

Market Post Interest Rate Cap & Cytonn Weekly #50/2019

Equities

Market Performance

During the week, the equities market recorded mixed performance with NASI gaining by 0.1% and NSE 20 and NSE 25 recording losses of 1.3% and 0.6%, respectively, taking their YTD performance to gains/(losses) of 14.3%, (8.7%) and 11.0%, for the NASI, NSE 20 and NSE 25, respectively. The performance in NASI was driven by gains recorded by large-cap stocks such as Standard Chartered, Barclays, KCB Group and Safaricom of 3.3%, 2.8%, 1.5%, and 0.7%, respectively.

Equities turnover increased by 19.2% during the week to USD 33.0 mn, from USD 27.7 mn the previous week, taking the YTD turnover to USD 1,444.7 mn. Foreign investors became net buyers for the week, with a net buying position of USD 4.7 mn, an improvement from a net selling position of USD 0.1 mn recorded the previous week.

The market is currently trading at a price to earnings ratio (P/E) of 12.3x, 7.4% below the historical average of 13.3x, and a dividend yield of 5.8%, 1.9% points above the historical average of 3.9%. With the market trading at valuations below the historical average, we believe there is value in the market. The current P/E valuation of 12.3x is 26.6% above the most recent trough valuation of 9.7x experienced in the first week of February 2017, and 48.0% 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 Highlight

The Insurance Regulatory Authority released **Q3'2019 Insurance Industry Report** summarizing the performance and financial position of the Kenya Insurance industry. According to the report:

- Industry Gross Written Premium grew by 6.5% to Kshs 174.9 bn as at the end of Q3'2019, from Kshs 164.3 bn recorded in Q3'2018. The Long-term Insurance segment recorded an 11.0% growth in Gross Written Premiums to Kshs 69.7 bn in Q3'2019, from Kshs 62.8 bn observed in a similar period last year, while the General Insurance segment's Gross Written Premiums improved by 3.7% to Kshs 105.2 bn, from Kshs 101.5 bn in Q3'2018,
- The General Insurance segment remained the largest contributor to the industry Gross Written Premium, contributing 60.2% of the Total Premium, with Motor Insurance and Medical Insurance businesses accounting for 34.5% and 32.0% of the Gross Premium Income under the General Insurance business, respectively,
- Long-term Insurance segment, on the other hand, contributed 39.8% of the Total Premium, with Pensions and Life Assurance businesses accounting for 38.5% and 29.1% of Total Long-Term Gross Insurance Premium, respectively,
- According to the quarterly claims statistics, in Q3'2019, the claims payment ratio, which is the

proportion of the number of claims paid in relation to the total number of claims actionable during the quarter, for general liability increased by 1.8% points to 10.0%, from 8.2% recorded in Q3'2018. Claims payment ratio for general non-liability claims, on the other hand, also increased by 6.7% points to 71.4%, compared to 64.7% observed in Q3'2018. The claims payment ratio for the Long-Term Insurance business recorded an 8.6% points increased to 73.5% in Q3'2019, from 64.9% observed in Q3'2018. Generally, the overall claims payment for the industry improved in Q3'2019 as compared to a similar period in 2018,

- Profit after Tax (PAT) of insurers in the quarter improved by 97.7% to Kshs 6.1 bn, from Kshs 3.1 bn, thus, the sector's Return on Assets (ROA) and Return on Equity (ROE) improved marginally to 1.7% and 4.7%, respectively, from 1.4% and 3.9%, respectively, recorded in Q3'2018,
- In terms of financial position, the industry's Total Assets grew by 10.6% to Kshs 690.9 bn, from Kshs 624.9 bn recorded in a similar period last year, with Investments recording a growth of 13.0% to Kshs 577.0 bn, from 510.4 bn recorded in Q3'2018 with Government Securities (Treasury Bills and Bonds) and Investment property accounting for the highest allocations of 61.5% and 14.5%, respectively,
- Shareholder's Funds increased by 6.1% to Kshs 158.0 bn, from Kshs 148.9 bn recorded in Q3'2018, with Total Liabilities recording a 12.0% increase to Kshs 532.8 bn, from Kshs 628.9 bn recorded in a similar period last year, driven by a 34.3% increase in Long-term Liabilities to Kshs 13.4 bn, from Kshs 10.0 bn recorded in Q3'2018, coupled with a 12.0% increase in Insurance Contract Liabilities to Kshs 360.6 bn, from Kshs 315.3 bn recorded in a similar period in 2018,
- Reinsurers, on the other hand, recorded a 31.4% increase in business volume with Gross Premium Income rising to Kshs 18.0 bn, from Kshs 13.7 bn in Q3'2018, with overall profitability declining by 56.3% to Kshs 1.2 bn, from Kshs 2.7 bn recorded in Q3'2018. The decline in profitability of reinsurers is attributable to a 36.7% rise in claims incurred to Kshs 9.1 bn, from Kshs 6.7 bn recorded in Q3'2018, which outperformed the 31.4% increase in Gross Premium Income, from Kshs 13.7 bn to Kshs 18.0 bn .

In light of various themes shaping the sector, including regulatory changes and technology and innovation, we expect to witness transition on these fronts which will drive the adoption of mobile and online underwriting platforms, enhancing convenience to customers in taking insurance policies thus raising the uptake of insurance products. These efforts, thus, will improve revenue channels for insurance firms and enhance the sustainability of profitable performance.

Universe of Coverage

| Banks | Price at 6/12/2019 | Price at 13/12/2019 | w/w change | Target Price* | Dividend Yield | Upside/Downside** | P/TBv Multiple | Recommendation |
|----------------------------|--------------------|---------------------|------------|---------------|----------------|-------------------|----------------|-------------------|
| Kenya Reinsurance | 3.03 | 3.10 | 2.3% | 4.8 | 14.5% | 72.9% | 0.3x | Buy |
| Diamond Trust Bank | 112.00 | 110.00 | (1.8%) | 189.0 | 2.4% | 71.1% | 0.5x | Buy |
| I&M Holdings*** | 51.75 | 50.00 | (3.4%) | 75.2 | 7.8% | 53.1% | 0.9x | Buy |
| Jubilee Holdings | 350.00 | 350.75 | 0.2% | 453.4 | 2.6% | 32.1% | 1.1x | Buy |
| KCB Group*** | 51.50 | 52.25 | 1.5% | 64.2 | 6.7% | 31.4% | 1.4x | Buy |
| Sanlam | 17.00 | 16.50 | (2.9%) | 21.7 | 0.0% | 27.6% | 0.7x | Buy |
| Co-op Bank*** | 15.70 | 15.55 | (1.0%) | 18.1 | 6.4% | 21.7% | 1.3x | Buy |
| Standard Chartered | 195.00 | 201.50 | 3.3% | 211.6 | 9.4% | 17.9% | 1.5x | Accumulate |
| NCBA | 33.55 | 33.80 | 0.7% | 37.0 | 4.4% | 14.7% | 0.8x | Accumulate |
| Equity Group*** | 52.25 | 51.25 | (1.9%) | 56.7 | 3.9% | 12.4% | 1.9x | Accumulate |

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| Barclays Bank*** | 12.65 | 13.00 | 2.8% | 13.0 | 8.5% | 11.2% | 1.6x | Accumulate |
| Stanbic Holdings | 105.00 | 100.00 | (4.8%) | 108.1 | 4.8% | 7.8% | 1.1x | Hold |
| Liberty Holdings | 10.45 | 10.50 | 0.5% | 10.1 | 4.8% | 1.1% | 0.9x | Lighten |
| CIC Group | 3.00 | 3.00 | 0.0% | 2.6 | 4.3% | (7.7%) | 1.1x | Sell |
| Britam | 8.16 | 8.20 | 0.5% | 6.8 | 0.0% | (17.2%) | 0.8x | Sell |
| HF Group | 5.52 | 5.54 | 0.4% | 4.2 | 0.0% | (23.9%) | 0.2x | Sell |

*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

We are “Positive” on equities for investors as the sustained price declines have 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.

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