Cytonn Annual Markets Review - 2021

Equities

Market Performance

During the year, the Kenyan equities market was on an upward trajectory, with NASI, NSE 25 and NSE 20 increasing by 9.5%, 9.8% and 1.6%, respectively. Below is a summary of the 2021 performance of the some of the large cap stocks in the Kenyan stock market:

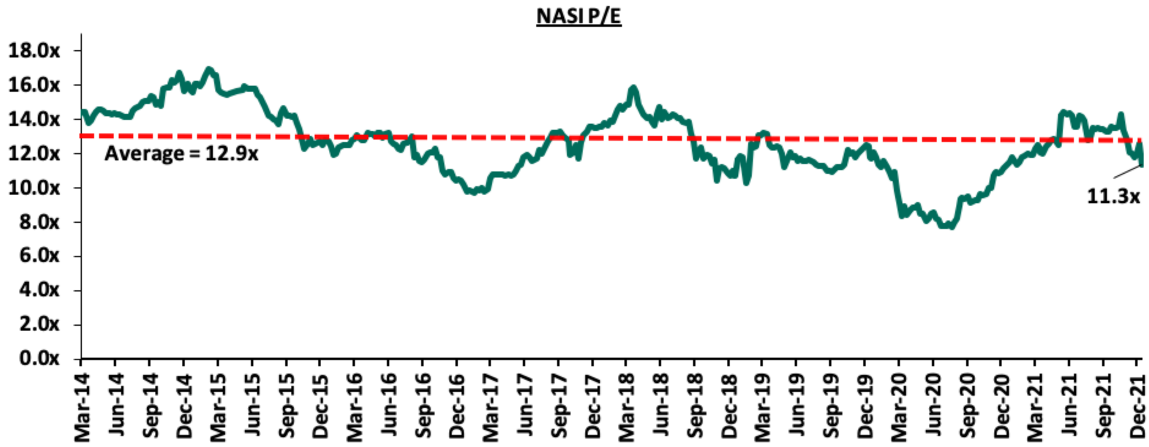
Kenyan Equities Performance – Large Cap Gainers and Losers 2021

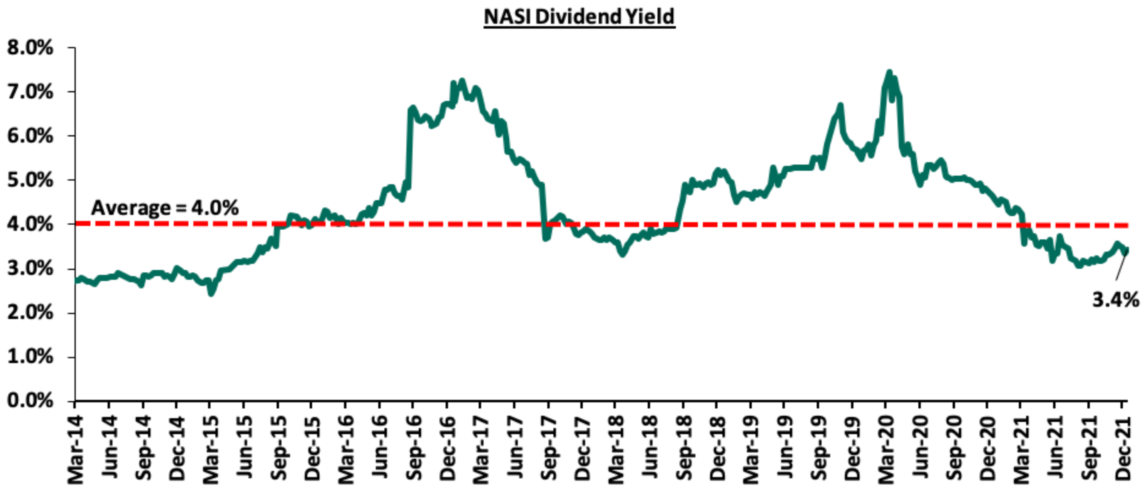
No	Company Name	Share Price Performance 2021
1	**Equity Group**	**45.5%**
2	ABSA Bank Kenya	24.5%
3	BAT Kenya	22.3%
4	KCB Group	18.4%
5	Safaricom	10.8%
6	East African Breweries Limited (EABL)	7.1%
7	Co-operative Bank Kenya	3.2%
8	Bamburi Cement	(4.9%)
9	NCBA Bank Kenya	(5.3%)
10	Standard Chartered Bank Kenya	(11.2%)
11	Diamond Trust Bank Kenya (DTB-K)	(22.5%)

Equity turnover during the year declined by 11.2% to USD 1.3 bn, from USD 1.4 bn in FY'2020. Foreign investors remained net sellers, with a net outflow of USD 91.9 mn, compared to net outflows of USD 280.9 mn recorded in FY'2020. The foreign-investor outflows during the year can be attributed mainly to profit taking activities as most large cap stocks recorded significant gains during the year, compared to 2020.

The market is currently trading at a price to earnings ratio (P/E) of 11.3x, similar to what was recorded at the end of 2020, and is 12.4% below the 12-year historical average of 12.9x. NASI's P/E ratio has remained high for most of the year, mainly attributable to price rallies on most stocks such as Safaricom whose price increased by 10.8% during the year, while its EPS decline by 6.8%. Safaricom continues to be a key part of Kenyan equities portfolios, accounting for 59.5% of Nairobi Stock Exchange (NSE's) market capitalization, and has dominated both the market turnover and determining the direction of the market given its weight and liquidity in the Nairobi Securities Exchange. On the other hand, the average dividend yield is currently at 3.4%, 0.6% points below the historical average of 4.0%.

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. The current P/E valuation of 11.3x is 47.1% above the most recent trough valuation of 7.7x experienced in the first week of August 2020. The charts below indicate the market's historical P/E and dividend yield:





Weekly Highlights:

I. **Q2'2021 Quarterly Economic Review**

During the week, the Central Bank of Kenya (CBK) released the Quarterly Economic Review for the period ending 30th June 2021, highlighting that the banking sector remained stable and resilient during the period. According to the report, the sector's total assets increased by 2.7% to Kshs 5.7 tn in June 2021, from Kshs 5.5 tn in March 2021. The increase was mainly attributable to a 2.7% increase in loans and advances during the quarter. On a yearly basis, total assets increased by 7.8% to Kshs 5.7 tn, from Kshs 5.3 tn in June 2020. Notably, loans and advances accounted for 49.3% of total assets in Q2'2021, which was a 0.5% points decrease from 49.8% of total assets in Q1'2021 and a 1.6% points decrease from 50.9% of the total assets in Q2'2020.

Other key take-outs from the report include:

i. The banking sector recorded a 10.1% increase in Profit before Tax (PBT) to Kshs 50.5 bn in Q2'2021, from Kshs 45.9 bn in Q1'2021, with the increase in profitability mainly attributable to a higher 6.3% increase in income to Kshs 154.0 bn, from Kshs 144.9 bn in Q1'2021, compared to the 4.5% increase in expenses to Kshs 103.5 bn, from Kshs 99.1 bn in Q1'2021. On a yearly basis, PBT increased by 132.7%, to Kshs 50.5 bn, from Kshs 21.7 bn recorded in Q2'2020. Consequently, the sector's Return on Assets (ROA) recorded a 0.1% point increase to come in at 2.7% in Q2'2021, from 2.6% recorded in Q1'2021, and, a 2.2% points increase from 0.5% recorded in Q2'2020. Additionally, Return On Equity (ROE) recorded an 0.7% points increase to 22.7% in June 2021, from 22.0% in March 2021, and, an 11.4% points increase from 11.3% recorded in June

2020,

ii. Lending increased by 2.3% to Kshs 3.1 tn in Q2’2021, from Kshs 3.0 tn in Q1’2021, attributable to an increase in loans and advances to Manufacturing, and Personal and Household, and Financial Services sectors. On a yearly basis, lending was up by 6.9% to Kshs 3.1 tn, from Kshs 2.9 tn in Q2’2020,
iii. Deposits recorded a 2.8% increase to Kshs 4.2 tn in June 2021, from Kshs 4.1 tn in March 2021, attributable to a 3.4% increase in local currency deposits which increased to Kshs 3.2 tn in June 2021, from Kshs 3.1 tn in March 2021. Compared to last year, deposits increased by 8.9% to Kshs 4.2 tn in Q2’2021, from Kshs 3.9 tn in Q2’2020. Key to note, customer deposits remain the main source of funding for banks, accounting for 74.8% of the sector’s total liabilities and shareholders’ funds as at Q2’2021, same as recorded in Q1’2021 but slightly lower than the 75.0% recorded in Q2’2020,
iv. Credit risk remained elevated in the sector, despite the gross Non-Performing Loans (NPLs) ratio reducing to 14.0% in Q2’2021, from 14.6% in Q1’2021. The Transport and Communication sector registered the highest increase in NPLs by 15.3% in Q2’2021 as a result of the disruptions caused by the COVID-19 pandemic. The asset quality, however, deteriorated compared with last year as the NPL ratio increased by 0.9% points to 14.0% in Q2’2021, from 13.1% in Q2’2020. The sector’s NPL coverage ratio decreased slightly to 53.0% in Q2’2021, from 53.1% in Q1’2021, an indication that the banks maintained the current relatively high provisioning levels to manage risks given the tough economic conditions. The NPL coverage as of Q2’2020 stood at 44.4%,
v. The banking sector remained adequately capitalized, with the aggregate Core Capital to Total Risk-Weighted Assets ratio coming in at 16.5% in Q2’2021, similar to what was recorded in Q1’2021 and 0.1% higher than the 16.4% recorded in Q2’2020. The Core Capital to Total Risk-Weighted Assets ratio was 6.0% points above the CBK’s minimum statutory ratio of 10.5%. On the other hand, Total Capital to Total Risk-Weighted Assets ratio, increased slightly by 0.1% points to 18.9% in Q2’2021, from 18.8% in Q1’2021, and, up 0.4% points from 18.5% recorded in Q2’2020. The Q2’2021 Total Capital to Total Risk-Weighted Assets ratio was 4.4% points above the CBK’s minimum statutory ratio of 14.5%, and,
vi. The sector remained liquid during the period under review, with the liquidity ratio rising to 56.8% in Q2’2021, from 56.3% in Q1’2021 and 52.8% record in Q2’2020. This was 36.8% points above the minimum statutory level of 20.0%. The increase in the banking sector’s liquidity is attributable to a 3.3% increase in total liquid assets, which outpaced the 2.4% increase in short term liabilities during the quarter.

The increasing profitability in Q2’2021 indicates that the banking sector remains on the path to recovery in 2021. The sector remains sufficiently capitalized and with adequate liquidity levels, evidenced by the capital adequacy and liquidity ratios remaining above the minimum statutory ratios. Overall, we expect the banking sector to remain resilient boosted by the CBK’s efforts to improve their liquidity positions by maintaining the Cash Reserve Ratio at 4.25%, proactive monitoring of the loan book by commercial banks and improved capital adequacy across the sector.

II. **Britam Shares Sale in Equity Group**

During the week, Equity Group disclosed that Britam Holdings PLC and Britam Life Assurance Company (Kenya) Limited had entered into a share purchase and sale agreement of Equity Group Shares with International Finance Corporation (IFC) and IFC Financial Institutions Growth Fund (IFC FIG Fund). The agreement will see IFC acquire 164,521,735 shares, 4.4% of the total Equity Group shares, and IFC FIG Fund would acquire 88,588,626 shares, 2.3% of the total Equity Group shares, from Britam in total. Britam Life is a subsidiary of Britam Holdings PLC. IFC and IFC FIG Fund are expected to acquire the shares at Kshs 55.0 per share, which represents a 4.3% premium on Equity Group’s current market price of Kshs 52.8 per share as of 31st December 2021. Britam will receive a total of Kshs 13.9 bn from the transaction. The split between Britam Holdings and Britam Life, and, the use of proceeds, have not been specified. However, we estimate that Kshs 3.3 bn will go towards paying the holding company's bank loan that was secured with quoted ordinary shares, and, Kshs 5.2 bn will go towards supporting the Britam Wealth Management Fund. Britam Holdings had made a provision for investment losses of Kshs 5.2 bn in their FY'2020 financials, to provide financial support to the Wealth Management Fund, a fund managed by Britam Asset Managers.

The move to sell the shares will help reduce the effect that the volatile equity investment has had on Britam's profit levels in the past. According to their FY'2020 annual report, its shareholding in Equity Group alone led to a fair value loss of Kshs 4.2 bn, representing 46.9% of the total Kshs 9.1 bn loss recorded during the year, due to a 33.5% share price decline in Equity Group's share price in 2020. We expect that this portfolio optimization will help Britam stabilize its performance going forward and enable it to focus on its core and profitable offerings.

2021 Key highlights;

I. **Banking Sector Earnings**

As per the Q3'2021 results, the listed banks recorded a weighted average increase in their core earnings per share of 102.0%, compared to a weighted decline of (32.4%) in Q3'2020. The table below highlights the performance of the banking sector, showing the 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
ABSA	328.3%	1.3%	(19.1%)	8.6%	7.0%	5.2%	32.0%	11.9%	9.0%	(5.6%)	85.2%	9.5%	21.1%
NCBA	159.0%	16.2%	10.8%	17.9%	8.4%	10.3%	29.4%	1.2%	11.2%	6.9%	75.9%	12.9%	22.7%
KCB	131.4%	28.7%	45.0%	23.3%	7.0%	28.8%	39.7%	34.2%	26.6%	25.8%	63.9%	23.2%	22.2%
Equity	78.6%	9.8%	(1.3%)	19.1%	6.2%	(0.2%)	44.3%	(4.3%)	11.2%	(14.1%)	53.2%	(4.6%)	11.8%
Stanbic	43.2%	(2.5%)	(23.3%)	2.8%	6.7%	19.1%	33.9%	17.9%	6.4%	(6.8%)	51.0%	0.1%	14.5%
SCBK	33.7%	0.5%	(7.3%)	12.2%	6.2%	4.2%	42.6%	(8.5%)	(5.8%)	(17.4%)	83.0%	11.2%	14.0%
I&M	25.1%	15.7%	(5.2%)	34.5%	6.0%	(3.5%)	30.7%	12.8%	14.2%	28.6%	71.9%	11.8%	14.3%
DTBK	20.1%	6.0%	6.2%	5.9%	5.4%	(4.9%)	24.5%	0.3%	12.3%	(2.7%)	63.5%	0.0%	6.8%
Co-op	18.0%	21.6%	22.4%	21.3%	8.5%	15.6%	35.4%	9.4%	12.0%	35.9%	72.9%	7.8%	14.2%
HF Group	(22.0%)	(18.4%)	(21.2%)	(14.8%)	3.9%	12.2%	24.7%	27.5%	(1.3%)	(9.5%)	92.2%	(7.9%)	(19.0%)
Q3'21 Mkt Weighted Average*	**102.0%**	**15.9%**	**14.9%**	**16.9%**	**7.3%**	**14.3%**	**35.2%**	**13.8%**	**14.3%**	**11.7%**	**69.7%**	**12.4%**	**18.7%**
Q3'20 Mkt Weighted Average**	**(32.4%)**	**10.8%**	**8.2%**	**11.7%**	**7.0%**	**2.1%**	**35.9%**	**(7.9%)**	**23.1%**	**47.4%**	**65.6%**	**15.0%**	**13.0%**

***Market cap weighted as at 10/12/2021**
****Market cap weighted as at 01/12/2020**

Key takeaways from the table above include:

i. For the third quarter of 2021, core Earnings per Share (EPS) recorded a weighted average growth of 102.0%, compared to a weighted average decline of 32.4% in Q3'2020 for the listed banking sector. The performance is however largely skewed by the strong performance from ABSA, NCBA and KCB Group of 3%, 159.0% and 131.4%, respectively,
ii. The Banks have recorded a weighted average deposit growth of 14.3%, a decline from the 23.1% recorded in Q3'2020,
iii. Interest expense grew at a faster pace, by 14.9%, compared to the 8.2% growth in Q3'2020 while cost of funds declined, coming in at a weighted average of 2.7% in Q3'2021, from 2.9% in Q3'2020, 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 12.4%, lower than the 15.0% growth recorded in Q3'2020. Notably, the loan growth outpaced the 11.7% growth in government securities, an indication that the banks' have increased their lending to private sectors due to decrease in credit risk on the back of economic recovery,
v. Interest income grew by 15.9%, compared to a growth of 10.8% recorded in Q3'2020. Notably, the

weighted average Yield on Interest Earning Assets (YIEA) for the listed banks increased to 9.8%, from the 9.5% recorded in Q3'2020, 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 7.3%, a 0.3% points increase from the 7.0% recorded in Q3'2020 for the listed banking sector, and,

vi. Non-Funded Income grew by 14.3%, compared to the 2.1% increase recorded in Q3'2020. This can be attributable to the faster growth in the fees and commission which grew by 13.8% compared to a decline of 7.9% in Q3'2020, and points to the diversification of income in the banking sector.

For more information, see our Kenya Listed Banks Q3'2021 Report.

II. **Insurance Sector Earnings:**

During the year, Kenyan listed insurers released their H1'2021 results, recording a weighted average increase in core earnings per share of 127.6%, an improvement, compared to an average decline of (280.5%) in H1'2020. The table below highlights the performance of the listed insurance sector, showing the performance using several metrics, and the key take-outs of the performance:

Listed Insurance Companies H1'2021 Earnings and Growth Metrics

Insurance	Core EPS Growth	Net Premium growth	Claims growth	Loss Ratio	Expense Ratio	Combined Ratio	ROaE	ROaA
CIC Group	177.3%	0.5%	7.0%	81.3%	50.8%	132.1%	3.4%	0.6%
Jubilee Holdings	146.2%	10.0%	42.1%	109.6%	30.4%	140.0%	12.5%	3.1%
Britam Holdings	123.0%	2.4%	15.8%	78.5%	79.4%	157.8%	1.7%	0.3%
Sanlam Kenya	68.8%	45.9%	64.9%	92.8%	47.1%	140.0%	(19.3%)	(0.9%)
Liberty Holdings	(20.4%)	(5.7%)	32.5%	75.0%	84.3%	159.3%	3.1%	0.7%
***H1'2021 Weighted Average**	**127.6%**	**6.3%**	**29.1%**	**92.8%**	**53.8%**	**146.6%**	**6.2%**	**1.6%**
****H1'2020 Weighted Average**	**(280.5%)**	**5.1%**	**6.5%**	**75.0%**	**48.8%**	**123.8%**	**2.0%**	**0.6%**

The key take-outs from the above table include;

i. Core EPS growth recorded a weighted growth of 127.6%, compared to a weighted decline of 280.5% in H1'2020. The increase in earnings was attributable to increased premiums during the period following robust recovery by the sector from the COVID-19 pandemic, coupled with gains recorded in the equities markets and higher yields from government papers,

ii. The premiums grew at a faster pace of 6.3% in H1'2021, compared to a growth of 5.1% in H1'2020, while claims grew at an aggressive faster rate of 29.1% in H1'2021, from the 6.5% recorded in H1'2020 on a weighted average basis,

iii. The loss ratio across the sector increased to 92.8% in H1'2021, from 75.0% in H1'2020, owing to increased claims in insurance sub sectors such as motor and medical and perennial challenges facing the industry such as fictitious claims and increased benefit payments from the life business owing to job layoffs,

iv. The expense ratio increased to 53.8% in H1'2021, from 48.8% in H1'2020, owing to an increase in operating expenses,

v. The insurance core business still remains unprofitable, with a combined ratio of 146.6% as at H1'2021, compared to 123.8% in H1'2020, and,

vi. On average, the insurance sector delivered a Return on Average Equity (ROaE) of 6.2%, an increase from a weighted Return on Average Equity of 2.0% in H1'2020.

For more information, see our Kenya H1'2021 Listed Insurance Report.

Other Key Results

Safaricom Limited released the H1'2022 results, recording core earnings per share increase of 12.1% to Kshs 0.9, from Kshs 0.8 in H1'2021. The increase in the earnings growth was attributable to the 45.8% increase in M-PESA revenue to Kshs 52.3 bn, from Kshs 35.9 bn in H1'2021, following the lifting of the waiver by the Central Bank of Kenya on all charges for transactions below Kshs 1,000.

This year, 4 companies issued profit warnings to investors compared to 15 companies in 2020, and 10 companies in 2019, as a results of the improved business environment following the lifting of COVID-related restrictions. Companies are required to issue profit warnings if they project a more than 25.0% decline in profits year-on-year. Below is the summary of the said companies:

Companies that issued profit warnings

No	2021	2020	2019
1	Centum Investment Company PLC	ABSA Kenya	Nairobi Stock Exchange
2	Umeme Limited	Diamond Trust Bank	BOC Kenya Plc
3	Williamson Tea Kenya PLC	Standard Chartered	UAP Holdings Limited
4	WPP ScanGroup PLC	I&M Holdings	Kenya Power and Lightning Company
5		NCBA Group	Eaagads
6		Britam Holdings	Williamson Tea Kenya
7		East African Breweries Limited	Standard Group Plc
8		Nation Media Group	CIC Insurance
9		Longhorn Publishers	Kenya Airways
10		Kenya Power	Kapchorua Tea Company
11		Unga Group	
12		East Africa Cables	
13		Kenya Orchards	
14		TPS East African	
15		Nairobi Business Ventures	

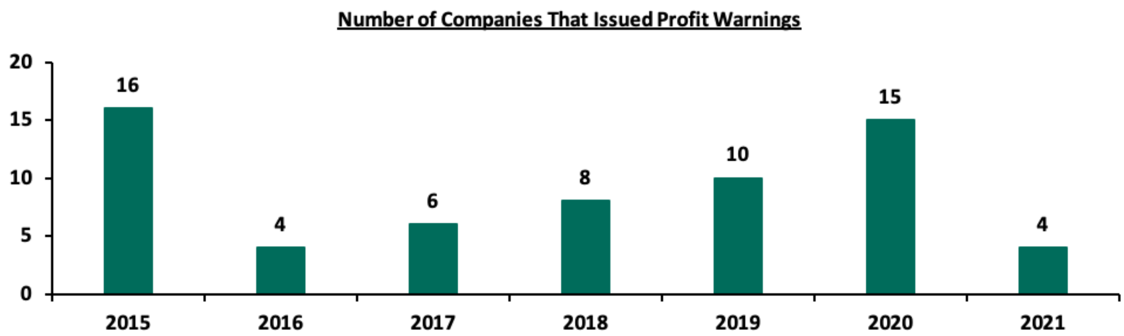
The key take-outs from the table above include:

i. Centum Investment Company Limited attributed the shortfall in profits to the impact of COVID-19 on their Private Equity portfolio businesses and the lack of gains on disposal of investments in the financial year ending 31st March 2021. Centum had registered significant gains on disposal of investments totalling Kshs 12.5 bn in the previous financial year ending 31st March 2020. Additionally, Centum pointed to the revenue recognition of sales in the Real Estate business as another reason for the depressed profit level, as sales revenues are only recognized once ownership of the real estate residential units are transferred to the new owners,

ii. Umeme Limited issued a profit warning statement attributing dismal performance to the attributed to (i) the effects of the Covid-19 pandemic as restrictions put in place which led to a 9.0% decline in Commercial, medium-industrial and large industrial electricity demand, (ii) regulatory lag, and, (iii) suspension of the Government's free connections policy,

iii. Williamson Tea Kenya PLC also issued a profit warning citing that the pandemic adversely affected the property market leading to a loss on revaluation of the firm's investment properties. Williamson Tea also cited rising production costs and lower global market prices as contributing factors to their depressed bottom-line in the financial year ending 31st March 2021, and,
iv. WPP ScanGroup cited that the impact of discontinued operations in 2020, when the company disposed of its interest in Millward Brown East Africa Limited, Millward Brown West Africa Limited, Millward Brown Nigeria and Research and Marketing Group Limited, on 30th June 2020, as the reason for the firm's lower earnings.

Below is a summary of the number of companies that issued profit warnings over the last 7 years:



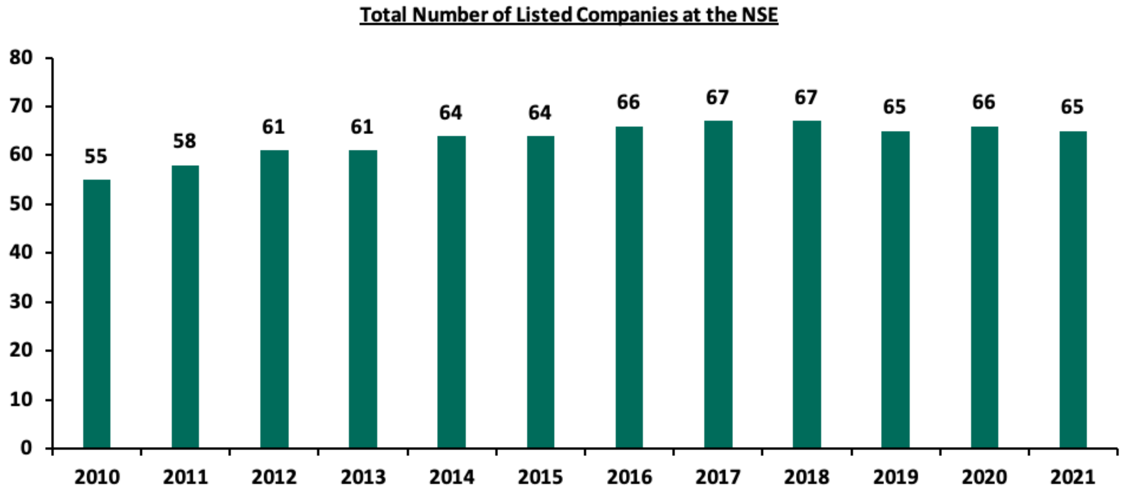
Source: Cytonn Research, NSE

1. **Listings and Suspensions**

During the year, the Nairobi Securities Exchange (NSE) delisted National Bank of Kenya (NBK), effective 25th November 2021. This came after the successful takeover by KCB of 100.0% of all the ordinary shares of National Bank of Kenya (NBK) through a share swap of 1 ordinary share of KCB for every 10 NBK shares, after the Capital Markets Authority (CMA) approved the acquisition in September 2019. The de-listing was approved by both the CMA and the shareholders of NBK. NBK became the 13th firm since 2001 to be de-listed in the NSE with Kenol/Kobil being the most recent exit in August 2019. The table below shows the delisted companies and the year they were delisted in:

No.	**Company Name**	**Year of De-listing**
1.	East African Packaging Industries	2001
2.	Africa Online Holding Ltd	2003
3.	Unilever Tea Kenya	2008
4.	Access Kenya	2013
5.	City Trust Ltd	2013
6.	Rea Vipingo Plantations Limited	2015
7.	CMC Holdings	2015
8.	Atlas Development and Support Services	2017
9.	Marshall East Africa Limited	2017
10.	Hutchings Biemer	2018
11.	A. Baumann & Co. Limited	2018
12.	Kenol/Kobil	2019
13.	National Bank of Kenya	2021

The chart below shows the number of listed companies in the Nairobi Securities Exchange (NSE) for the period 2010 - 2021:



Source: CMA Quarterly Statistical Bulletins

IV. **Liquidations**

During the year, the Central Bank of Kenya (CBK) approved the liquidation of three banks; namely, Chase Bank Limited (In Receivership), Imperial Bank Limited (In Receivership) and Charterhouse Bank Limited. Charterhouse Bank had been under statutory management since 23rd June, 2006 over severe violations of the Banking Act relating to lending, accuracy of returns submitted to CBK, and failure to obtain account opening documentation for a number of customers. The bank's liquidation was announced on 7th May 2021, with the Kenya Deposit Insurance Corporation (KDIC) being appointed as the liquidator in order to protect the interest of the bank's depositors, its creditors, and other stakeholders. Charterhouse Bank had assets totalling Kshs 4.0 bn and deposits totalling Kshs 2.9 bn, as of 2006.

For both Chase Bank and Imperial Bank, KDIC acted as the receiver and liquidation approvals came after recommendation by KDIC that liquidation was the only feasible option going forward. Chase Bank Limited (In Receivership) (CBLIR)'s liquidation announcement was made in 16th April 2021, and came five years after CBK appointed KDIC as the receiver for Chase Bank Limited on April 7, 2016. Please see our Note on the Liquidation of Chase Bank Limited, In Receivership (CBLIR) for a detailed analysis. We expect total recoveries of Kshs 59.6 bn out of the total Kshs 76.1 bn in deposits held by Chase Bank Limited In Receivership; resulting in a potential loss of Kshs 16.5 bn. This represents a 78.3% recovery rate. Out of the Kshs 59.6 bn recoveries, Kshs 57.1 bn is the deposits amount transferred to SBM Bank (K) and expected to be fully recovered while Kshs 2.5 bn is the maximum amount to be paid by KDIC after liquidation.

Additionally, CBK announced on 9th December 2021, 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. Imperial Bank Limited was put under receivership by 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. According to CBK, 37.3% of the total deposits will be recovered, totalling Kshs 21.7 bn. Out of the 50,000 depositors, 45,700 will be paid fully representing 91.4% of the total depositors. For more information on the liquidation of Imperial Bank Limited In Receivership (IBLIR), please see our Cytonn Weekly #49/2021.

V. **Legislations and other Developments**

The year 2021 saw a number of legislative changes and other developments that affected the equities market and investor sentiment, namely:

a. **Guidance on Loan Restructuring:** The Central Bank of Kenya announced that the emergency measures on restructuring of loans for bank borrowers put in place in March 2020, expired on 2nd March 2021. The circular, intended to cushion the borrowers from the adverse effects of the pandemic, provided commercial banks and mortgage finance companies with guidelines on loan reclassification, and provisioning of extended and restructured loans as per the Banking Circular No 3 of 2020. According to the Central Bank, the measures were highly effective, giving borrowers restructuring options which included moratorium on principle or interest and waivers on interest fees. The measures gave borrowers room to readjust their businesses and operations to the 'new normal' in addition to helping mitigate job losses. The banking sector also benefitted from the measures, presenting banks with the opportunity to re-evaluate their loan books, build additional capital and liquidity buffers and minimizing the effect of the pandemic on their Non-Performing Loan book,
b. **Draft CMA Investments Regulations:** In August 2021, the Cabinet Secretary for the National Treasury and Planning, through the Capital Markets Authority (CMA), published 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 CIS regulations seek to update the current Collective Investment Scheme regulations given the changes in the market dynamics since the last published Regulations in 2001, as well as address emerging issues. Additionally, the draft Alternative Investment Funds' (AIFs) regulations seek to create a regulatory environment for privately pooled funds whose investors seek higher returns by investing in specified alternative asset classes including Debt funds, Equity and equity linked investments, Hedge funds, or infrastructure. For a detailed analysis of the draft regulations, please see our Cytonn Weekly#37/2021. However, we still await the release of the Regulatory Impact Assessment by the regulator and a revised draft taking into account market commentaries,
c. **Integration of Climate-Related Risk Management:** In October 2021, the Central Bank of Kenya (CBK) released Guidance on Climate-Related Risk Management, highlighting that all banks and mortgage finance companies ought to integrate the risks and opportunities arising from climate change in their risk management, strategy and governance structure. Opportunities expected to arise from climate change include financing activities such as the transition to renewable energy, appropriate housing, resilient infrastructure and innovative agricultural practices. On the other hand, banks are expected to build their capacity going forward to identify and mitigate the risks arising from climate change,
d. **Guidelines on Buybacks for Listed Companies** - In November 2021, the Capital Market Authority (CMA) released guidelines on share buybacks for listed companies, following the issuance of proposed guidelines on share buy-backs, in June 2020, which have been in the process of revision following public participation. The guidelines are in line with Part XVI, Section 447 of the Companies Act, 2015, that introduced a share buyback option for publicly traded companies and aims to enhance investor protection, promote liquidity and ensure transparency in share buyback transactions.The new guidelines came after Nation Media Group (NMG) became the first listed company in the Nairobi Stock Exchange (NSE) to conduct a share buyback which ran from 28th June 2021 to 24th September 2021, which saw NMG acquire 17.1 mn ordinary shares out of the targeted 20.7 mn ordinary shares, representing an 82.5% success rate. For more information on the guidelines, please see our Cytonn Weekly #46/2021,
e. **Suspension of the Listing of Borrower's Negative Credit Information**: On 8th November 2021, the Central Bank of Kenya (CBK) announced a 12 months suspension of listing of negative credit information for borrowers with loans below Kshs 5.0 mn, whose loans were performing previously, but have become non-performing from 1st October, 2021. The move by the CBK is an intervention measure aiming to cushion Micro Small and Medium Enterprises from adverse

effects of the COVID-19 pandemic,

f. **Central Bank of Kenya Amendment Act, 2021** - In December 2021, President Uhuru Kenyatta 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.
g. **Consolidation:** Consolidation activity remained one of the key highlights witnessed in 2021, as players in the sector were either acquired or merged, leading to the formation of relatively larger, well capitalized, and possibly more stable entities. The following were some of the major M&A's activities witnessed during the year:

    a. In May 2021, Equity Group disclosed that it had 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 followed 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. The BCDC subsidiary is already the second largest most profitable regional subsidiary, having contributed Kshs 1.3 bn to the Group's Profit After Tax of Kshs 20.1 bn in 2020. Read more information on the transaction here,
    b. In May 2021, 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. Read more on the same here,
    c. On 25th August 2021, KCB Group announced that it had completed the 62.1% acquisition of Banque Populaire du Rwanda Plc (BPR), after receiving all the required regulatory approvals. KCB Group had agreed to purchase 62.1% stake in BPR from Atlas Mara Limited using a Price to Book Value (P/Bv) of 1.1x. According to the latest BPR financials released as of June 2021, the bank had a book value of Rwf 52.9 bn (Kshs 5.8 bn), and thus at the trading multiple of 1.1x, we expect KCB Group to have spent an estimated Kshs 6.3 bn to acquire BPR Rwanda. The valuation of 1.1x P/Bv is lower than the 7-year average which is at 1.3x 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 1.0x as of Q1'2021. Additionally, KCB Group will take over 135 branches from BPR, taking its total branches to 489, from 354 branches as of June 2021. Read more information on the transaction here,
    d. On 14th September 2021, Liberty Holdings Limited (Liberty), a financial services and property holding company completed the acquisition of 84.2 mn shares in Liberty Kenya Holdings Plc (Liberty Kenya), which represents 15.7% of the company's issued share capital. This followed the June 2021 announcement of Liberty Holdings intention to buy 49.5 mn ordinary shares from the Conrad N. Hilton Foundation, Kimberlite Frontier Africa Master Fund, L.P. and Vanderbilt University (the KFAMF Acquisition), and a further 34.7 mn ordinary shares from Coronation Africa Frontiers Fund and Coronation All Africa Fund (the Coronation Acquisition), which represented 9.3% and 6.5% of the company's shareholding, respectively. The completed acquisition has increased Liberty Holding's stake to 73.5% (393.6 mn ordinary shares), from the current 57.7% (309.3 mn ordinary shares), retaining Liberty Holding's status as the largest

shareholder of Liberty Kenya. Read more information on the transaction here, and,

e. In November 2021, HF Group announced the invitation of strategic investors to acquire a stake in the Company following a Proposed Transaction disclosure in their published FY'2020 Financial Statements. The Proposed Transaction aims to inject capital to the company so as to increase its liquidity and enable expansion into mainstream banking including retail and SME lending, while also reducing reliance on the Real Estate market segment. This comes after the Kshs 1.0 bn capital injection the group received from its top shareholder, Britam Holdings Plc, in January this year, which aimed at growing the firm's full-service banking offering. The price at which an investor will buy a stake in the company is expected to be based on negotiations with the issuer. Read more on the same here.

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	5.3	100.0%	5.6	1.1x	August 2021
KCB Group**	ABC Tanzania	Unknown	100%	0.8	0.4x	Nov-20*
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

Acquirer	Bank Acquired	Book Value at Acquisition (Kshs bn)	Transaction Stake	Transaction Value (Kshs bn)	P/Bv Multiple	Date
Average			**76.7%**		**1.3x**	

*** Announcement Date**
**** Deals that were dropped**

In 2021, Kenya's operating environment was characterized by a relatively improved macro-economic environment owing to the easing of the COVID-19 restrictions in the country coupled with the gradual recovery in various sectors of the economy. In 2021, the market remained slumped with NASI's P/E of 11.3x trading below its' historical average of 12.9x, and below the most recent peak of 15.9x in April 2018, showing that pockets of value still exist. 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.