Cytonn Q1’2022 Markets Review

Equities

Market Performance:

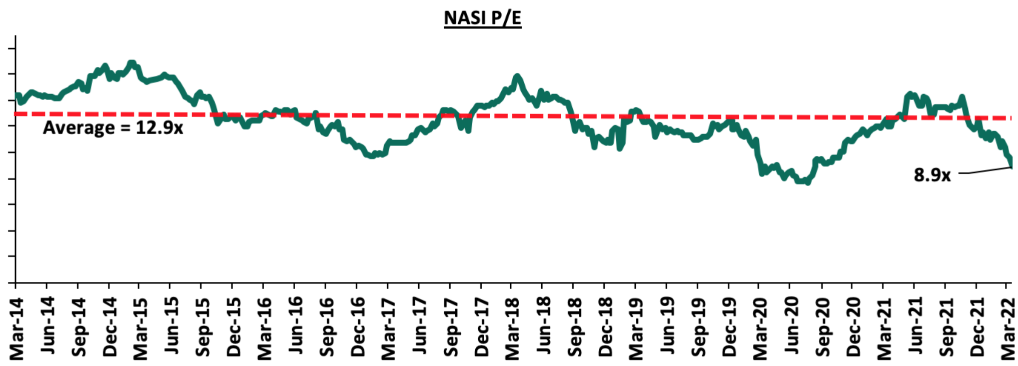
During Q1’2022, the equities market was on a downward trajectory, with NASI, NSE 20 and NSE 25 declining by 6.4%, 2.9% and 4.8%, respectively, taking their YTD performance as at the end of March to losses of 6.8%, 3.5% and 5.1% for NASI, NSE 25 and NSE 20 respectively. The equities market performance during the quarter was driven by losses recorded by large caps such as Safaricom, EABL, Bamburi and Equity Group of 10.0%, 9.1%, 5.9% and 4.3%, respectively. The losses were however mitigated by gains recorded by stocks such as BAT, Standard Chartered Bank (SCBK), ABSA and NCBA Group of 12.4%, 12.1%, 5.1% and 2.6%, respectively.

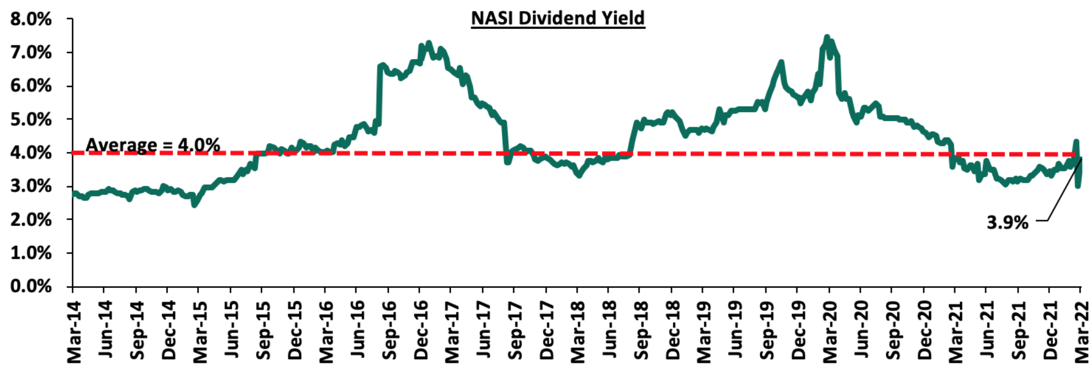
Equities turnover declined by 24.8% during the quarter to USD 244.0 mn, from USD 324.2 mn in Q4’2021. Foreign investors remained net sellers during the quarter, with a net selling position of USD 14.8 mn, from a net selling position of USD 72.9 recorded in Q4’2020.

During the week, the equities market was on a downward trajectory, with NASI, NSE 20 and NSE 25 declining by 2.7%, 0.9% and 2.3%, respectively, driven by losses recorded by Equity Group, Safaricom, Co-operative Bank and ABSA of 4.6%, 4.0%, 2.3% and 2.0%, respectively. The losses were however mitigated by gains recorded by stocks such as Diamond Trust Bank (DTB-K) and Bamburi of 3.1% and 1.1%, respectively.

During the week, equities turnover declined by 16.3% to USD 17.0 mn from USD 20.2 mn recorded the previous week, taking the YTD turnover to USD 248.2 mn. During the week, foreign investors remained net sellers, with a net selling position of USD 3.0 mn, from a net selling position of USD 0.9 mn recorded the previous week, taking the YTD net selling position to 14.8 mn.

The market is currently trading at a price to earnings ratio (P/E) of 8.9x, 30.9% below the historical average of 12.9x, and a dividend yield of 3.8%, 0.2% points below the historical average of 4.0%. Notably, this week’s P/E is the lowest it has been since August 2020. Key to note, NASI’s PEG ratio currently stands at 1.1x, an indication that the market is trading at a premium to its future earnings growth. 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 8.9x is 15.6% 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.





Earnings Releases:

i. **Asset Quality**

The table below is a summary of the asset quality for the banks that have released

	FY'2020 NPL Ratio**	FY'2021 NPL Ratio*	% point change in NPL Ratio	FY'2020 NPL Coverage**	FY'2021 NPL Coverage*	% point change in NPL Coverage
ABSA Bank Kenya	7.7%	7.9%	0.2%	71.1%	77.7%	6.6%
KCB	14.8%	16.6%	1.8%	59.8%	52.9%	(6.9%)
Equity Group	11.5%	8.6%	(2.9%)	62.4%	68.7%	6.3%
NCBA Group	14.7%	16.0%	1.3%	60.9%	73.6%	12.7%
Standard Chartered Bank Kenya	16.0%	16.0%	(0.0%)	80.6%	84.4%	3.8%
Stanbic Bank	11.8%	9.3%	(2.5%)	60.6%	51.8%	(8.8%)
I&M Holdings	11.6%	9.5%	(2.1%)	66.8%	71.4%	4.6%
Diamond Trust Bank	11.9%	12.9%	1.0%	40.0%	41.8%	1.8%
Co-operative Bank of Kenya	18.7%	14.6%	(4.1%)	50.3%	60.6%	10.3%
HF Group	24.6%	21.1%	(3.5%)	63.4%	73.6%	10.2%
Mkt Weighted Average	**13.3%**	**12.2%**	**(1.1%)**	**62.3%**	**65.3%**	**3.0%**

***Market cap weighted as at 01/04/2022**

****Market cap weighted as at 15/04/2021**

Key take-outs from the table include;

ii. Asset quality for the listed banks that have released their FY'2021 results improved during the period, with the weighted average NPL ratio declining by 1.1% points to a market cap weighted average of 12.2%, from an average of 13.3% for the listed banking sector in FY'2020. The improvement in asset quality is attributable to declining credit risk on the back of increased business activities in 2021 driven by the gradual economic recovery,

iii. NPL Coverage for the listed banks increased to a market cap weighted average of 65.3% in FY'2021, from 62.3% recorded in FY'2020, as the banks increased their provisioning levels to proactively manage risks brought about by the emergence of new COVID-19 variants coupled with the slow recovery of some sectors such as tourism and hospitality and,

iv. KCB Group recorded a decline in their NPL coverage despite the NPL ratio rising, which would suggest modest provisioning. Given the slow recovery in some sectors locally and the high NPL ratios in some of the group's subsidiaries, we expected the group to maintain the high provisioning to cater for the existing credit risk. Key to note, if KCB's NPL Coverage remained at the 59.8% level recorded in 2020, the bank would have had an additional provisioning of Kshs 8.4 bn, which would have reduced the earnings per share from the reported Kshs 10.6 to Kshs 8.6.

ii. **Summary Performance**

The table below highlights the performance of the banks that have released so far, 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	161.2%	1.9%	15.9%	8.0%	7.1%	4.7%	31.6%	11.6%	5.9%	5.2%	87.2%	12.20%	21.1%
NCBA	123.7%	5.1%	3.9%	6.1%	5.9%	5.6%	45.0%	2.5%	11.5%	20.9%	51.9%	(1.8%)	13.6%
Equity	99.4%	27.9%	37.2%	24.8%	6.8%	15.8%	39.3%	29.4%	29.5%	30.0%	61.3%	23.0%	26.6%
KCB	74.3%	15.1%	17.6%	14.4%	8.4%	8.8%	28.0%	9.0%	9.1%	29.7%	80.7%	13.5%	21.8%
SCBK	66.2%	(6.1%)	(24.7%)	(1.6%)	6.4%	24.9%	35.5%	19.9%	3.5%	(4.2%)	47.5%	3.7%	17.4%
HF Group	65.1%	(8.0%)	(12.7%)	(2.1%)	4.2%	3.6%	22.8%	21.2%	(5.6%)	7.8%	92.0%	6.2%	(7.2%)
COOP	53.0%	13.9%	17.0%	12.9%	8.0%	11.0%	32.1%	18.1%	7.7%	13.7%	76.1%	8.2%	17.3%
Stanbic	43.2%	1.6%	15.2%	12.2%	6.2%	4.2%	42.6%	(8.5%)	(5.8%)	(17.4%)	83.0%	11.2%	14.0%
DTB	25.1%	9.1%	6.9%	10.6%	5.1%	3.0%	24.0%	10.8%	11.2%	11.9%	66.5%	5.7%	6.8%
I&M	0.7%	18.8%	(0.4%)	33.8%	6.3%	1.1%	29.0%	16.9%	13.0%	23.4%	71.0%	12.4%	12.2%
FY'21 Mkt Weighted Average*	**83.2%**	**14.0%**	**17.1%**	**15.4%**	**7.1%**	**10.9%**	**34.6%**	**15.9%**	**13.4%**	**18.4%**	**70.1%**	**13.2%**	**20.3%**
FY'20 Mkt Weighted Average**	**(26.8%)**	**16.7%**	**12.5%**	**18.9%**	**7.3%**	**6.4%**	**35.4%**	**(2.1%)**	**22.3%**	**26.3%**	**69.8%**	**11.7%**	**13.2%**

***Market cap weighted as at 01/04/2022**

****Market cap weighted as at 15/04/2021**

Key takeaways from the table above include:

i. The listed banks that have released recorded an 83.2% weighted average growth in core Earnings per Share (EPS), compared to a weighted average decline of 26.8% in FY'2020 for the listed banking sector. The performance is however largely skewed by the strong performance from ABSA Bank and NCBA whose core EPS grew by 161.2% and 123.7%, respectively,

ii. The Banks have recorded a weighted average deposit growth of 13.4%, slower than the 22.3% growth recorded in FY'2020,

iii. Interest expense grew at a faster pace, by 17.4%, compared to the 12.5% growth in FY'2020. On the other hand, cost of funds declined, coming in at a weighted average of 2.8% in FY'2021, from 2.9% in FY'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 13.2%, 1.5% points lower than the 11.7% growth recorded in FY'2020. Additionally, the loan growth was lower than the 18.4% growth in government securities, an indication that banks shied away from lending due to uncertainties surrounding the emergence of new COVID-19 variants coupled with the slow recovery of some sectors such as tourism and hospitality,

v. Interest income grew by 14.0%, compared to a growth of 16.7% recorded in FY'2020 while the weighted average Yield on Interest Earning Assets (YIEA) increased to 9.7%, from the 9.5% recorded in FY'2020 for the listed banking sector, an indication of the increased allocation to higher-yielding assets by the sector during the period. Net Interest Margin (NIM) now stands at 7.1%, 0.2% points lower than the 7.3% recorded in FY'2020 for the whole listed banking sector, and,

vi. Non-Funded Income grew by 10.9%, compared to the 6.4% growth recorded in FY'2020. This can be attributable to the faster growth in the fees and commission which grew by 11.0% compared to a decline of 2.1% in FY'2020, following the expiry of the waiver on fees on mobile transactions.

For the various earnings notes of the various companies, click these links:

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

Quarterly Highlights:

During the quarter;

i. The International Finance Corporation (IFC) disclosed that it would disburse USD 165.0 mn (Kshs 18.6 bn) to Equity Bank Kenya Limited in form of a 7-year Tier 2 subordinated loan. This amount is expected to be used to shore up the Bank's Tier 2 capital and for onward lending to climate smart projects and Small and Medium Enterprises (SMEs) in Kenya. For more information, please see our Cytonn Weekly #01/2022,
ii. Equity Group Holdings (EGH), announced the completion of the incorporation of a subsidiary, Equity Group Insurance Holdings Limited, a non-operating insurance holding company and issuance of a life insurance license to Equity Life Assurance Kenya (ELAK) Limited. ELAK, which is fully owned by Equity Group Insurance Holdings Limited, will conduct and undertake long-term insurance business in Kenya. This came after EGH obtained the prerequisite approvals from its shareholders and the Central Bank of Kenya (CBK), before subsequent registration and licensing from the Insurance Regulatory Authority (IRA) on 10th January 2022. For more information, please see our Cytonn Weekly #02/2022,
iii. The Central Bank of Kenya (CBK) recently released the Quarterly Economic Review for the period ending 30th September 2021, highlighting that the banking sector's total assets increased by 10.6% to Kshs 5.8 tn, from Kshs 5.3 tn in September 2020. The sector's Profit before Tax (PBT) increased by 68.2% to Kshs 49.1 bn, from Kshs 29.2 bn recorded in September 2020. For more information, please see our Cytonn Weekly #04/2022
iv. Moody's Rating Agency rated the Kenyan banking sector as stable following the banks' impressive performance in the eleven months to November 2021, with the profits before tax coming in at Kshs 178.8 bn exceeding the pre-pandemic earnings of Kshs 150.1 bn over the same period in 2019. The gradual economic recovery is expected to support banks in improving their loan quality and profitability, while capital, funding, and liquidity will remain strong, in line with our Q3'2021 Banking Sector report. For more information, please see our Cytonn Weekly #06/2022,
v. Standard Africa Holdings Limited (SAHL), the majority shareholder in Stanbic Holdings, announced that it had received regulatory approval from the Capital Markets Authority for further extension to acquire increased stake of up to 75.0% in Stanbic Holdings. This comes after SAHL had received an exemption from making a full take-over under the Capital Markets (Take over and Mergers) Regulations, 2002 in July 2018. Under the exemption, SAHL aims to bring its total shareholding to up to 75.0% of Stanbic Holdings' ordinary shares, from 72.3% as of 31st December

2021. For more information, please see our Cytonn Weekly #07/2022,

vi. The Central Bank of Kenya (CBK), released the Commercial Banks' Credit Survey Report for the quarter ended December 2021. The quarterly Credit Officer Survey is undertaken by the CBK to identify the potential drivers of credit risk in the banking sector. During the quarter, 38 operating commercial banks and 1 mortgage finance company participated in the Commercial Banks Credit Officer Survey. The report highlights that the banking sector's loan book recorded an 8.3% y/y growth, with gross loans increasing to Kshs 3.3 tn in December 2021, from Kshs 3.0 tn in December 2020. For more information, kindly see our Cytonn Weekly #10/2022,

vii. The Central Bank of Kenya (CBK) released the Quarterly Economic Review Report October-December 2021, highlighting that the sector's total assets increased by 10.8% to Kshs 6.0 tn in December 2021, from Kshs 5.4 tn in December 2020 and Profit before Tax (PBT) increased by 0.4% to Kshs 49.3 bn, from Kshs 49.1 bn in Q4'2020. For more information, kindly see our Cytonn Weekly #12/2022, and,

viii. The Insurance Regulatory Authority of Kenya (IRA) released the Quarterly Insurance Industry Report for the period ended 31st December highlighting that the industry's gross premiums rose by 18.5% to Kshs 276.1 bn, from Kshs 233.0 bn recorded in Q4'2020, with the general insurance business contributing 55.2% of the industry's premium income, a 1.0% point decline from the 56.2% contribution witnessed in Q4'2020. For more information, kindly see our Cytonn Weekly #12/2022.

Cytonn Coverage:

Company	Price as at 25/03/2022	Price as at 1/04/2022	w/w change	q/q change	YTD Change	Year Open 2022	Target Price*	Dividend Yield	Upside/ Downside**	P/TBv Multiple	Recommendation
Kenya Reinsurance	2.3	2.2	(1.8%)	(2.2%)	(3.5%)	2.3	3.2	4.5%	48.4%	0.2x	Buy
Jubilee Holdings	274.0	274.8	0.3%	(14.1%)	(13.3%)	316.8	381.7	5.1%	44.0%	0.5x	Buy
Liberty Holdings	6.3	5.7	(8.9%)	(15.4%)	(19.3%)	7.1	7.7	0.0%	34.4%	0.4x	Buy
I&M Group***	21.2	20.5	(3.3%)	(0.9%)	(4.2%)	21.4	24.4	7.3%	26.2%	0.6x	Buy
KCB Group***	44.0	44.0	0.0%	(3.1%)	(3.4%)	45.6	51.4	6.8%	23.5%	0.9x	Buy
Equity Group***	51.5	49.2	(4.6%)	(4.3%)	(6.8%)	52.8	56.6	6.1%	21.3%	1.3x	Buy
Britam	6.8	6.7	(2.3%)	(11.5%)	(11.6%)	7.6	7.9	0.0%	17.9%	1.1x	Accumulate
NCBA***	25.9	25.9	0.0%	2.6%	1.8%	25.5	26.4	11.6%	13.5%	0.6x	Accumulate
Co-op Bank***	12.9	12.6	(2.3%)	(0.8%)	(3.1%)	13.0	13.1	7.9%	11.6%	0.9x	Accumulate
Diamond Trust Bank***	57.0	58.8	3.1%	(0.8%)	(1.3%)	59.5	61.8	5.1%	10.3%	0.3x	Accumulate
Sanlam	11.4	11.0	(3.5%)	(4.8%)	(4.8%)	11.6	12.1	0.0%	9.6%	1.2x	Hold
Stanbic Holdings	102.0	104.8	2.7%	18.1%	20.4%	87.0	105.2	8.6%	9.0%	0.9x	Hold
ABSA Bank***	12.4	12.0	(2.8%)	5.1%	2.1%	11.8	11.9	9.2%	8.4%	1.2x	Hold
Standard Chartered***	142.0	143.8	1.2%	12.1%	10.6%	130.0	137.7	9.7%	5.5%	1.1x	Hold
HF Group	3.2	3.2	(2.5%)	(19.0%)	(17.1%)	3.8	3.0	0.0%	(6.2%)	0.2x	Sell
CIC Group	2.0	2.2	10.0%	(2.3%)	1.8%	2.2	1.9	0.0%	(14.8%)	0.8x	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 "Neutral" on the Equities markets in the short term. With the market currently trading at a premium to its future growth (PEG Ratio at 1.1x), we believe that investors should reposition towards value stocks with strong earnings growth and that are trading at discounts to their intrinsic value. We expect the discovery of new COVID-19 variants, the upcoming Kenyan general elections and the slow vaccine rollout to continue weighing down the economic outlook. On the upside, we believe that the relaxation of COVID-19

containment measures in the country will lead to improved investor sentiments.

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