Cytonn H1’2018 Markets Review

F. Private Equity

Financial Services Sector:

The financial services sector remained attractive in H1’2018 for both local and international investors. Some of the key deals include;

1. Old Mutual, a UK based international financial services group providing investment and savings, insurance, asset management and retirement solutions, increased its stake in UAP Holdings in a deal to convert a Kshs 2.7 bn loan into equity through its subsidiary Old Mutual Holdings Kenya. The transaction was valued at a P/B multiple of 1.8x, a 15% discount from the average insurance sector transaction P/B multiple of 2.1x over the last seven years, hence a valuation discount. For more information, see our Cytonn Weekly #25/2018
2. European financial services company Allianz Group agreed to acquire 8.0% in African reinsurer Africa Re. The total cash consideration payable at closing amounted to Eur. 69.0 mn (Kshs 8.14 bn). An 8.0 % stake at Eur. 69.0 mn equalled to 228,112 shares and implied a market valuation of Eur. 862.5 mn (Kshs 101.7 bn); based on their last published financial statements (December 2016). The book value was Eur. 774.8 mn (Kshs 91.4 bn), implying a P/B valuation of 1.2x. For more information, see our Cytonn Weekly #23/2018
3. AfricInvest, a private equity and venture capital firm based in Tunisia with a focus on agribusiness, financial services, healthcare, education and commercial sectors, completed a transaction to buy a 14.3% stake in Britam, a diversified financial services group that is listed on the Nairobi Securities Exchange, for Kshs 5.7 bn. The transaction involved the creation of 360.8 mn new shares, which AfricInvest bought at a price of Kshs 15.9 per share. Britam will use the capital to accelerate property development, inject fresh investments into its subsidiaries, and to revamp its technology to enable it deliver its products via digital channels like mobile phones, with an eye on Micro-insurance. The acquisition was carried out at a P/B multiple of 1.4x which is a discount from the average insurance sector transaction P/B multiple of 2.1x over the last seven years, hence a relatively cheaper transaction valuation. For more information, see our Cytonn Weekly #21/2018. Following the same, Swiss Re, a reinsurance company based in Zurich Switzerland, also acquired a 13.8% stake in Britam for Kshs 4.8 bn. The transaction involved the acquisition of 348.5 mn shares of Plum LLP at a price of Kshs 13.8 per share. The acquisition was carried out at a P/B multiple of 1.3x, again, a 38.0% discount from the average insurance sector transaction P/B multiple of 2.1x over the last seven years, hence a relatively cheaper transaction valuation. For more information, see our Cytonn Weekly #24/2018.
4. Centum Investments, an investment company based in Kenya, injected Kshs 1.1 bn into its banking subsidiary Sidian Bank, through a rights issue meant to fund the lender’s growth initiatives and to drive its strategic goal of becoming a Tier 2 bank by 2022. With a 72.9% stake in Sidian Bank, the additional sum meant that Centum had defended its entire stake in the rights issue. The additional capital will support the bank’s growth plans, including further investments in its trade finance business, which saw a growth in portfolio from Kshs 896.0 mn in 2016 to Kshs 6.6 bn by close of 2017. For more information, see our Cytonn Q1' 2018 Markets Review.
5. Sanlam Kenya, a financial services company listed on the Nairobi Securities Exchange, which

mainly deals in insurance, investments and retirements schemes, invested an additional Kshs 121.7 mn in equity in Sanlam General, formally Gateway Insurance. Sanlam Kenya, then Pan Africa Insurance Holdings Limited (Pan Africa), first acquired 31,948,950 ordinary shares of Gateway Insurance, a 51.0% stake, in March 2015 for Kshs 561.0 mn. It also subscribed to additional shares in Gateway amounting to Kshs 139.7 mn to increase its shareholding to 56.5% in the same year. After the transaction, it renamed Gateway Insurance to Sanlam General. The first and second transaction valued the company at Kshs 1.1 bn and Kshs 1.2 bn, respectively. The acquisitions were carried out at a P/B multiple of 1.1x compared to the market average of 2.1x . The acquisition was a strategic move for the company to re-enter the general insurance market and to enable them to offer their clients with more comprehensive solutions such as personal and institutional insurance products. For more information, see our Cytonn Weekly #19/2018,

6. Digital Financial Services (DFS) Lab, a Fintech accelerator supported by The Bill and Melinda Gates Foundation, announced an investment of USD 200,000 (Kshs 20.0 mn) in four African start-ups, two of which are Kenyan: (i) Cherehani Africa, which relies on mobile-based tech to provide credit and distribute personalized financial literacy content to women and adolescent girls who own micro-enterprises, and (ii) another unnamed start-up that focuses on digital lending. DFS Lab identifies promising entrepreneurs and invests in for-profit companies that focus on consumers in Sub-Saharan Africa and Asia. Products from the four companies have been found to simplify processes for accessing financial information and cash via mobile phone. Cherehani Africa provides access to finances to women and adolescent girls with basic level education, aged 17-45 years. For more information, see our Cytonn Weekly #17/2018,
7. Fonds Européen de Financement Solidaire (Fefisol), a Luxembourg-based private equity (PE) firm, invested Kshs 100.0 mn in Kenya's Musoni Microfinance Limited for an undisclosed stake. The investment by Fefisol will be used to grow their loan book, which stood at Kshs 1.2 bn as at January 2018. The funds will support Musoni's objective of achieving competitive low-cost lending in the country at a time where bank funding continues to be relatively expensive. For more information, see our Cytonn Weekly #7/2018,
8. Kuramo Capital, a New-York based private equity firm completed a transaction to acquire a minority stake in Kenyan investment bank Sterling Capital for an undisclosed amount. The acquisition came after the reinstatement of Sterling's investment banking license in October 2017, after it was downgraded to stockbroker level in 2011, for failing to meet CMA's revised minimum capital limit that required investment banks to raise their minimum capital to Kshs 250.0 mn from Kshs 30.0 mn, while stockbrokers were required to increase their capital to Kshs 50.0 mn, up from Kshs 5.0 mn. For more information, see our Cytonn Weekly #4/2018,
9. Atlas Mara Limited, a financial services holding company, increased its strategic stake in Union Bank Nigeria (UBN) through a Naira 26.3 bn (USD 75.0 mn) investment in UBN's rights issue. UBN completed a Naira 49.7 bn (USD 138.2 mn) rights offering on the Nigerian Stock Exchange at a price of Naira 4.1 per share and registered a 120.0% subscription rate. Atlas Mara's investment of USD 75.0 mn translated to around 6.6 bn shares. Atlas Mara previously owned 44.5% of UBN's issued share capital at the time, translating to 7.6 bn shares. With the acquisition, Atlas obtained a total shareholding of 14.1 bn shares from the 29.1 bn shares issued, translating to a 48.6% ownership in UBN. The transaction was valued at a P/B of 0.3x, an 84.2% discount to the average P/B multiple of 1.9x for select listed Banks in Nigeria. For more information, see our Cytonn Weekly #3/2018,

The insurance sector recorded significant activity during H1'2018, the same being witnessed in recent years. This is indicated in the table below that highlights the transaction multiples in Kenya's insurance sector over the last seven years;

Insurance Sector Transaction Multiples over the Last Seven Years

No.	Acquirer	Insurance Acquired	Book Value (bn Kshs)	Transaction Stake	Transaction Value (bn Kshs)	P/B	Date
1.	Africa Development Corporation	Resolution Health East Africa	N/A	25.1%	0.2	**N/A**	Dec-10
2.	Leapfrog Investments	Apollo Investments	0.3	26.9%	1.1	**15.6x**	Dec-11
3.	Saham Finances	Mercantile Insurance	0.5	66.0%	Undisclosed	**N/A**	Jan-13
4.	Swedfund	AAR	0.4	20.0%	0.4	**5.4x**	May-13
5.	BAAM	Continental Re Kenya	0.7	30.0%	0.3	**1.4x**	Apr-14
6.	Union Insurance of Mauritius	Phoenix of East Africa	1.8	66.0%	2.0	**1.6x**	May-14
7.	UK Prudential	Shield Assurance	0.1	100.0%	1.5	**10.2x**	Sep-14
8.	Swiss Re	Apollo Investments	0.6	26.9%	Undisclosed	**N/A**	Oct-14
9.	Britam	Real Insurance Company	0.7	99.0%	1.4	**2.1x**	Nov-14
10.	Leapfrog Investments	Resolution Insurance	0.2	61.2%	1.6	**11.7x**	Nov-14
11.	Old Mutual Plc	UAP Holdings	9.6	60.7%	11.1	**1.9x***	Jan-15
12.	MMI Holdings	Cannon Assurance	1.7	75.0%	2.4	**1.9x**	Jan-15
13.	Pan Africa Insurance Holdings	Gateway Insurance Company Ltd	1.0	51.0%	0.6	**1.1x**	Mar-15
14.	Barclays Africa	First Assurance	2.0	63.3%	2.9	**2.2x**	Jun-15
15.	IFC	Britam	22.5	10.4%	3.6	**1.5x**	Mar-17
16.	AfricInvest III	Britam	28.5	14.3%	5.7	**1.4x**	Sep-17
17.	Swiss Re Asset Management	Britam	22.6	13.8%	4.8	1.3x	Jun-18
18	Old Mutual Plc	UAP Holdings	19.0	7.30%	2.7	1.8x**	Jun-18
	Harmonic Mean			**29.9%**		**2.1x**	
	Median			**55.9%**		**1.9x**	

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***-Proforma transaction multiple after goodwill impairment write-off**
****-Excluded in the harmonic mean and median**

We expect that Investors will continue to show interest in the financial services sector, motivated by attractive valuations, growth of financial inclusion and regulation that requires institutions to increase their capital requirements across the sector.

Fintech Sector

1. Cellulant, a leading Pan-African digital payments service provider that prompts, collects, settles and reconciles payments in real time, raised Kshs 4.8 bn (USD 47.5 mn) in Series C funding from a consortium of investors led by: Texas Pacific Group (TPG), through The Rise Fund, the impact fund run by the private equity group, Endeavour Catalyst, and Satya Capital, the private equity firm owned by Sudanese-British billionaire Mo Ibrahim. The USD 47.5 million represented the largest deal of its kind dedicated solely to Africa's FinTech and payments space. However, the stake acquired was not disclosed. Cellulant offers digital payments platforms and mobile banking services aimed at those who do not have a bank account. For more information, see our Cytonn Weekly #20/2018.
2. Technology investment fund Orange Digital Ventures, the strategic Corporate Venture Fund of the Orange Group invested Kshs 260.0 mn (USD 2.6 mn) in Kenya's mobile tech company Africa's Talking alongside California-based venture capital firm Social Capital. Founded in 2010, Nairobi based Africa's Talking provides a platform for businesses and developers who want to integrate mobile communication and payment services to their applications. The new funding brought the total investment received by Africa's Talking to Kshs 860.0 mn (USD 8.6 mn), in addition to Kshs 600 mn (USD 6.0 mn) by International Finance Corporation (IFC) announced in 25th April 2018. The new capital injection is set to accelerate expansion strategies and scale up its operations on the continent. Beyond Kenya, the company has started working in Uganda, Rwanda, Tanzania, Malawi, Nigeria and Ethiopia. For more information, see our Cytonn Weekly #17/2018.
3. Branch International, a mobile-based Microfinance Institution (MFI) operating in Kenya, Tanzania, Nigeria and California, raised USD 70.0 mn in Series B funding, which combined USD 50.0 mn in debt and USD 20.0 mn in equity of an undisclosed stake. The funds will enable the mobile loan app company to expand its services beyond credit access, to savings and payments, and to start operations in India. The funding was led by California-based Trinity Ventures, a venture capital firm specializing in growth capital investments. The Series B investment brings Branch's total funding to above USD 80.0 mn in the three-years since it was founded. Similar investments in the past include debt financing led by Nabo Capital in 2017 of Kshs 200.0 mn (USD 2.0 mn), a Series A equity funding round for Branch International, the company's first significant round of venture capital financing, of USD 9.6 mn led by Andreessen Horowitz, US-based venture capital firm in 2016, which was used for expansion into Nigeria, and an undisclosed seed capital from US-based Formation 8 and Khosla Ventures. For more information, see our Cytonn Weekly #15/2018.
4. France-based Proparco, the private sector financing arm of the French Development Agency (Agence Française de Dévelopement), announced an equity investment of USD 3.0 mn in JUMO, an emerging market technology start-up that offers access to credit through their mobile application. JUMO currently operates in Africa (Tanzania, Kenya, Uganda, Zambia and Ghana) and had recently launched its first activities in Asia (Pakistan). In 2017 alone, the start-up handled 12.2 mn loan transactions to customers. For more information, see our Cytonn Weekly #14/2018.

Fintech lending and Microfinance institutions in general have been a major attraction for investors in

Kenya and Sub-Saharan Africa. Lack of access to finance is a major issue for entrepreneurs and MSMEs across Africa. According to the IMF, there are 44.2 mn MSMEs in Sub-Saharan Africa with a potential demand for USD 404.0 bn in financing. The current volume of financing in Sub-Saharan Africa is estimated at USD 70.0 bn signifying a huge financing gap of USD 331.0 bn. Microfinance institutions aim to bridge this gap by offering convenient access to credit.

Hospitality Sector

1. South-African based private equity fund Uqalo invested Kshs 404.0 mn (USD 4.0 mn) to acquire an undisclosed stake in Kenyan fast food chain Big Square. The investment is beneficial for both parties as it will (i) finance Big Squares expansion plan, as the outlet targets to expand Big Squares footprint from the current 9 branches to 30 branches over the next four-years, and (ii) expand Uqalo's footprint and portfolio in Kenya. Uqalo has previously invested in Kenya's Twiga Foods, where it owns a 5.0% stake in the business-to-business food supplier. For more information, see our Cytonn Weekly #10/2018.

The interest by investors in the hospitality sector in the country indicates a positive outlook in the performance of the sector, which is supported by (i) the growing middle class with increasing disposable income, and (ii) the continued growth of the sector in the country in the past years. The food and services sector produced a total of Kshs 16.2 bn in Gross Income in 2016, a 4.5% increase from Kshs 15.5 bn recorded in 2015.

Education Sector

1. In its first investment in the education sector in Africa, One Thousand & One Voices (1K1V), a private family capital fund backed exclusively by families from around the globe, invested an undisclosed amount in Higher Ed Partners South Africa (HEPSA), a South African online education company. Based in Johannesburg, HEPSA is an integrated provider of online program management services to the leading tertiary educational institutions in South Africa. The Company assists universities in converting their on-campus degree programs into an online format, recruits qualified students for those programs, and supports enrolled students through graduation. For more information, see our Cytonn Weekly #20/2018,
2. Dubai Investments, a private equity company listed on the Dubai Financial Market stock exchange, is set to invest USD 20 mn (Kshs 2.0 bn) in the consortium set to build a chain of Sabis-branded private schools in Africa. The consortium was previously made up of Centum Investment Company, Investbridge Capital, and Sabis Education Network. Prior to the investment, 40.0% of the consortium was owned by Centum, 40% by Investbridge and 20.0% by Sabis. The value of the investment by each party and the new shareholding after the investment by Dubai Investments is undisclosed. The consortium, which is investing through the holding company Africa Crest Education (ACE). For more information, see our Cytonn Weekly #7/2018, and
3. Schole Limited, a London based education provider acquired 100% stake of Makini Schools for an undisclosed amount. Schole operates 3 institutions across Africa, (i) Crested Crane Academy, Zambia, (ii) Pestallozi Education Centre in Zambia, and (iii) Kisun High School in Uganda.

Other investors who are setting up institutions in Kenya include:

?. Johannesburg Stock Exchange listed firm, Advtech, who is set to open a school in Tatu City under its Crawford Schools brand, offering the THRASS (Teaching, Handwriting, Reading, and Spelling Skills) education system, which focuses on pre-primary education,

i. South Africa based Nova Pioneer, who have set up a Primary and Secondary School in Tatu City offering the 8-4-4 curriculum,

ii. Cytonn Investments, through its education affiliate Cytonn Education Services (CES), who are looking to provide education for all levels, from the Early Childhood Development Education (ECDE) to Tertiary Education, beginning with a Technical College branded, Cytonn College of

Innovation and Entrepreneurship, and,

iii. Investment firm Centum Ltd who plan to build a Kshs 2.0 billion school in Runda Estate in partnership with Sabis Education Network.

The acquisitions indicate the increased interest in investment in the education sector in Sub-Saharan Africa, as investors are motivated by (i) increasing demand for quality and affordable education, with the Gross Enrolment Ratio (GER) having doubled in the last 10-years to 8.5% in 2016 from 4.5% in 2006 according to a report, "The Business of Education in Africa" by Caerus Capital, and (ii) support, such as ease of approvals, offered to investors in the education sector by governments looking to meet Sustainable Development Goals (SDGs) targets of universal access to tertiary education.

Real Estate Sector

1. South African-based Vantage Capital, Africa's largest mezzanine fund manager with funds in excess of Kshs 50.0 bn invested in projects across Africa, acquired an undisclosed stake in the Rosslyn Riviera Shopping Mall for USD 8.0 mn (Kshs 800.0 mn). The Kshs 2.9 bn mall located along Limuru Road sits on a 4.5-acre piece of land and measures approximately 116,000 SQFT. For more information, see our Cytonn Weekly #17/2018
2. UK headquartered construction and management consultant, Turner and Townsend, acquired a 79.5% majority stake in Kenyan based Mentor Management Limited, MML, a project management company from private Equity firm Actis for an undisclosed amount. The management team of MML retained the minority stake. For more information, see our Cytonn Weekly #6/2018

We expect that Investors will continue to show interest in Kenya's real estate and construction industry, which is on the rise driven by (i) a high urbanization rate of 4.4% against the global average of 2.1%, leading to a rise in demand for housing, (ii) an expanding middle class with increased disposable income, with the country's disposable income having increased to Kshs 7.4 tn in 2016 from Kshs 6.5 tn in 2015 as per Kenya National Bureau of Statistic's Economic Survey 2017, (iii) Kenya's housing deficit of approximately 2.0 mn units with an increasing annual shortfall of 200,000 units, and (iv) a better operating environment for developers, characterised by tax relief of 15.0% for developers developing more than 100 affordable housing units per annum.

Exits

1. Centum Investments Limited completed a sale of its 25.0% stake in Platcorp Holdings Limited, the holding company of Platinum Credit, to Suzerain Investment Holdings Limited, for an undisclosed amount. Centum invested in Platinum Credit in December 2012 with purchase of a 36.0% stake for approximately Kshs 0.8 bn, effectively valuing the microfinance institution at Kshs 2.2 bn at the time of purchase. This stake was thereafter diluted to 33.0% following the entry of a new undisclosed investor. Earlier this year, Centum sold off 8.0% through a partial exit, bringing its shareholding to 25.0%, with the 8.0% being sold for Kshs 432.0 mn, effectively valuing Platinum Credit at Kshs 5.4 bn, a 145.0% increase in value from 2012. Centum announced the sale of the remaining 25.0% for an undisclosed amount. Going by the value of Platinum Credit as at Centum's partial exit, the divestment from Platinum is set to earn Centum about Kshs 1.3 bn. For more information, see our Cytonn Weekly #12/2018, and,
2. In another transaction, Centum reached a deal to sell off a controlling 73.4% stake in fund manager GenAfrica (formerly Genesis Kenya Investment Management Limited) to New York-based equity fund Kuramo Capital LLC. GenAfrica manages assets of about Kshs 157.0 bn as at March 2017. The deal is subject to regulatory approval. According to Centum's 2017 Annual Report, their stake in GenAfrica is valued at Kshs 1.4 bn. With GenAfrica's earnings of Kshs 141.0 mn for the year ended March 2017, the transaction could have been carried out at a P/E multiple of 9.95x. Similar transactions that have been carried out in the past include the acquisition 100.0% of ApexAfrica Capital by Axis a Mauritian private equity fund in 2015 for Kshs 470.0 mn, translating to a transaction multiple of 40.2x on a P/E basis. For more information, see our Cytonn Weekly

#12/2018.

According to the 2018 survey by Ernst & Young (EY) and Africa Venture Capitalist Association (AVCA), the number of annual PE exits in Africa have steadily increased from 30 in 2011 to peak at 50 in 2016. Despite challenging exit environments in key African markets in 2017 (with elevated political uncertainty and a weak economic environment in South Africa, the repeated Kenyan elections and continuing Nigerian currency challenges), PE activity remained resilient recording 49 exits, only slightly below the peak in 2016 (50 exits). Regionally, PE exit activity in North Africa increased in the last two years, while South Africa remained the market with the most PE exits. From 2016-2017, besides South Africa (45%) and Nigeria (6%), PE exit activity was high in the three large North African economies; Egypt (8%), Morocco (6%) and Tunisia (6%).

Exits to PE and other financial buyers continued to increase in 2017 (37%) compared to 34 % in 2016 and now represent the most common exit route. This is likely to be due to the large amount of capital raised by PE firms in 2014-2016 and PE firms needing to invest the capital raised. Looking forward, we expect to see investment in the Fintech, Education, Consumer Products and services and Energy sector.

Outlook

During the week, Safaricom staff pension fund announced its intention to explore investment opportunities in private equity (PE) firms in an effort to get higher returns for its estimated 5,000 members. Safaricom's pension scheme disclosed during an annual general meeting that assets rose by 25.9% to Kshs 10.7 bn in 2017, from Kshs 8.5 bn in 2016. This is in line with the current trend that has seen an increase in the number of pension funds investing in PE firms. According to EAVCA, the number of pensions in Kenya which have invested in PE firms has grown to 13 in 2018 from 2 in 2015.

Data released by the Retirement Benefits Authority (RBA) indicates that retirement schemes' investment in Private Equity (PE) and venture capital have grown rapidly as indicated in the table below;

Pension Schemes' Investment in Private Equity

	Dec-16	**Jun-17**	**Dec-17**
Kshs Bn.	0.22	0.25	1.00
% of Portfolio	0.02%	0.03%	0.09%

Despite this performance, PE funds still control a paltry 0.09%, of the Kshs 1.1 tn pension industry against an accepted investment limit of up to 10.0%. This can be attributed largely to; (i) little awareness among pension schemes trustees, and (ii) risk averseness among the pension scheme trustees that have knowledge of the sector. In an effort to diversify their investment portfolios in order mitigate risk and increase returns, we expect pensions to show stronger interest in private equity, which is not correlated with other traditional investments.

Private equity investments in Africa remains robust as evidenced by the increasing investor interest, which is attributed to; (i) rapid urbanization, a resilient and adapting middle class and increased consumerism, (ii) the attractive valuations in Sub Saharan Africa's private markets compared to its public markets, (iii) the attractive valuations in Sub Saharan Africa's markets compared to global markets, and (iv) better economic projections in Sub Sahara Africa compared to global markets. We remain bullish on PE as an asset class in Sub-Sahara Africa. Going forward, the increasing investor interest and stable macro-economic environment will continue to boost deal flow into African markets.