Sub-Saharan Africa (SSA) Eurobonds, & Cytonn Weekly #03/2019

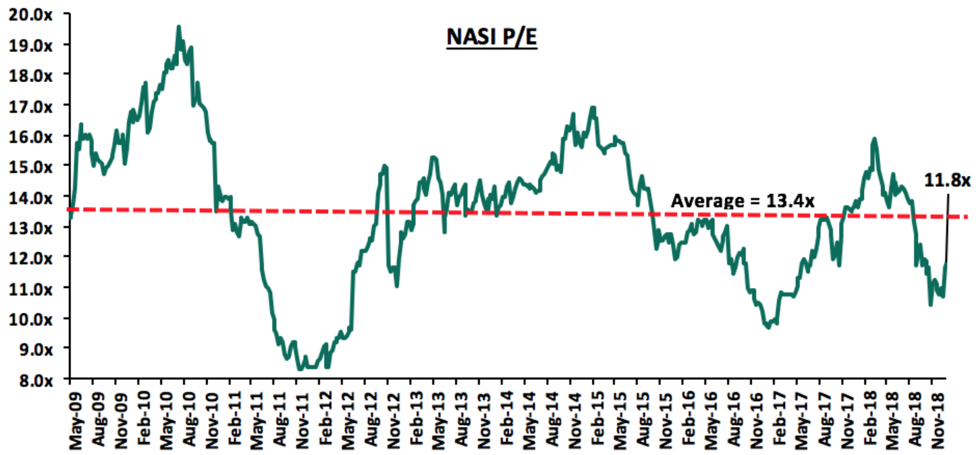
Equities

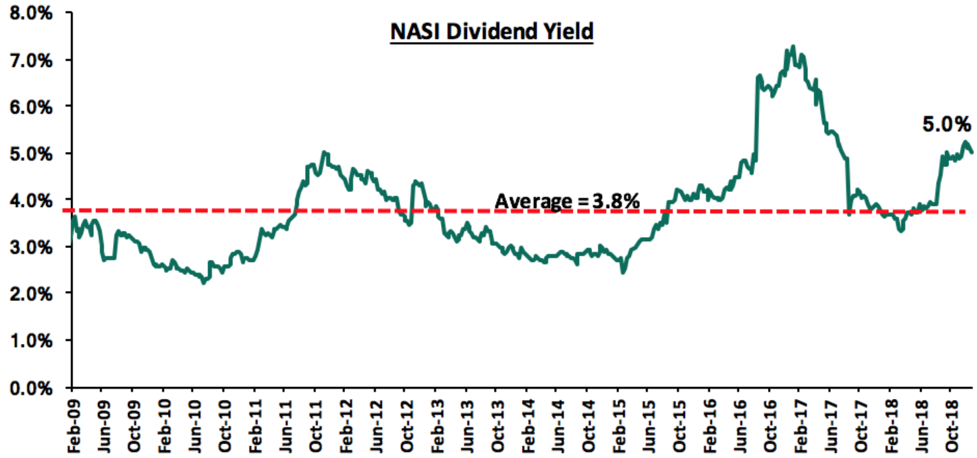
Market Performance

During the week, the equities market was on an upward trend with NASI, NSE 20 and NSE 25 gaining by 1.9%, 2.1% and 2.7%, respectively, taking their YTD performance to 3.4%, 0.6% and 4.0%, for NASI, NSE 20 and NSE 25, respectively. The gain in NASI was mainly driven by gains in the banking sector stocks such as NIC Group, Equity Group Holdings, KCB Group and Barclays Bank of Kenya, which gained by 7.6%, 6.4%, 5.1% and 5.0%, respectively.

Equities turnover gained by 58.7% during the week to USD 34.7 mn, from USD 21.9 mn the previous week, taking the YTD turnover to USD 63.9 mn. Foreign investors remained net sellers for the week, with a net selling position of USD 2.2 mn, which is a 12.1% increase from last week's net selling position of USD 1.9 mn.

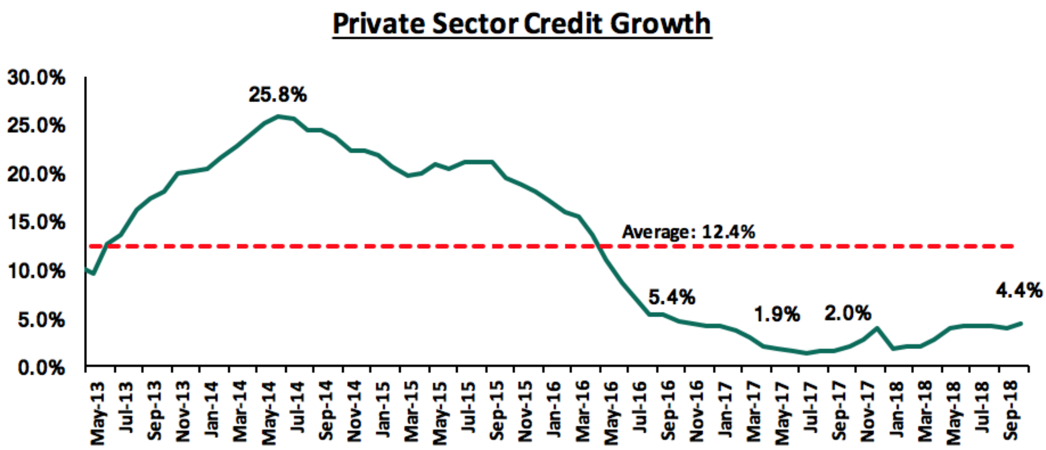
The market is currently trading at a price to earnings ratio (P/E) of 11.8x, 11.9% below the historical average of 13.4x, and a dividend yield of 5.0%, above the historical average of 3.8%. With the market trading at valuations below the historical average, we believe there is value in the market. The current P/E valuation of 11.8x is 21.6% above the most recent trough valuation of 9.7x experienced in the first week of February 2017, and 42.2% above the previous trough valuation of 8.3x experienced in December 2011. The charts below indicate the historical P/E and dividend yields of the market.





Weekly Highlights

A proposal has been made by Mr. Moses Kuria, who is the Member of Parliament for Gatundu South, to amend the Banking (Amendment) Act 2015, to allow credit consumers negotiate for interest rates on loans, depending on their risk profile, with an upper limit of up to 6.0% above the existing interest rate cap levels, currently at 13.0%. This proposal, if passed, will see borrowers be able to access credit at rates of a maximum of 19.0% per annum. The move comes in a bid to try and improve credit extension to the private sector, comprised largely of the Micro, Small and Medium Enterprises (MSMEs). Credit extension to the private sector has remained below 5.0%, and below the 5-year average of 12.4%, as can be seen in the graph below:



The proposal aims to provide the room for banks to price risk within the new margins, with banks citing the inability to price risk within the 4.0% margin above the Central Bank Rate (CBR), as a key impediment to lending, owing to the lower risk adjusted returns when compared to investments in government securities. As such banks had continually increased allocations to government securities, shunning lending to MSMEs in the process. With the rate cap having failed to achieve its intended objective of improving credit access, we are of the view that the amendment presents an opportunity for risk-based lending to kick off, as cost of credit becomes pegged to the associated risks. If successfully tabled and passed in Parliament, it would go a long way towards significantly improving credit access, as banks begin to lossen the tighter credit standards adopted after the enactment of the Banking (Amendment) Act 2015, as they will likely have enough headroom to price risk.

Barclays Bank of Kenya’s (BBK) mobile app dubbed “Timiza” has seen its loan applications rise to 10,000 applications per day, from 5,000 per day, which the bank was processing before the launch of Timiza in March 2018. The mobile application with 3.0 mn subscribers has seen the bank venture into a target market that doesn’t have the requisite documentation and is in need of faster processing of loans. Commercial banks have increasingly been focusing on the adoption and promotion of mobile applications in a bid to leverage on the alternative channel, to boost lending activities with the high number of low-value loans, and consequently increase transactional income. Examples of applications by banks include Commercial Bank of Africa’s Mshwari and Loop, Equity Group’s Equity EazzyApp, Equity EazzyBiz and Equitel, KCB’s KCB Mpesa, Co-operative Bank’s MCo-op cash, and HF Group’s HF Whizz. We maintain our view that continued focus, and increased adoption of these alternative channels will continue to see banks increase their Non-Funded Income (NFI), which contributed 34.5% of total operating income as at Q3’2018, an increase from the 33.3% in Q3’2017 for listed banks, while at the same time aiding banks in improving their operational efficiency, with the Cost to Income Ratio (CIR) of listed banks declining to 56.3% as at Q3’2018 from 59.4% in Q3’2017, owing to the relatively lower cost demands of these channels compared to the brick and mortar model of operation. Revenue expansion and cost containment will aid banks in achieving sustainable growth going forward.

The Board of Directors of Nairobi Securities Exchange (NSE) listed oil marketer Kenol Kobil has endorsed the proposed takeover by France-based Rubis Energie. Following this approval, Kenol Kobil shareholders have been granted until 18th February 2019 to accept the buyout offer of Kshs 23.0 per share. Rubis, already with a 25.0% stake in Kenol Kobil seeks to expand its presence in East and Central Africa, and is effectively valuing the company at Kshs 35.7 bn if the transaction is successful. Since the announcement on 23rd October 2018, the share has gained by 39.2% to Kshs 21.3 per share as at 18th January 2018, from Kshs 15.3 per share. The offer by Rubis was at a premium, being 50.3% above the prevailing Kshs 15.3 price per share. The buyout is set to take place, with the only impediment being the refusal of the offer by any shareholders, or possibly the filing of an injunction in court by a shareholder to stop the process.

Universe of Coverage

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Banks	Price as at 11/1/2019	Price as at 18/1/2019	w/w change	YTD Change	Target Price*	Dividend Yield	Upside/Downside**	P/TBv Multiple
Diamond Trust Bank	152.0	150.0	(1.3%)	(4.2%)	283.7	1.7%	90.9%	**0.9x**
Ghana Commercial Bank***	4.6	4.5	(2.0%)	(2.2%)	7.7	8.4%	80.0%	**1.1x**
Access Bank	5.7	5.6	(0.9%)	(17.6%)	9.5	7.1%	76.8%	**0.4x**
NIC Bank	27.6	29.7	7.6%	6.7%	48.8	3.4%	68.0%	**0.8x**
Zenith Bank***	21.9	21.5	(1.6%)	(6.7%)	33.3	12.6%	67.5%	**1.0x**

Universe of Coverage

Banks	Price as at 11/1/2019	Price as at 18/1/2019	w/w change	YTD Change	Target Price*	Dividend Yield	Upside/Downside**	P/TBv Multiple
KCB Group	36.9	38.8	5.1%	3.6%	61.3	7.7%	65.7%	**1.2x**
UBA Bank	7.4	7.3	(0.7%)	(5.2%)	10.7	11.6%	58.2%	**0.5x**
I&M Holdings	91.0	94.3	3.6%	10.9%	138.6	3.7%	50.8%	**1.0x**
Co-operative Bank	13.9	14.0	0.7%	(2.4%)	19.9	5.7%	48.4%	**1.2x**
CRDB	140.0	140.0	0.0%	(6.7%)	207.7	0.0%	48.4%	**0.5x**
Equity Group	37.0	39.3	6.4%	12.8%	56.2	5.1%	48.1%	**1.9x**
Ecobank	7.5	7.5	(0.4%)	(0.4%)	10.7	0.0%	43.6%	**1.6x**
CAL Bank	1.0	1.0	(1.0%)	1.0%	1.4	0.0%	41.4%	**0.8x**
Stanbic Bank Uganda	30.0	30.0	0.0%	(3.2%)	36.3	3.9%	24.8%	**2.1x**
Guaranty Trust Bank	33.5	32.0	(4.6%)	(7.3%)	37.1	7.5%	23.6%	**2.0x**
Union Bank Plc	6.0	6.8	12.5%	20.5%	8.2	0.0%	20.7%	**0.7x**
HF Group	5.4	5.8	7.4%	4.7%	6.6	6.0%	19.8%	**0.2x**
Barclays	11.1	11.7	5.0%	6.4%	12.5	8.6%	15.9%	**1.6x**
SBM Holdings	6.0	6.1	1.3%	2.3%	6.6	4.9%	12.5%	**0.9x**
Bank of Kigali	290.0	290.0	0.0%	(3.3%)	299.9	4.8%	8.2%	**1.6x**
Standard Chartered	194.5	195.8	0.6%	0.6%	196.3	6.4%	6.7%	**1.6x**
Stanbic Holdings	90.0	95.0	5.6%	4.7%	92.6	2.4%	(0.2%)	**0.9x**
Bank of Baroda	135.0	135.0	0.0%	(3.6%)	130.6	1.9%	(1.4%)	**1.2x**
FBN Holdings	7.4	7.3	(1.4%)	(8.2%)	6.6	3.4%	(5.8%)	**0.4x**
Standard Chartered	21.4	21.1	(1.7%)	0.4%	19.5	0.0%	(7.7%)	**2.6x**
National Bank	5.2	5.5	5.8%	2.6%	4.9	0.0%	(10.3%)	**0.4x**
Stanbic IBTC Holdings	47.0	46.2	(1.8%)	(3.8%)	37.0	1.3%	(18.5%)	**2.4x**
Ecobank Transnational	14.0	13.5	(3.6%)	(20.6%)	9.3	0.0%	(31.3%)	**0.5x**

***Target Price as per Cytonn Analyst estimates**
****Upside / (Downside) is adjusted for Dividend Yield**
*****Banks in which Cytonn and/or its affiliates are invested in**
******Stock prices indicated in respective country currencies**

We are "Positive" on equities for investors as the sustained price declines has seen the market P/E decline to below its historical average. We expect increased market activity, and possibly increased inflows from foreign investors, as they take advantage of the attractive valuations, to support the positive performance.