

# Administration as a Business Restructuring Option & Cytonn Weekly #37/2022

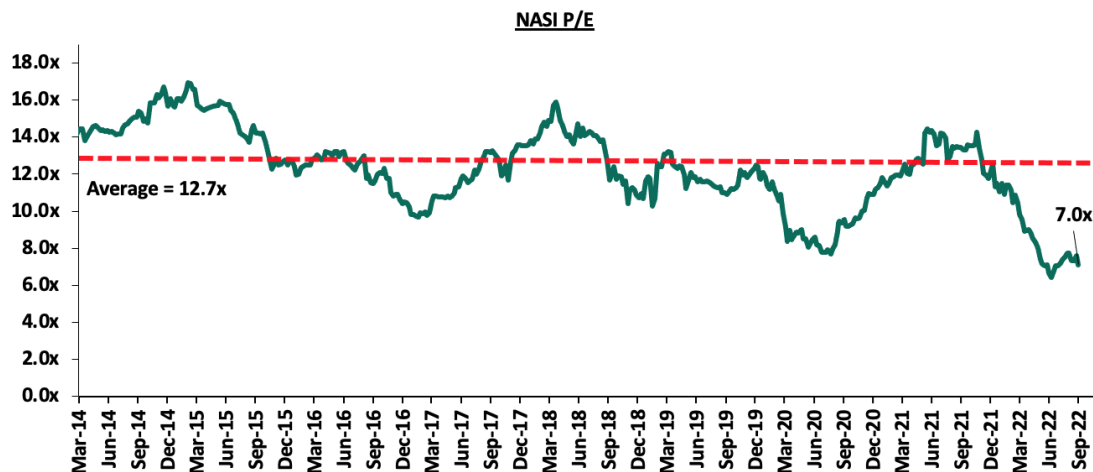
## Equities

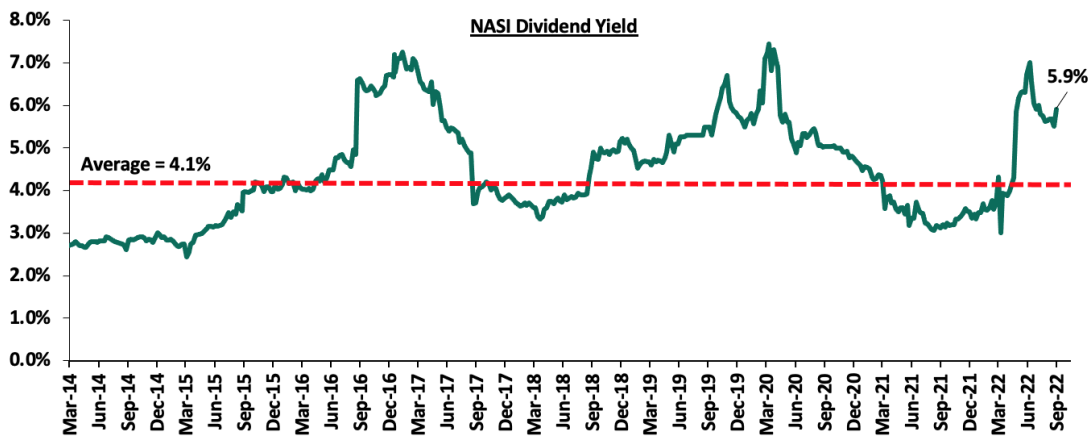
### Markets Performance

During the week, the equities market was on a downward trajectory with NASI, NSE 20 and NSE 25 declining by 6.6%, 2.2% and 5.5% respectively, taking their YTD performance to losses of 20.8%, 8.7% and 16.0%, for NASI, NSE 20 and NSE 25, respectively. The equities market performance was mainly driven by losses recorded by large-cap stocks such as Safaricom, KCB Group, NCBA and EABL of 9.2%, 8.0%, 7.7% and 7.2%, respectively. The losses were slightly mitigated by gains recorded by stocks such as Sanlam Kenya of 5.5%.

During the week, equities turnover increased by 59.3% to USD 21.4 mn, from USD 13.5 mn recorded the previous week, taking the YTD turnover to USD 621.7 mn. Foreign investors remained net sellers, with a net selling position of USD 4.6 mn, from a net selling position of USD 0.6 mn recorded the previous week, taking the YTD net selling position to USD 152.5 mn.

The market is currently trading at a price to earnings ratio (P/E) of 7.0x, 44.8% below the historical average of 12.7x, and a dividend yield of 5.9%, 1.8% points above the historical average of 4.1%. Key to note, NASI's PEG ratio currently stands at 0.9x, an indication that the market is undervalued relative to its future 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 charts below indicate the historical P/E and dividend yields of the market:





## Weekly Highlight:

### Equity Group Holdings' acquisition of Spire Bank

During the week, Equity Group Holdings Plc through Equity Bank (Kenya) Limited, announced that it had entered into an Assets and Liabilities purchase agreement with Spire Bank Limited for purchase of certain assets and liabilities. In this deal which is anchored in Equity's plan to support economic recovery post COVID-19, Equity Bank Kenya Limited will acquire approximately 20,000 deposit customers with deposits totaling Kshs 1.3 bn, and 3,700 loan customers with outstanding loan balances at Kshs 1.7 bn, with a net carrying value of Kshs 0.9 bn after adjusting for statutory loan loss provisions of Kshs 0.8 bn. Upon completion of the proposed transaction on 30<sup>th</sup> November 2022, all existing depositors of Spire Bank with exemption of deposits from Mwalimu National Sacco will become customers of Equity Bank Kenya, which ensures preservation of their deposits.

Upon completion of the proposed transaction, Mwalimu Sacco, which owns Spire Bank will pay Equity Group an additional Kshs 1.7 bn to cover liabilities hence the P/Bv multiple in this transaction is inconsequential. Spire Bank, which is fully owned by Mwalimu National Sacco, reported a loss of Kshs 403.0 mn in H1'2022, a decrease of 21.4% from Kshs 512.9 in H1'2021. The Bank has been recording losses since 2013, when it last recorded a profit of Kshs 55.6 mn. The losses have eroded Spire Bank's shareholder's funds, which currently stand at a paltry Kshs 9.6 mn, with accumulated losses at Kshs 10.0 bn. Additionally, the bank's capital adequacy levels have also been adverse, with key ratios such as the core capital to liabilities ratio coming in at (40.8%), below the regulatory limit of 8.0%. Similarly, the core capital to risk weighted assets came in at (33.4%), 43.9% below the regulatory limit of 10.5% while the liquidity ratio came in 6.8%.

The combined pro-forma financials for the banks upon transaction approval are shown in the table below;

<b>Combined Pro-forma Balance Sheet</b>			
<b>Balance Sheet</b>	<b>Equity Group (Kshs bn)</b>	<b>Spire Bank (Kshs bn)</b>	<b>Combined Entity (Kshs bn)</b>
Net Loans (Kshs bn)	650.6	1.7	652.3
Customer deposits (Kshs bn)	970.9	1.3	972.2
Total assets (Kshs bn)	1,333.9	3.6	1,337.4
Total liabilities	1,183.5	2.9	1186.4

**\*Figures as of June 2022**

In our view, we commend Equity Group Holdings for coming to the aid of Spire Bank and preventing

collapse of another banking player, following the collapse of Imperial Bank, Dubai Bank and Chase Bank. We expect the bank to benefit from Equity Group's financial muscle and restore full operations and reverse the loss making trend. It is also commendable that the Central Bank of Kenya continued to support the bank with short term liquidity that ensured the bank stayed the course until it found a buyer, as compared to placing it under receivership. However, Spire Bank's weak capital adequacy underlines the challenges being faced by the tier 3 banks as the gap between them, tier 2 and tier 1 banks widens. As such, we expect to see more consolidation activities in the Kenyan Banking Sector as weaker banks are merged with the big banks to form a stronger banking system in order to boost their capital adequacy and liquidity ratios to the required minimum statutory levels.

Below is a summary of the deals in the last 8-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
Equity Group	Spire Bank	0.01	Undisclosed	Undisclosed	N/A	Sep-22
KCB Group	Trust Merchant Bank	12.4	85.0%	15.7	1.5x	Aug-22
Access Bank PLC	Sidian Bank	4.1	83.4%	4.3	1.1x	June-22*
KCB Group	Banque Populaire du Rwanda	5.3	100.0%	5.6	1.1x	Aug-21
I&M Holdings PLC	Orient Bank Limited Uganda	3.3	90.0%	3.6	1.1x	Apr-21
KCB Group**	ABC Tanzania	Unknown	100.0%	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	1.0	51.0%	Undisclosed	N/A	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	7.0	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	3.0	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

Acquirer	Bank Acquired	Book Value at Acquisition (Kshs bn)	Transaction Stake	Transaction Value (Kshs bn)	P/Bv Multiple	Date
I&M Holdings	Giro Commercial Bank	3.0	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
<b>Average</b>			<b>76.7%</b>		<b>1.2x</b>	

\* Announcement Date

\*\* Deals that were dropped

### Universe of Coverage

Company	Price as at 09/09/2022	Price as at 16/09/2022	w/w change	YTD Change	Target Price*	Dividend Yield	Upside/Downside**	P/TBv Multiple	Recommendation
Kenya Reinsurance	2.2	2.1	(2.8%)	(8.7%)	3.2	4.8%	56.9%	0.2x	Buy
Jubilee Holdings	245.0	245.3	0.1%	(22.6%)	379.4	0.4%	55.1%	0.4x	Buy
KCB Group***	42.5	39.1	(8.0%)	(14.3%)	53.5	7.7%	44.7%	0.7x	Buy
Sanlam	10.9	11.5	5.5%	(0.4%)	15.9	0.0%	38.3%	1.2x	Buy
Equity Group***	48.6	47.2	(2.9%)	(10.5%)	62.2	6.4%	38.2%	1.1x	Buy
Co-op Bank***	12.6	12.4	(1.6%)	(5.0%)	15.6	8.1%	34.4%	0.7x	Buy
ABSA Bank***	12.0	11.6	(2.9%)	(1.3%)	14.9	1.7%	30.2%	1.0x	Buy
I&M Group***	17.0	17.0	(0.3%)	(20.8%)	20.5	8.8%	30.0%	0.4x	Buy
Diamond Trust Bank***	50.5	50.0	(1.0%)	(16.0%)	59.5	6.0%	25.0%	0.2x	Buy
Standard Chartered***	139.0	136.3	(2.0%)	4.8%	155.0	10.3%	24.0%	0.9x	Buy
NCBA***	33.0	30.5	(7.7%)	19.6%	35.2	6.6%	22.0%	0.7x	Buy
Britam	6.7	6.5	(3.9%)	(14.3%)	7.7	0.0%	18.8%	1.1x	Accumulate
Stanbic Holdings	93.5	94.3	0.8%	8.3%	99.9	9.5%	15.5%	0.7x	Accumulate
Liberty Holdings	7.5	7.0	(6.2%)	(0.8%)	7.8	0.0%	11.4%	0.5x	Accumulate
HF Group	3.6	3.5	(2.0%)	(8.2%)	3.6	0.0%	2.6%	0.2x	Lighten
CIC Group	2.1	2.1	(0.9%)	(3.2%)	2.1	0.0%	0.0%	0.7x	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 due to the current adverse operating environment and huge foreign investor outflows, and, “Bullish” in the long term due to current cheap valuations and expected global and local economic recovery.*

*With the market currently trading at a discount to its future growth (PEG Ratio at 0.9x), 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 current high foreign investors sell-offs, and the slow vaccine rollout to continue weighing down the economic outlook in the short term.*

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