Kenya Listed Banks Q3'2021 Report, & Cytonn Weekly #49/2021

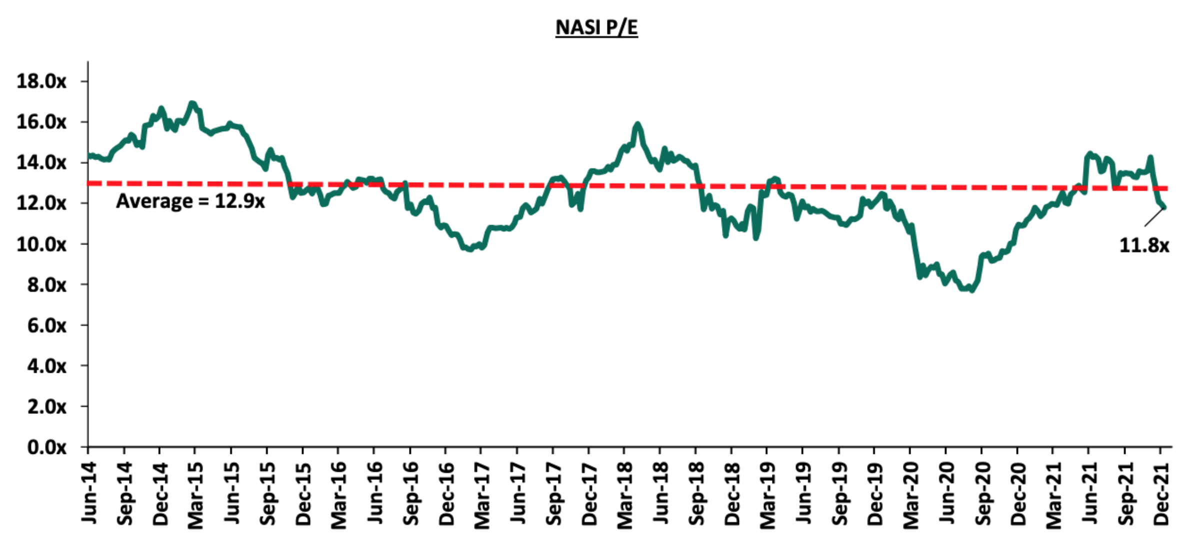
Equities

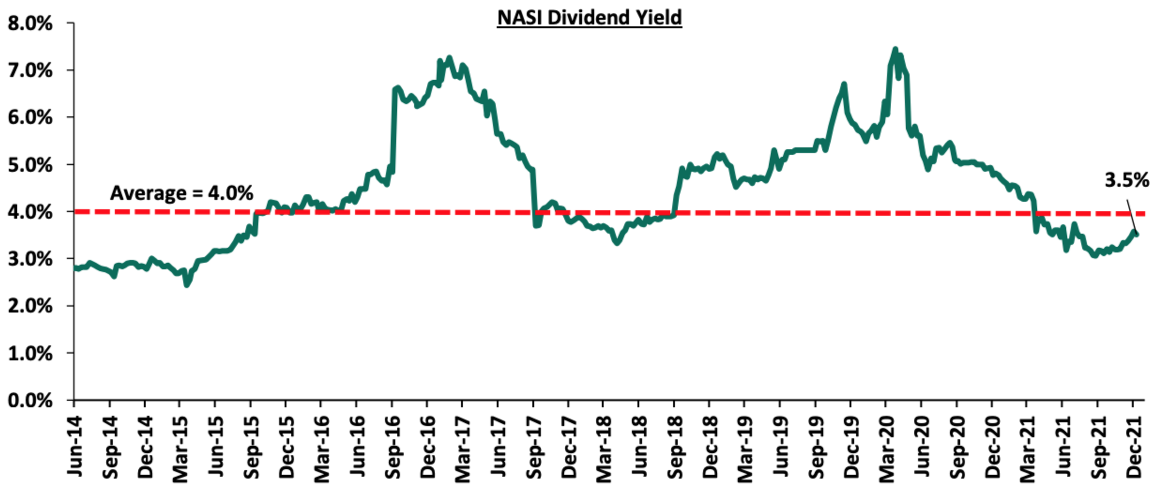
Markets Performance

During the week, the equities market was on an upward trajectory, with both NASI and NSE 25 gaining by 1.7%, while NSE 20 gained by 0.9%, taking their YTD performance to gains of 7.1% and 5.4% for NASI and NSE 25, respectively, while NSE 20 declined by 0.9% on a YTD basis. The equities market performance was driven by gains recorded by large cap stocks such as KCB, Co-operative bank, Safaricom, and Equity of 5.1%, 3.4%, 2.0% and 1.9%, respectively. The gains were however weighed down by losses recorded by other large cap stocks such as Standard Chartered Bank and EABL which declined by 1.6% and 0.7%, respectively.

During the week, equities turnover increased by 10.8% to USD 35.0 mn, from USD 31.6 mn recorded the previous week, taking the YTD turnover to USD 1.2 bn. Foreign investors remained net sellers, with a net selling position of USD 12.5 mn, from a net selling position of USD 5.7 mn recorded the previous week, taking the YTD net selling position to USD 80.4 mn.

The market is currently trading at a price to earnings ratio (P/E) of 11.8x, 8.8% below the historical average of 12.9x, and a dividend yield of 3.5%, 0.5% points below the historical average of 4.0%. Notably, this week's P/E is the lowest it has been since February 2021. Key to note, NASI's PEG ratio currently stands at 1.3x, 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 11.8x is 53.1% 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 highlights:

I. **Imperial Bank liquidation**

During the week, the Central Bank of Kenya, (CBK), announced that it had approved the liquidation of Imperial Bank Limited In Receivership, (IBLIR,) in order to pave way for the sale of IBLIR's remaining assets to settle any existing debts to depositors and creditors. This follows the recommendation by Kenya Deposit Insurance Corporation (KDIC), the receiver, to liquidate the bank, coupled with a report from an external auditor that ascertained that winding down the lender was the only feasible option based on the weak status of IBLIR's financial position. IBLIR was put under receivership by the CBK on 13th October 2015 due to irregularities and malpractices in the bank which exposed depositors, creditors and the banking sector to financial risk. At the time of receivership, IBLIR had 32 branches, Kshs 70.3 bn (as of 30th June 2015) worth of assets, and Kshs 58.1 bn worth of deposits, owed to 50,000 depositors.

In December 2015, CBK and KDIC announced that 44,300 depositors with deposits of less than Kshs 1.0 mn would get access to their full amounts, while the remaining 5,700 depositors would only access up to 1.0 mn of their deposits. In June 2020, KCB Bank acquired certain assets of IBLIR totalling Kshs 3.2 bn and an equivalent amount of liabilities. For more information, please see our Cytonn Weekly #49/2020.

However, the paid amounts do not include other creditors such as the Kshs 2.0 bn corporate bond that IBLIR, then Imperial Bank, floated in September 2015. It is also key to note that Imperial Bank had listed the Kshs 2.0 bn corporate bond just a month before its eventual collapse, which exposes the regulator for the bonds issuance, the Capital Markets Authority, (CMA), to scrutiny as the listing should not have proceeded under the institution's financial health. We are of the view that confidence in the financial markets is of paramount importance for any economy. Therefore, the liquidation of IBLIR is a welcome move as it will allow for settling of the remaining amounts owed to the various parties. However, we believe that the CBK should put in sufficient mechanisms to protect depositor's funds through better supervision of the banking sector.

II. **Central Bank of Kenya Amendment Act, 2021**

During the week, President Uhuru Kenyatta recently signed into law the Central Bank of Kenya (CBK) Amendment Act, 2021 which confers the CBK powers to regulate the digital lending services sector and aims to amend the Central Bank of Kenya Act Chapter 491 to provide and allow for the licensing of digital credit service providers, who are currently not regulated. The act also defines relevant terms for the business of digital credit lending where a digital credit provider is a person licensed by the CBK to carry on digital credit business while a digital credit business is one of providing credit facilities or loan services through a digital channel. Further, the act aims to provide for a fair and non-discriminatory marketplace for access to credit. In order to achieve this, CBK will have the power to;

i. License digital credit providers,
ii. Determine capital adequacy requirements for digital credit providers,
iii. Determine the minimum liquidity requirements for digital credit providers,
iv. Approve digital channels and business models through which digital credit business may be conducted,
v. Supervise digital credit providers,
vi. Suspend or revoke a license, and,
vii. Direct or require changes as the CBK may consider necessary.

The above will be effected through subsequent provisions of the Act which will grant the CBK the ability to make regulations on;

i. Registration requirement for digital credit businesses,
ii. Management requirements for digital credit providers,
iii. Permissible and prohibited activities,
iv. Anti-money laundering and measures for countering financing terrorism,
v. Credit information sharing,
vi. Data protection,
vii. Consumer protection,
viii. Reporting requirements for digital credit providers,
ix. Offences and penalties, and,
x. Such other measures necessary for regulation of digital lending.

The CBK will have a period of three months to make any regulations aimed at regulating the digital lending space. For businesses providing credit facilities or credit facilities through a digital channel and are not regulated under any other law, they will be required to register with the CBK within six months of coming into force of this Act. This excludes digital service lenders operating under their parent banks as they are regulated by the Banking Act. Any digital credit provider who operates without a license will be susceptible to a fine not exceeding Kshs 5.0 mn or to imprisonment upon conviction for a term not exceeding three (3) years or both.

The Act is a step in the right direction towards streamlining the lending digital lending services sector and will weed out unscrupulous digital lenders who have taken advantage of the unregulated space to infringe on various consumer rights and privacy. This is not only a win for the consumers but also a win for the lenders who will acquire licenses to increase their market share and operate in a better environment. Given that the Act does not provide for capping of interest rates for digital lending, we believe that CBK, through the regulations, will provide an enabling environment by allowing the lenders to continue using their risk and pricing models rather than set interest caps for digital lenders. We also expect the CBK to avoid setting high minimum capital adequacy and liquidity requirements for the digital lenders seeing they are not deposit taking institutions and would be counterproductive to their purpose.

Universe of coverage:

Company	Price as at 03/12/2021	Price as at 10/12/2021	w/w change	YTD Change	Year Open 2021	Target Price*	Dividend Yield	Upside/ Downside**	P/TBv Multiple	Recommendation
Kenya Reinsurance	2.3	2.3	(1.3%)	(0.9%)	2.3	3.3	8.7%	53.6%	**0.2x**	Buy
I&M Group***	20.6	21.0	1.7%	(53.3%)	44.9	24.4	10.7%	27.1%	**0.6x**	Buy

Company	Price as at 03/12/2021	Price as at 10/12/2021	w/w change	YTD Change	Year Open 2021	Target Price*	Dividend Yield	Upside/ Downside**	P/TBv Multiple	Recommendation
KCB Group* **	41.2	43.3	5.1%	12.6%	38.4	51.4	2.3%	21.0%	**0.9x**	**Buy**
Britam	6.9	7.0	0.6%	(0.3%)	7.0	8.3	0.0%	19.5%	**1.2x**	**Accumulate**
Standard Chartered* **	129.0	127.0	(1.6%)	(12.1%)	144.5	137.7	8.3%	16.7%	**1.0x**	**Accumulate**
NCBA* **	24.0	24.1	0.2%	(9.6%)	26.6	26.4	6.2%	16.0%	**0.6x**	**Accumulate**
Co-op Bank* **	11.8	12.2	3.4%	(2.8%)	12.6	13.1	8.2%	15.2%	**0.9x**	**Accumulate**
Jubilee Holdings	339.8	336.0	(1.1%)	21.8%	275.8	371.5	2.7%	13.2%	**0.6x**	**Accumulate**
Equity Group* **	46.6	47.5	1.9%	31.0%	36.3	52.5	0.0%	10.6%	**1.2x**	**Accumulate**
Diamond Trust Bank* **	55.3	56.0	1.4%	(27.0%)	76.8	61.8	0.0%	10.3%	**0.2x**	**Accumulate**
Liberty Holdings	7.0	7.2	2.6%	(7.0%)	7.7	7.8	0.0%	8.6%	**0.5x**	**Hold**
ABSA Bank* **	11.1	11.1	0.0%	16.1%	9.5	11.9	0.0%	7.7%	**1.1x**	**Hold**
Stanbic Holdings	90.5	92.3	1.9%	8.5%	85.0	94.7	4.1%	6.8%	**0.8x**	**Hold**
Sanlam	11.5	11.5	0.0%	(11.5%)	13.0	12.1	0.0%	5.3%	**1.2x**	**Hold**
CIC Group	2.2	2.2	0.0%	2.4%	2.1	2.0	0.0%	(5.4%)	**0.7x**	**Sell**
HF Group	4.1	4.0	(3.2%)	26.4%	3.1	3.0	0.0%	(25.6%)	**0.2x**	**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**
Key to note, I&M Holdings 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 1.3x), we believe that investors should reposition towards companies with a strong earnings growth and are trading at discounts to their intrinsic value. We expect the discovery of new COVID-19 variants coupled with slow vaccine rollout in developing economies to continue weighing down the economic outlook. On the upside, we believe that the recent relaxation of lockdown measures in the country will lead to improved investor sentiments in the economy.