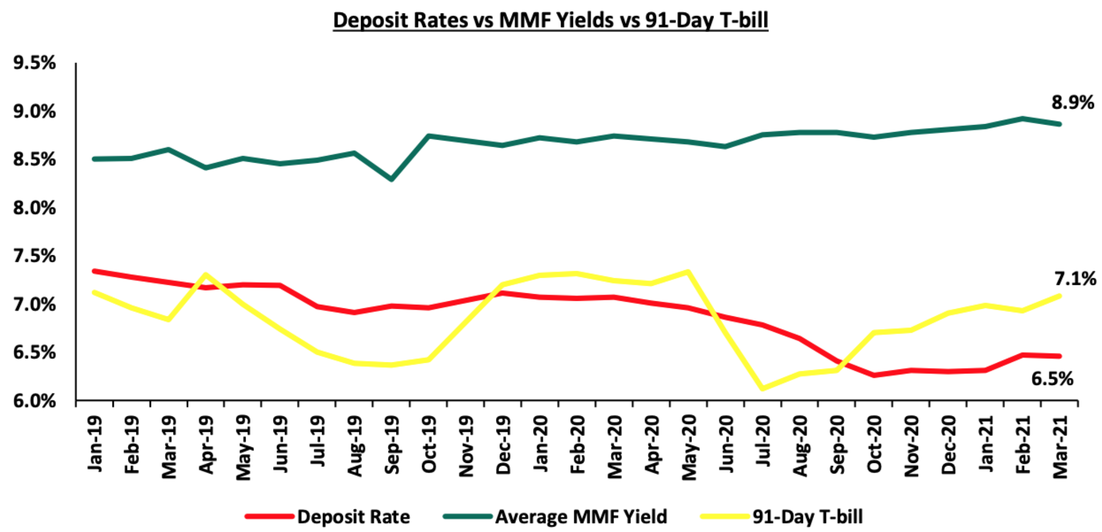
Key to note from the above table:

- Assets Under Management: CIC Asset Managers remained the largest overall Unit Trust Fund Manager with an AUM of Kshs 44.8 bn in Q1'2021, from an AUM of Kshs 43.0 bn as at FY'2020, translating to a 4.1% AUM growth,
- Market Share: CIC Asset Managers remained the largest overall Unit Trust with a market share of 40.3%, a decline from 41.1% in FY'2020. Key to note, Britam recorded the highest increase in its market share with the market share increasing to 12.7%, from 11.8% in FY'2020, and,
- Growth: In terms of AUM growth, Co-op Trust Investment Services Limited recorded the strongest growth of 36.2%, with its AUM increasing to Kshs 1.4 bn, from Kshs 1.0 bn in FY'2020. Cytonn Asset Managers recorded a growth of 17.2%, with its AUM increasing to Kshs 960.2 mn, from Kshs 819.5 mn in FY'2020. Amana Capital recorded the largest decline, with its AUM declining by 44.2% to Kshs 75.6 mn in Q1'2021, from Kshs 135.4 mn in FY'2020.

Metropolitan Cannon Asset Managers, FCB Capital Limited, Fusion Investment Management Ltd, Standard Investment Trust, NatBank Trustee & Investment Services, and ABSA Asset Management Ltd remained inactive as at the end of Q1'2021.

Section II: Performance of Money Market Funds

Money Market Funds (MMFs) in the recent past have gained popularity in Kenya, with one of the main reasons being the higher returns money market funds offer compared to the returns on bank deposits and treasury bills. According to the Central Bank of Kenya data, the average deposit rate during the year declined to 6.4% in Q1'2021, from an average of 6.7% recorded as at the end of FY'2020. The average deposit rate and average 91-Day T-bill rate still remained lower than the average MMF yields of 8.9%.



As per regulations, funds in MMFs should be invested in liquid interest-bearing securities. These securities include bank deposits, securities listed on NSE, and securities issued by the Government of Kenya. The fund is best suited for investors who require a low-risk investment that offers capital stability, liquidity, and require a high-income yield. The fund is also a good safe haven for investors who wish to switch from a higher risk portfolio to a low risk portfolio, especially in times of uncertainty.

Top Five Money Market Funds by Yields

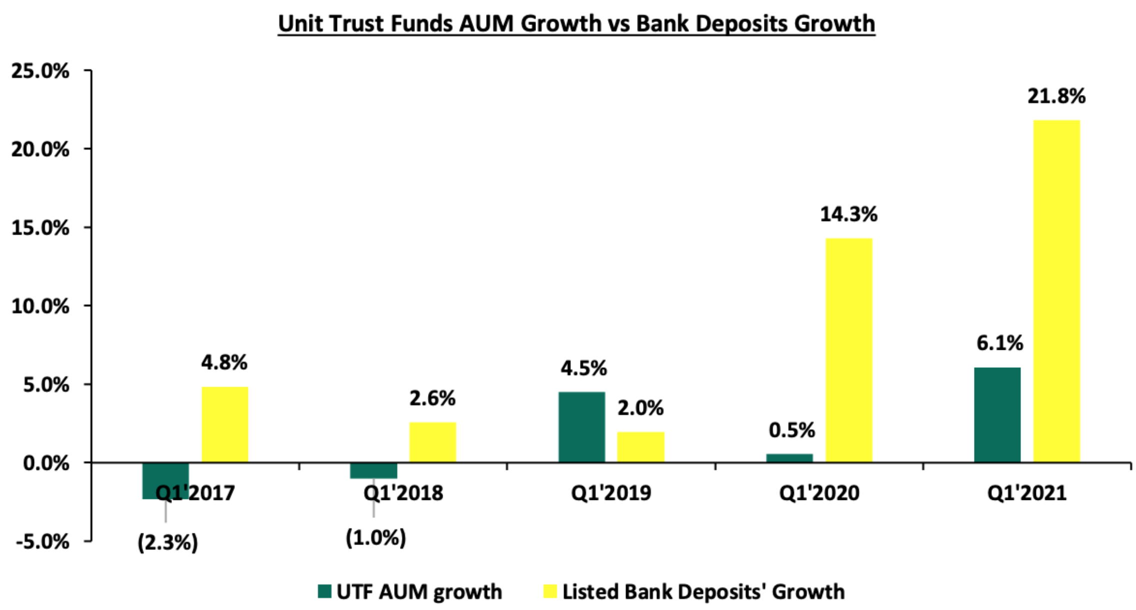
During the period under review, the following Money Market Funds had the highest average effective annual yield declared, with the Cytonn Money Market Fund having the highest effective annual yield at 10.7% against the industrial average of 8.9%.

Top 5 Money Market Fund Yield in Q1'2021

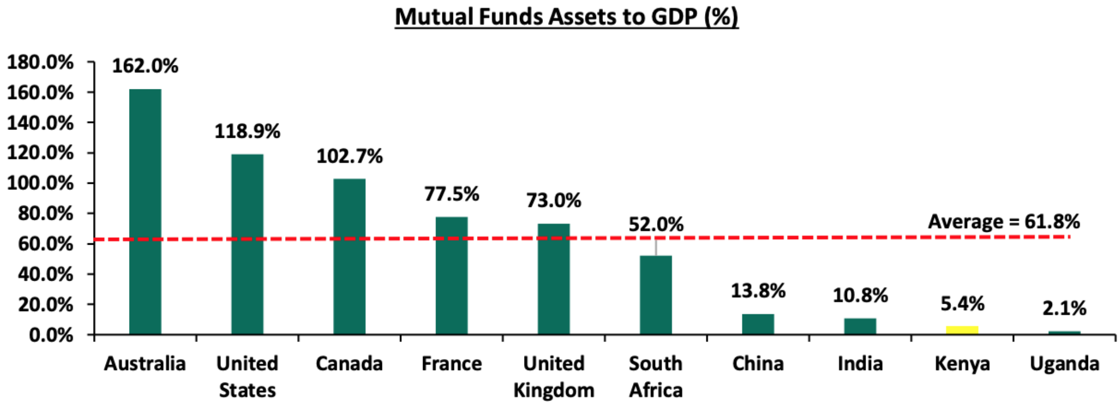
Rank	Money Market Fund	Effective Annual Rate (Average Q1'2021)
1	Cytonn Money Market Fund	10.71%
2	Zimele Money Market Fund	9.85%
3	Alphafrica Kaisha Money Market Fund	9.85%
4	Nabo Africa Money Market Fund	9.80%
5	CIC Money Market Fund	9.66%
	Industrial Average	8.87%

Section III: Comparing Unit Trust Funds AUM Growth with other Markets

Unit Trust Funds assets recorded a q/q growth of 6.1% in Q1’2021, while the listed bank deposits recorded a weighted growth of 21.8% over the same period. For both the Unit Trust Funds and bank deposits, this was higher than the values recorded as at Q1’2020 of 0.5% and 14.3%, respectively. The chart below highlights the Unit Trust Funds AUM growth vs bank deposits growth in Q1’2021;

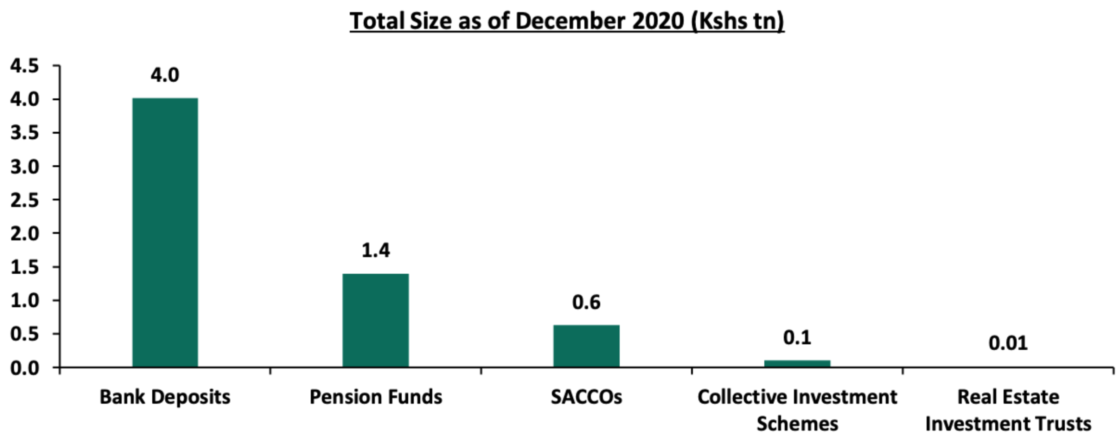


Unit Trust Funds’ growth of 6.1% was outpaced by the listed banking sector’s deposit growth of 21.8% in Q1’2021. We note that Q1’2021’s performance was better than the 0.5% growth seen in Q1’2020, an indication of the improving investor confidence in our capital markets. However, the faster growth of bank deposits highlights that the potential of our capital markets remains constrained. According to World Bank data, in well-functioning economies, businesses rely on bank funding for a mere 40.0%, with the larger percentage of 60.0% coming from the Capital markets. Closer home, CMA notes that in 2020, businesses in Kenya relied on banks for 95.0% of their funding while less than 5.0% came from the capital markets. Additionally, our Mutual Funds/UTFs to GDP ratio at 5.4% is still very low compared to global average of 61.8%, indicating that we still have room to improve and enhance our capital markets. The table below shows some countries’ mutual funds as a percentage of GDP:



Source: World Bank Data

Over the past 4 years, the UTFs AUM has grown at a CAGR of 18.8% to Kshs 111.1 bn in Q1'2021, from Kshs 55.8 bn recorded in Q1'2017. However, even at Kshs 111.1 bn, the industry is dwarfed by asset gatherers such as bank deposits at Kshs 4.0 tn and the pension industry at Kshs 1.4 tn as of the end of 2020. Below is a graph showing the sizes of different saving channels and capital market products in Kenya as at December 2020:



In order to improve our Capital Markets and stimulate its growth, we recommend the following actions:

i. Allow for sector funds: The current capital markets regulations require that funds must diversify. Consequently, one has to seek special dispensation in the form of sector funds such as a financial services fund, a technology fund or a real estate UTF fund. Regulations allowing unit holders to invest in sector funds would expand the scope of unit holders interested in investing,
ii. Reduce the minimum investments to reasonable amounts: Currently, the minimum investment for sector specific funds is Kshs 1.0 mn, while that for Development REITS is currently at Kshs 5.0 mn. The high minimum initial and top up investments amounts are unreasonably high given that the national median income for employed individuals is estimated at around Kshs 50,000, it therefore locks out a lot of potential investors. Additionally, these high amounts discriminate against most retail investors giving them fewer investment choices,
iii. Eliminate conflicts of interest in the governance of capital markets: The capital markets regulations should enable a governance structure that is more responsive to market participants and market growth,
iv. Create increased competition in the market by encouraging different players to set up shop and offer different services such as the opening up of Trustees to non-financial institutions: Competition in capital markets will not only push Unit Trust Fund managers to provide higher returns for investors but will also eliminate conflicts of interest in markets and enhance the provision of innovative products and services, and,
v. Improve fund transparency to provide investors with more information: Each Unit Trust Fund

should be required to publish their portfolio holdings on a quarterly basis and make the information available to the public so as to enhance transparency for investors. Providing investors with more information will help both investors and prospects make better informed decisions and subsequently improve investor confidence.

During Q3'2021, we saw the Capital Markets Authority (CMA) publish two draft regulations; the Capital Markets (Collective Investment Schemes) Regulations 2021 and the Capital Markets (Collective Investment Schemes) (Alternative Investment Funds) Regulations 2021. The proposed regulations seek to update the current Collective Investment Scheme Regulations given the change in market dynamics since the last published Regulations in 2001, as well as address emerging issues. The move by CMA to review the current regulations is welcomed as it seems intended to improve the Capital Markets in Kenya by providing more versatile regulations and provide for existence of regulated funds that invest in alternative asset classes. However, it's our view that proceeding with the regulations as proposed would not be ideal for the market. In our Draft CMA Investments Regulations topical, we analyzed these regulations and thereafter gave our recommendations on the areas of improvement.

Section IV: Conclusion

There is a need to leverage more on innovation and digitization in order to ensure continued growth of the capital markets and further propel the growth of UTFs in Kenya. The use of technology as a distribution channel for mutual fund products has potential to open up the capital markets to the retail segment, which is characterized by strong demand among retail clients for convenient and innovative products. Regulators should also strive to promote and facilitate growth of UTFs as this will enhance the growth of capital markets and consequently encourage entry of new players into the market. For instance, Yu'eBao, formerly the world's largest Money Market Fund, rapidly grew since it leveraged on technology and made itself readily available to retail clients. However, it saw some regulatory intervention from Chinese authorities to reduce its size citing the fund's dominance and liquidity risks. This led to the fund's AUM declining by 18.6% to USD 148.4 bn as at March 2021, from USD 182.4 bn in December 2020.

Cytonn Asset Managers, which largely leverages on technology such as USSD and digital platforms, experienced a growth of 17.2% to Kshs 960.2 mn in Q1'2021, from Kshs 819.5 mn in FY'2020. The advent of digitization and automation within the industry has also enhanced liquidity. Cytonn Money Market Fund clients can issue withdrawal instructions and have funds remitted to their bank accounts within 2–4 working days while funds withdrawn through the USSD or digital platforms are remitted to their M-Pesa and Bank accounts within 5 minutes and 2 working days respectively. The Cytonn Money Market Fund is accessible through dialing *809#. As highlighted in our topical Potential Effects of COVID-19 on Money Market Funds, we believe that amidst the Coronavirus pandemic, returns for Money Market Funds will remain stable with a bias to a slight increase upwards should rates on government securities increase. They will also remain the most liquid of all mutual funds providing a short-term parking bay that earns higher income yields compared to deposits and savings accounts. UTFs provide a more convenient platform in terms of accessibility and liquidity with the additional benefit of higher returns for investors.