Cytonn Monthly – April 2017

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Executive Summary:

Fixed Income and Macro Economic Review: Yields on T-bills were relatively unchanged during the month, with the 91-day paper increasing to 8.8% from 8.7% in March, while the 364-day remained unchanged at 10.9%. There was no change on the 182-day paper as it has not been on offer for the 8th week in a row, as the government aims to spread maturity concentration risk across the three papers. The Kenya National Bureau of Statistics (KNBS) released the 2017 Economic Survey, which indicated that Kenya's GDP grew by 5.8% in 2016 from 5.7% in 2015, in line with our projection of a 5.7% - 6.0% growth;

Equities: During the month of April, the equities market was on an upward trend with NASI, NSE 20 and NSE 25 gaining 2.4%, 1.4% and 1.3%, respectively, taking their YTD performance to 0.0%, (0.9%) and (0.4%), for NASI, NSE 20 and NSE 25, respectively. The Cabinet approved the State-sponsored Financial Services Authority Bill 2017, which seeks to create the Financial Services Authority, a body that will consolidate and take over the functions of the Capital Markets Authority (CMA), the Insurance Regulatory Authority (IRA), the Retirement Benefits Authority (RBA) and the SACCOs Societies Regulatory Authority (SASRA);

Private Equity: During the month of April, buyouts and fundraising activities in Africa's private equity space continued to gather pace, evidenced by the purchase of Shell's shareholding in Vivo Energy by Vitol Group and the raising of USD 116.0 mn by Frontier Investments Management in the first close of its second fund, Frontier Energy II;

Real Estate: Reduced activity witnessed in the real estate sector as the election draws near. During the month, a number of real estate reports were released covering the sector's performance in 2016, which showed a slowdown in the commercial theme, increased demand in the low to middle income residential theme, and a recovering hospitality theme in Kenya.

Company Updates

- Cytonn Real Estate has promoted Johnson Denge, to Senior Manager, Regional Markets; Johnson will be responsible for the brand extension to regional markets. Commenting on the appointment, Edwin H. Dande, Managing Partner and Chief Executive Officer, said that, "Our next phase of growth will entail regional expansion. We have been in discussion with partners in countries such as Rwanda and Uganda for over a year now, it's time to do a pilot project in one of those countries. And with our principal financier, Taaleri of Finland already the leading investor in Kigali through Kigali Heights, it makes it easier to enter the region."
- Cytonn Real Estate has promoted Martin Gitonga to Senior Manager, Projects Management, with overall responsibility for delivery of all projects. Commenting on the appointment, Senior Partner and Chief Investment Officer, Elizabeth N. Nkukuu, CFA, said that "with our increasing portfolio of projects, it makes sense to separate Project Management into its own delivery units with its own leadership. Martin will lead a team of twenty in Project Management."

Cytonn INVESTMENTS

- On Monday 10th April 2017, Cytonn Investments released the Cytonn FY'2016 Banking Sector Report that ranked KCB Group as the most attractive bank in Kenya. See Cytonn FY'2016 Banking Sector Report
- On Monday 24th April 2017, Cytonn Real Estate, the development affiliate of Cytonn Investments, released the Nairobi Commercial Office Report that analyzed the performance of the sector in 2016. The report themed "*Transition to a Buyers' Market*" looked at both the demand and the supply of the office space and finally the expected performance of the commercial office subsector in Nairobi in 2016. See Event Note and the Cytonn Commercial Office Report 2017
- Our Investments Manager, Maurice Oduor, discussed the banking sector report released by Cytonn Investments. Watch Maurice Oduor on Citizen TV here
- Our Investment Analyst, John Ndua, discussed the banking sector report by Cytonn Investments that ranked KCB Group as the most attractive bank in Kenya. Watch John Ndua on KTN here
- We continually showcase real estate developments by our real estate development affiliate, Cytonn Real Estate, through weekly site visits. The site visits target both investors looking to invest in real estate directly, and also those interested in high yielding investment products to familiarize themselves with how we support the high yield returns. If interested in attending the site visits, kindly register here
- We continue to see very strong interest in our Private Wealth Management training, which is at no cost, and is held bi-weekly, but is open only to pre-screened participants. To register for the training kindly use thislink
- For recent news about the company, see our news section here

- We have 12 investment-ready projects, offering attractive development and buyer targeted returns of around 25.0% p.a. See further details here: Summary of investment-ready projects
- We are inviting proposals from eligible candidates for services required in the structuring and issuance of Kshs 5.0 bn real estate medium term notes via a contemplated public offer to provide the following services: (i) lead transaction services, (ii) note trustee services, and (iii) tax consultancy. For more details, see our Request for Proposal (RFP) here
- To invest in any of our current or upcoming real estate projects, please visit Cytonn Real Estate
    - The Alma, which is over 56.0% sold, has delivered an annualized return of upto 55.0% p.a. for investors who bought off-plan. See The Alma
    - Amara Ridge is currently 100.0% sold and has delivered 33.0% p.a. returns to investors. See Amara Ridge
    - The Ridge Phase One is currently 20.0% sold and has delivered an average return of 29.5% for investors earlier. See The Ridge
    - Taraji Heights is currently 10.0% sold. See Taraji Heights
- Following the completion of sales for Amara Ridge, we are currently looking for land in Karen for our next development. We are also looking for 3-10 acres of land in Garden Estate, Muthaiga North, South C and Lang'ata. Contact us at rdo@cytonn.com if you have any land for sale or joint ventures in the above areas
- We continue to beef up the team with the ongoing hires: Careers at Cytonn

Fixed Income and Macro Economic Review

Liquidity in the money markets remained high as witnessed by the high treasury bills subscriptions, which remained oversubscribed, with subscriptions coming in at 131.8% from 152.6% in March. The 182-day paper was not on offer throughout the month and for the 8th week in a row, as the government aims to spread maturity concentration risk across the three papers. The subscription rates for the 91 and 364-day papers during the month came in at 125.1% and 138.6%, respectively, from 93.8% and 166.4% the previous month. Yields on T-

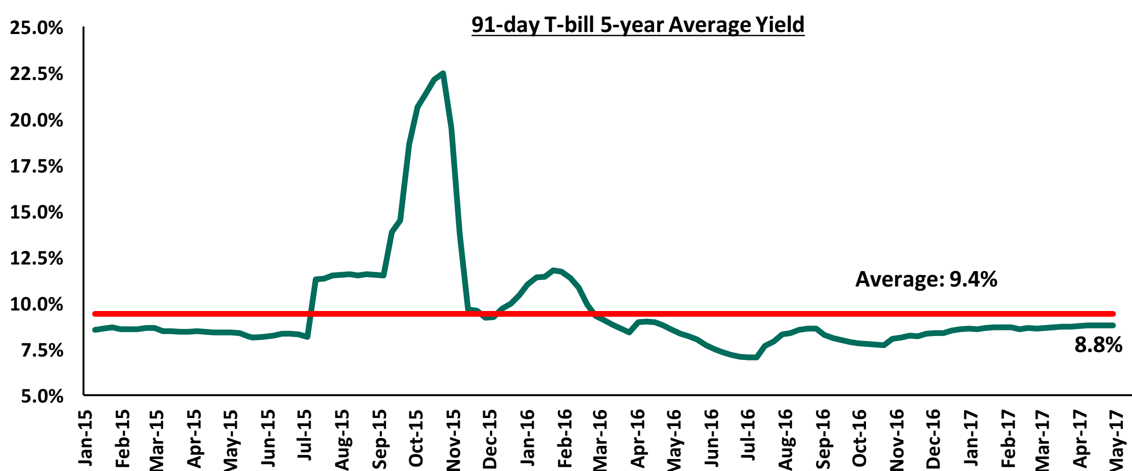
bills were relatively unchanged during the month of April, with the 91-day increasing to 8.8% from 8.7% while the 364-day remained unchanged at 10.9%. The Central Bank of Kenya (CBK) has remained disciplined in stabilizing interest rates in the auction market by rejecting bids priced above the market, with the overall bids acceptance rate in April declining marginally to 79.2%, compared to 82.1% in March.

During the last week of the month, T-bills were oversubscribed for the 13th week running, with overall subscription coming in at 103.1%, compared to 166.7% recorded the previous week, with the subscription rate on the 91 and 364-day papers decreasing to 123.7% and 82.5% from 136.7% and 196.6% the previous week, respectively. The significant decline in the 364-day paper subscription rate could be attributed to the preference of investors to bid for the government bonds, which offered better returns on a risk adjusted basis of 11.3% and 12.0% for bonds with 1.4 and 2.0 years to maturity, respectively. Yields on the 91 and 364-day T-bills remained unchanged during the week, coming in at 8.8% and 10.9%, respectively. Given the possible upward pressures on interest rates, which are currently at low levels, we maintain our recommendation for investors to be biased towards short-term fixed income instruments.

The 91-day T-bill is currently trading below its 5-year average of 9.4%. The lower yield on the 91-day paper is mainly attributed to the low interest rates environment we have been experiencing, given that CBK has remained disciplined in stabilizing interest rates in the auction market by rejecting bids priced above the market. However, as indicated previously, despite the current low interest rates environment, there exists possible upward pressure on interest rates as:

i. The government has only borrowed Kshs 205.8 bn, of the budgeted foreign borrowing, representing 44.5% of its foreign borrowing target of Kshs 462.3 bn, the balance of which it will most likely plug from the domestic market, and,
ii. Kenya Revenue Authority (KRA) has already missed its first half of 2016/17 fiscal year revenue collection target by 3.2%, and are expected to miss their overall revenue collection target of Kshs 1.5 tn for the current fiscal year.

It is important to note that while the government is behind on their borrowing target, they are also behind on their spending targets, with total expenditure for the first half of the 2016/17 fiscal year coming in at Kshs 928.5 bn, which represents 83.6% of the pro-rated target of Kshs 1.1 tn. Of this, development expenditure came in at Kshs 619.1 bn, and had an absorption rate of 73.8%, against the Kshs 309.4 bn used for recurrent expenditure, which had a 92.5% absorption rate. Given that the government has historically exceeded the absorption rate on recurrent expenditure averaging 103.5% while the development expenditure has averaged 65.0%, leaving the overall budget absorption rate below 100.0% consistently in the last 5 fiscal years, there still exists upward pressure on interest rates, but may be subdued as we approach the end of the fiscal year in the event spending does not increase.



During the month of April, the Kenyan Government re-opened two bonds, the FXD 3/2008/10 and FXD 1/2009/10, with effective time to maturity of 1.4 and 2.0-years, respectively, and a coupon of 10.8% for both, in a bid to raise Kshs 30.0 bn for budgetary support. Yields on the bonds came in at 11.3% and 12.0%, below our recommended bidding range of between 12.1% - 12.6%, and 12.6% - 13.1% for the 1.4-year and the 2.0-year, respectively. The bonds were oversubscribed, with a performance rate coming in at 164.6%, attracting Kshs 49.4 bn. Given that the market weighted average rates came in at 11.5% and 12.2%, respectively, above the accepted rate of 11.3% and 12.0%, respectively, it is clear from this auction the government did not accept expensive bids, having only accepted Kshs 32.8 bn out of the Kshs 49.4 bn worth of bids received, translating to an acceptance rate of 66.3%.

During the month, the average interbank rate closed at 6.4%, up from 4.0% at the end of March, owing to interbank market segmentation with liquidity skewed towards a few large banks, despite a net liquidity injection of Kshs 22.5 bn in the money market. The net liquidity position was a decline from a net liquidity injection of Kshs 31.2 bn in March, as a result of a decrease in government payments and T-bill redemptions, which came in at Kshs 124.7 bn and Kshs 42.5 bn, from Kshs 148.7 bn and Kshs 94.9 bn, respectively, last month. The interbank rate is often determined by the liquidity distributions within the banking sector as opposed to the net liquidity position in the interbank market.

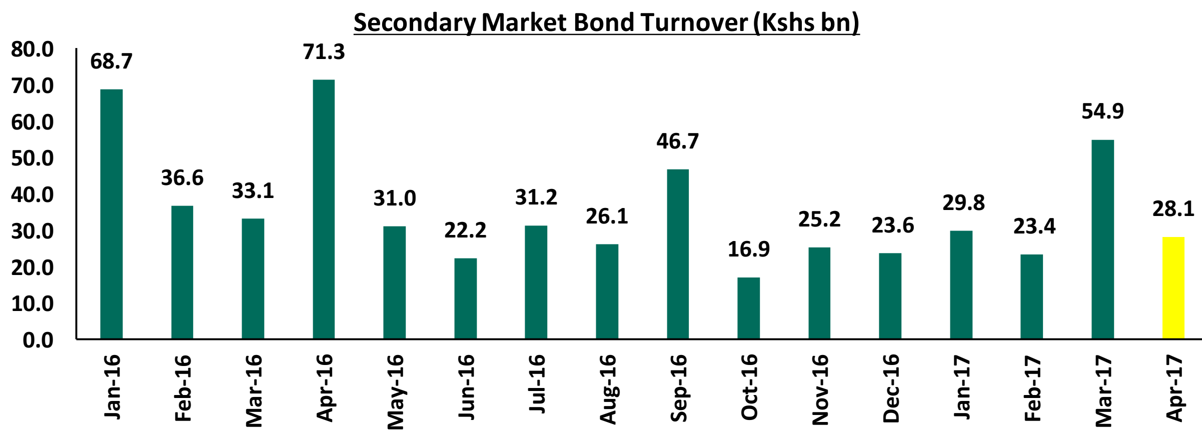
Below is a summary of the money market activity during the month:

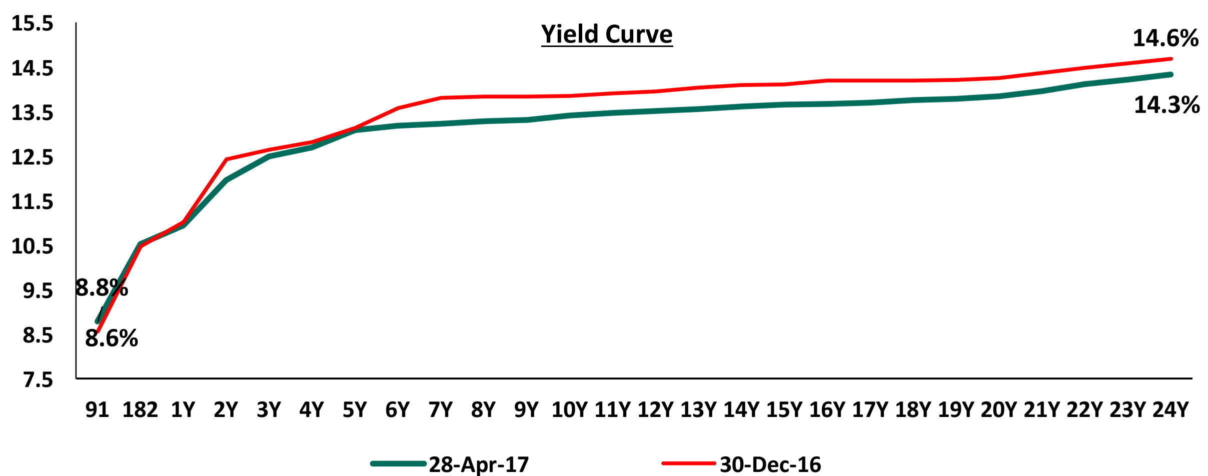
all values in Kshs bn, unless stated otherwise

April Monthly Liquidity Position – Kenya			
Liquidity Injection		**Liquidity Reduction**	
Term Auction Deposit Maturities	124.5	T-bond sales	48.2
Government Payments	124.7	Transfer from Banks - Taxes	75.6
T-bill Redemption	42.5	T-bill (Primary issues)	85.2
T-bond Interest	13.2	Term Auction Deposit	91.9
Reverse Repo Purchases	33.7	Reverse Repo Maturities	39.4
Repos Maturities	48.5	Repos	24.3
Total Liquidity Injection	**387.1**	**Total Liquidity Withdrawal**	**364.6**
		Net Liquidity Injection	**22.5**

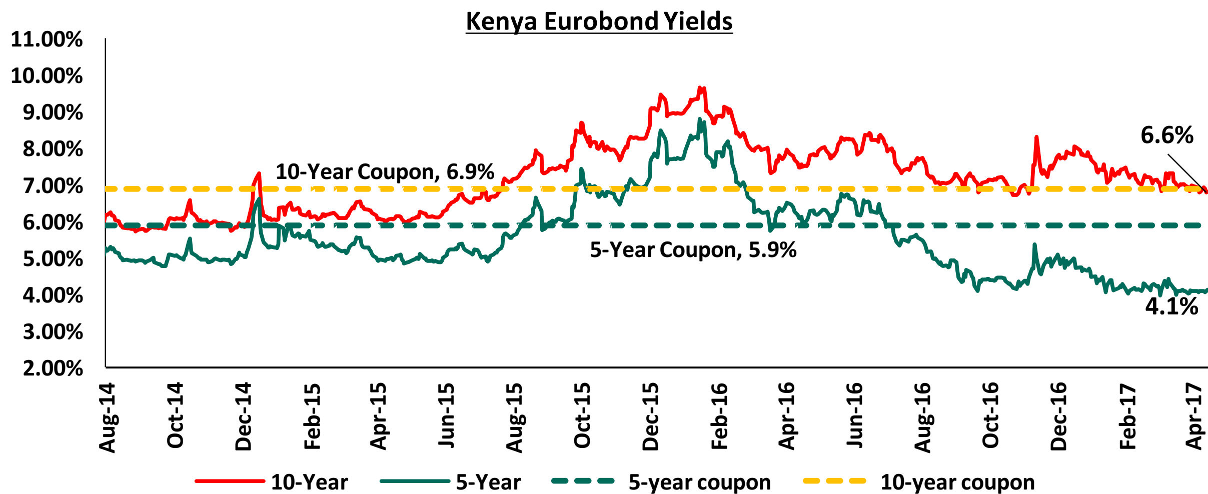
As can be seen in the graphs below, the secondary bonds market recorded reduced activity, with turnover decreasing by 48.8% to Kshs 28.1 bn in the month of April, from Kshs 54.9 bn recorded in March. The yields on government securities have remained relatively low during the month as highlighted in the yield curve below. The performance for the secondary bonds stood

at (2.7%) in April, as per the NSE FTSE Bond Index.





According to Bloomberg, the yield on the 5-year Eurobond with 2.2-years to maturity increased to 4.1%, from 4.0% in March, whereas that on the 10-year Eurobond with 7.2-years to maturity decreased to 6.6% from 6.9% the previous month. Since the mid-January 2016 peak, yields on the Kenya Eurobonds have declined by 4.7% points and 3.0% points, for the 5-year and 10-year Eurobonds, respectively, due to the stable macroeconomic conditions. The declining Eurobond yields and Standard & Poor's (S&P) having maintained Kenya's foreign and local currency sovereign credit ratings for the short and long term at "B+/B", respectively, are an indication that Kenya remains a stable and hence attractive investment destination.



The Kenya Shilling depreciated marginally against the US Dollar by 0.2% during the month to close at Kshs 103.2, from Kshs 103.0 in March. The weakening of the shilling during the month was primarily driven by dollar demand from oil and retail importers. On a year to date basis, the shilling has depreciated against the dollar by 0.7%. The forex reserve level currently stands at USD 8.3 bn (equivalent to 5.5 months import cover) from USD 7.0 bn (equivalent to 4.6 months import cover) recorded on 17th March 2017, largely as a result of the receipt of the Kshs 82.3 bn syndicated loan. Going forward, we expect the shilling to come under pressure from (i) global strengthening of the dollar due to the expected series of rate hikes by The Federal Reserve during the year, and (ii) recovery of global oil prices. However, with the current forex reserve level, we believe the CBK will be able to support any depreciation in the shilling in the short term.

The inflation rate for the month of April increased by 120 bps to 11.5%, from 10.3% in March, above our projection of 10.7% - 11.0%. The rise was driven by (i) an increase in food prices, which rose 3.6% m/m on account of the prevailing drought in the country, and (ii) an increase in housing, water, electricity, gas and other fuels, which rose by 0.6% due to increased cost of house rents, other cooking fuels and water services. Below is a table with the notable changes during the month;

Key Changes in the Consumer Price Index (CPI) during the month of April			
Broad Commodity Group	**Price change m/m**	**Price change y/y**	**Reason**
Food & Non-Alcoholic Beverages	3.6%	21.0%	Increase in the prices of vegetables, maize flour, milk, and maize grain, attributed to the prevailing drought
Restaurant and Hotels	1.1%	5.7%	Increased demand for restaurant and hotel services over the Easter Holiday
Housing, Water, Electricity, Gas and other Fuels	0.6%	2.9%	Increase in costs due to increased cost of house rents, other cooking fuels and water services

Going forward, we expect upward inflationary pressures from (i) the food component of the CPI basket due to the persistent drought that is expected to carry on for the first half of the year, with depressed rainfall expected in the long rains season that comes in between March and May, (ii) the global recovery of oil prices spurring cost-push inflation, (iii) the weakening shilling due to global strengthening of the dollar, which will lead to an increase in the cost of imports, and (iv) given this is an electioneering period, we expect an increase in money supply due to campaign money. We expect upward inflationary pressures to persist in the first half of 2017, and average above the upper bound of the government target range of 2.5% - 7.5% given that the inflationary pressure we see is more supply driven and not a monetary policy issue (where the government reduces rates to spur growth that leads to inflation) as the government has managed to maintain interest rates low and the Central Bank Rate (CBR) is still at 10.0%.

During the month, the Kenya National Bureau of Statistics (KNBS) released the 2017 Economic Survey, which indicated that Kenya's GDP growth for 2016 came in at 5.8%, up from 5.7% in 2015, in line with our projection of a 5.7% - 6.0% growth. Growth in Q4'2016 was hampered by the drought that took a toll on agriculture and electricity supply, whereas accommodation and food service registered the biggest improvement, growing at 13.3% in 2016, from a decline in growth of 1.3% in 2015, in line with our outlook of a recovering tourism sector. Agriculture experienced subdued growth of 4.0% in 2016, from 5.5% in 2015, with the slow-down attributable to unfavorable weather conditions on account of depressed rainfall in the second half of the year. Real estate registered strong growth of 8.8% in 2016, up from 7.2% in 2015, highlighting the increased confidence and growth in the sector. The table below indicates the growth of key sectors that drove GDP growth in 2016;

Kenya's GDP Contribution & Growth per Sector

Sector	Contribution FY'2015	Contribution FY'2016	FY'2015 Growth	FY'2016 Growth
Agriculture and Forestry	22.2%	**21.8%**	5.5%	4.0%
Manufacturing	10.5%	**10.3%**	3.6%	3.5%
Real estate	8.2%	**8.4%**	7.2%	8.8%
Wholesale and retail trade	7.7%	**7.5%**	5.9%	3.8%
Transport and Storage	6.8%	**6.9%**	8.0%	8.4%
Financial Intermediation	6.2%	**6.2%**	9.4%	6.9%
Construction	5.2%	**5.4%**	13.9%	9.2%
Public administration	3.9%	**3.9%**	5.5%	5.3%
Information and Communication	3.7%	**3.8%**	7.4%	9.7%

For a more comprehensive analysis on the economic growth review, see our Kenya 2016 GDP Growth and Outlook. During the month, the World Bank issued a revised outlook on Kenya's 2017 GDP growth, revising it downwards to 5.5% from 6.0% previously. The basis of their downward revision was pinned on the slowdown in private sector credit growth and the prevailing drought, which is likely to affect the agricultural sector adversely as outlined in our Cytonn Weekly #15/2017. This came at a time when the International Monetary Fund (IMF), also revised the country's GDP growth for 2017 to 5.5%, from 6.0% previously. Kenya's growth is still set to be above the Sub-Saharan Africa projected growth of 2.9%, and will be supported by government spending on infrastructure and recovery of the tourism sector.

During the month, the National Treasury ordered the tax and duty-related provisions of the Finance Bill 2017 to be put into effect even before the Bill passes into Law. The order will see excise stamp fees paid on cigarettes and alcoholic beverages with more than 10.0% alcohol content increase to Kshs 2.8 per retail unit, from Kshs 1.5 previously. Contrary to this, excise stamp fees on non-alcoholic beverages, mineral water and cosmetics have practically been halved, reducing to Kshs 0.6, Kshs 0.5 and Kshs 0.6 per retail unit, respectively. Keeping in mind that non-alcoholic beverages are consumed by a larger population and at a higher frequency than alcoholic beverages (above 10.0% alcohol content), the net effect of these changes would be a tax cut on beverages in general. The provisions in the Finance Bill are in line with taxation measures outlined in the National Budget for the fiscal year 2017/18 as outlined in our Cytonn Weekly #15/2017 among other budget changes that will influence the 2017/2018 fiscal year. Some of the key changes as highlighted in our Q1'2017 Markets Review include;

i. Additional tax incentives for businesses in the Special Economic Zone (SEZ), including allowing a capital deduction of 100% of the cost of buildings and machinery owned by the SEZ enterprise, and exempting goods exported from and imported by an SEZ enterprise from Export Duty and Import Declaration Fees,
ii. Exemptions from VAT on transactions related to transfer of assets into Real Estate Investment Trusts and Asset Backed Securities,
iii. Increased the taxation on gains from gambling to 50% to discourage the betting culture,
iv. Exemptions from VAT on locally assembled tourist vehicles, and,
v. Zero rate importation of maize for four months.

The rates on the fixed income market have remained stable, despite indication of possible upward pressure on interest rates. The Government is ahead of its domestic borrowing for the current fiscal year, having borrowed Kshs 270.3 bn against a target of Kshs 239.0 bn (assuming a pro-rated borrowing throughout the financial year of Kshs 294.6 bn budgeted for the full financial year). The government has only borrowed Kshs 205.8 bn of the budgeted foreign borrowing, representing 44.5% of its foreign borrowing target of Kshs 462.3 bn, and the Kenya Revenue Authority (KRA) is expected to miss its overall revenue collection target of Kshs 1.5 tn for the current fiscal year having missed its first half target. It is important to note that the government is also behind its spending target,

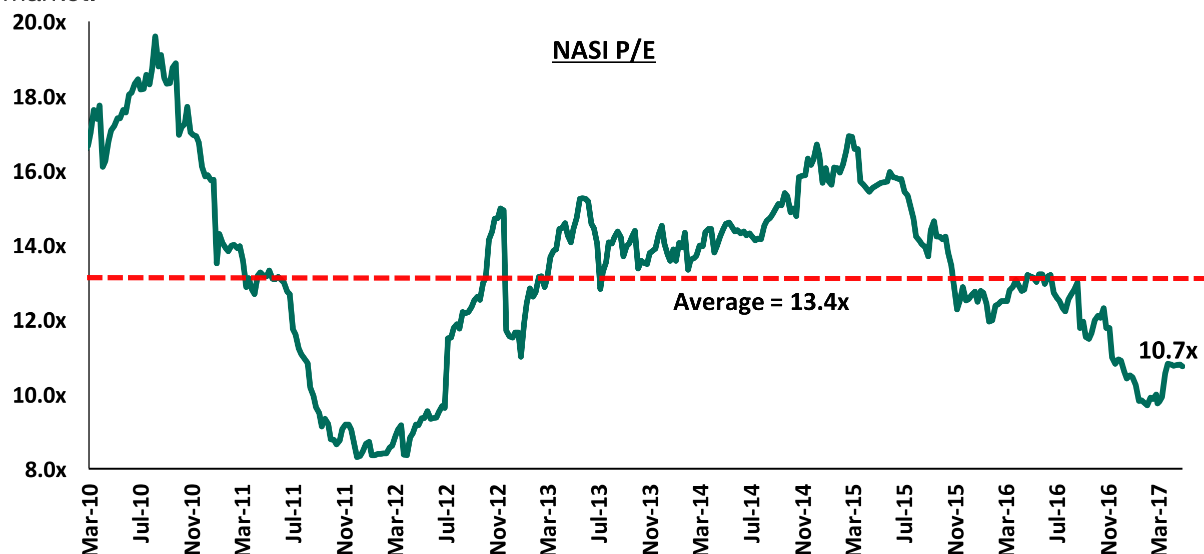
though not to the deficit level of borrowing, with total expenditure for the first half of the 2016/17 fiscal year coming in at Kshs 928.5 bn, which represents 83.6% of the pro-rated target of Kshs 1.1 tn. Development expenditure for the first half of the 2016/17 fiscal year had an absorption rate of 73.8% against 92.5% for recurrent expenditure. Given that the government has historically exceeded the absorption rate on recurrent expenditure averaging 103.5% while the development expenditure has averaged 65.0%, leaving the overall budget absorption rate below 100.0% consistently in the last 5 fiscal years, there still exists upwards pressure on interest rates, but may be subdued unless spending picks up. Government may also be looking at concessionary loans to finance the spending rather than borrowing from the foreign market. This creates a level of uncertainty in the interest rate environment as domestic borrowing may exert an upward pressure on interest rates, and result in longer term papers not offering investors the best returns on a risk-adjusted basis. It is due to this that we think it is prudent for investors to be biased towards short-term fixed income instruments.

Equities

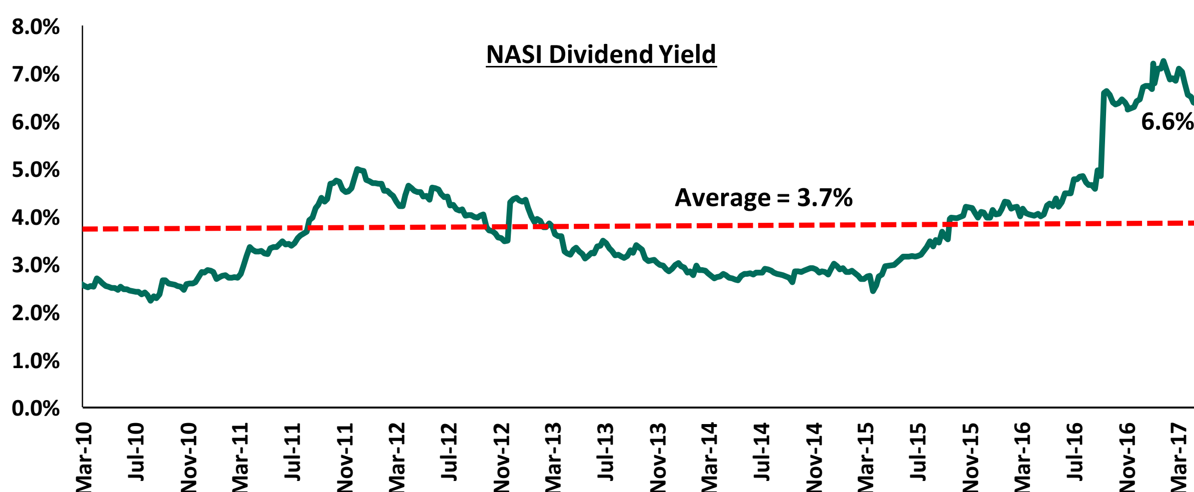
During the month of April, the equities market was on an upward trend with NASI, NSE 20 and NSE 25 gaining 2.4%, 1.4% and 1.3%, respectively, taking YTD performance to 0.0%, (0.9%) and (0.4%), for NASI, NSE 20 and NSE 25, respectively. The equities market performance during the month was driven by gains in large caps led by Diamond Trust Bank, Safaricom and Barclays, which gained 7.8%, 6.9% and 3.1%, respectively. The biggest losers were Standard Chartered and KCB Group, which lost 9.8% and 9.4%, respectively, but losses were mainly due to the stocks going ex-dividend, having offered dividend yields of 6.7% and 8.8%, respectively, at the time of going ex-dividend. Since the February 2015 peak, the market has lost 24.9% and 42.6% for NASI and NSE 20, respectively.

Equities turnover increased by 7.5% during the month to USD 110.4 mn from USD 102.7 mn in March 2017. Foreign investors were net buyers for this month with net inflows of USD 7.2 mn, compared to net outflows of USD 2.2 mn witnessed in March 2017.

The market is currently trading at a price to earnings (PE) ratio of 10.7x, versus a historical average of 13.4x, with a dividend yield of 6.6% versus a historical average of 3.7%. The current 10.7x valuation is 10.3% above the most recent trough valuation of 9.7x experienced in the first week of February of 2017, and 28.9% above the previous trough valuation of 8.3x experienced in December of 2011. The charts below indicate the historical P/E and dividend yields of the market.



Cytonn INVESTMENTS



As indicated in our Cytonn Weekly #14 2017, the month of April saw the Cabinet approve the State-sponsored Financial Services Authority Bill 2017, which seeks to create the Financial Services Authority, a body that will consolidate and take over the functions of the Capital Markets Authority (CMA), the Insurance Regulatory Authority (IRA), the Retirement Benefits Authority (RBA) and the SACCOs Societies Regulatory Authority (SASRA). The merger of the four bodies will (i) provide a consolidated supervisory body for the entire non-banking financial services sector to eliminate regulatory gaps by reducing the number of regulatory bodies, (ii) provide an opportunity for a standard approach to product governance and service delivery, and (iii) raise the level of consumer protection, hence boosting investor confidence in the financial markets.

The Central Bank of Kenya (CBK) issued an operating license to Dubai Islamic Bank Kenya Ltd (DIB), the first by the CBK since 2015 when it placed a moratorium on approving new licenses for banks. This makes DIB Bank Kenya the third fully shariah-compliant lender to operate in East Africa after Gulf African Bank Limited and First Community Bank. DIB's entry, which is anchored on its strategic focus of enhancing its international presence, will expand the offerings in the market, particularly in the promising shariah-compliant banking niche. In addition to DIB Bank, the CBK is also finalizing the licensing of Mayfair Bank, which had received 'approval in principle' before the 2015 suspension of licensing as highlighted in our Cytonn Weekly #11/2017.

In response to the challenging operating environment, banks are increasingly adopting cost rationalization measures such as laying off their staff, closure of branches, reviewing operating hours for some branches, or outright sales in the case of Tier III banks. In addition to KCB Group reporting laying off of 223 employees in 2016, the bank is now offering a voluntary employee buyout programme estimated to save the bank Kshs 2.0 bn per annum and should recover the buyout costs within 18-months. Standard Chartered Bank also intensified the push for customers to embrace digital banking by reducing the number of working hours at some of its branches in Nairobi, leaving customers with the option of transacting through mobile applications and online banking platform. For more details, see Cytonn Weekly#16/2017

Barclays Bank is the latest bank to report laying off of 171 employees in 2016, bringing to 11 the number of banks that have announced downsizing plans since the implementation of the interest rate cap. The bank has steadily been reducing the number of employees as it seeks to automate more operations and cut costs.

	Kenya Banking Sector Restructuring		
	Bank	Staff Retrenchment	Branches Closed
1	Sidian Bank	108	-
2	Equity Group	400	-

3	Ecobank	-	9
4	Family Bank	Unspecified	-
5	First Community Bank	106	-
6	Bank of Africa	-	12
7	National Bank	Unspecified	-
8	NIC	32	-
9	Standard Chartered	300	-
10	KCB Group	223	-
11.	Barclays Bank	171	-

The Communications Authority of Kenya (CAK) released the Telecommunications Sector statistics for Q4'2016, recording improved growth in terms of mobile subscriptions and data consumption. Given the rapid population growth and technological advancements, we expect the industry to continue experiencing strong growth. For more details, see Cytonn Weekly #14 2017. In addition to this, CAK released a report on quality standards in Kenya's telecommunications industry, where Safaricom, Airtel and Telkom Kenya failed to meet the quality standards of voice services, with their overall performance for the year to June 2016 coming in at 50.0%, lower than 62.5% recorded in FY'2014/15, and the regulator's requirement of an 80.0% score on indicators such as speech quality, completed calls, call success rate and drop rate. For more details, see Cytonn Weekly #16/2017

During the month, we had a number of earnings releases, namely:

- Nation Media Group released FY'2016 results, posting a 24.6% decline in earnings per share to Kshs 8.9 from Kshs 11.8 in FY'2015, attributed to a 5.7% decline in operating revenue that outpaced a 2.8% decline in operating expenses. Excluding one-off costs totaling to Kshs 342.9 mn attributed to staff reorganization costs and closure costs on QTV, QFM and KFM Rwanda, the group recorded a 9.2% decline in core earnings per share to Kshs 10.7. For more details, see Cytonn Weekly #14/2017
- Home Afrika released FY'2016 results, posting an improvement in loss per share to Kshs 0.4 from Kshs 0.9 in FY'2015, driven by a 56.4% decrease in operating expenses to Kshs 152.0 mn from Kshs 349.0 mn, attributed to cost reduction measures instituted in 2016 as part of their restructuring.

Below is our equities recommendation table. Key changes from our previous recommendation are:

- We have placed all Insurance stocks under review as we update our valuations following release of their FY'2016 results. We shall be releasing a comprehensive sector report covering Kenya's insurance sector on 8th May 2017.

all prices in Kshs unless stated otherwise

EQUITY RECOMMENDATION

No.	Company	Price as at 31/03/17	Price as at 28/04/17	m/m Change	YTD Change	Target Price*	Dividend Yield	Upside/ (Downside)**	Recommendation
1.	Bamburi	165.0	160.0	(3.0%)	0.0%	231.7	7.8%	52.6%	Buy
2.	KCB***	34.8	31.5	(9.4%)	9.6%	40.1	7.8%	35.1%	Buy
3.	ARM	20.0	25.0	25.3%	(2.0%)	31.2	0.0%	24.8%	Buy
4.	BAT (K)	849.0	844.0	(0.6%)	(7.2%)	970.8	6.2%	21.2%	Buy
5.	Cooperative	14.0	14.0	0.4%	6.1%	14.4	5.7%	8.3%	Hold
6.	Safaricom	18.0	19.3	6.9%	0.5%	19.8	4.7%	7.4%	Hold
7.	Barclays	8.0	8.2	3.1%	(3.3%)	7.9	10.0%	6.3%	Hold
8.	SCBK	215.0	194.0	(9.8%)	2.6%	189.5	6.7%	4.4%	Lighten
9.	Stanbic	63.0	62.5	(0.8%)	(11.3%)	60.2	8.1%	4.4%	Lighten
10.	NIC	26.5	26.8	0.9%	2.9%	26.4	3.0%	1.7%	Lighten
11.	I&M	87.0	91.0	4.6%	1.1%	88.0	3.9%	0.6%	Lighten

12.	Equity	33.0	33.0	0.0%	10.0%	30.7	6.1%	(0.9%)	Sell
13.	HF Group	9.8	10.1	3.6%	(27.9%)	9.2	4.8%	(4.0%)	Sell
14.	DTBK	116.0	125.0	7.8%	5.9%	104.0	2.2%	(14.6%)	Sell
15.	NBK	6.5	6.3	(2.3%)	(12.5%)	1.7	0.0%	(73.0%)	Sell

**Target Price as per Cytonn Analyst estimates*
***Upside / (Downside) is adjusted for Dividend Yield*
****For full disclosure, Cytonn and/or holds a significant stake in KCB Group, ranking as the 14th largest shareholder in the group*
Accumulate – Buying should be restrained and timed to happen when there are momentary dips in stock prices.
Lighten – Investor to consider selling, timed to happen when there are price rallies

We remain "neutral with a bias to positive" for investors with short to medium-term investments horizon and are "positive" for investors with long-term investments horizon.

Private Equity

During the month of April, there were a number of fundraising activities carried out by private equity firms in Africa, as well as acquisitions and buyouts of a number of companies;

On Partnerships, Buyouts and Acquisitions

- Distell Group Limited, a multinational brewing and beverage company based in South Africa, is now the majority owner of Kenya Wine Agencies Ltd (KWAL), after buying out investment firm Centum for an undisclosed amount. The acquisition of Centum's 26.4% stake brings Distell's stake in KWAL to 52.4% from a 26.0% stake acquired in 2014 for Kshs 860 mn, translating to Kshs 34.5 per share. If offered at the same price, Centum, which acquired a stake in KWAL in 1977 at Kshs 12.2 mn, was bought out by Distell for at least Kshs 874.3 mn, translating to an annualized holding period return of 11.3%, excluding any income earned from the investment over the 40-year period. For more information, see our Cytonn Weekly #14/2017,
- Naspers, Africa's biggest e-commerce and digital company, is to invest USD 69.4 mn (Kshs 7.2 bn) into Takealot Online, South Africa's largest e-commerce company. The deal, which is subject to Competition Commission approval, will increase Naspers' stake in the South African e-commerce company to 53.5% from 41.0% (acquired in 2015), effectively valuing Takealot Online at USD 555.2 mn, a premium of 249.6% compared to a value of USD 222.4 mn in 2015 and placing Naspers as the majority shareholder. For more information, see our Cytonn Weekly #16/2017,
- Anglo Dutch petroleum giant Shell has finalized a deal to sell its remaining 20% shareholding in Vivo Energy for USD 250 mn (Kshs 25.8 bn) to Dutch firm Vitol Group, effectively valuing Vivo Energy Investments BV at USD 1.3 bn (Kshs 129 bn). Vivo Energy was a joint venture between Vitol Group, a Dutch firm, Helios Investment Partners, an African private investment firm, and Shell. Vitol will now own a 60% stake in Vivo, leaving Helios Investment with a 40% stake in the firm. Vivo Energy has been the Shell licensee in 16 African markets. In Kenya, Vivo has the second largest Kenyan market in both petroleum and lubricant sales, with 16% and 35% share, respectively after Total which has 18% and 40% share. The transaction sees the completion of a plan by Shell to pull out of the African oil retailing business and focus in areas where it can be most competitive. Vivo will however have to pay royalties to Shell for using the Shell brand,
- CDC, the UK Government owned Development Finance Institution (DFI) and Industrial Promotion Services (IPS), which is Aga Khan Fund for Economic Development's (AKFED) industrial and infrastructure development arm, have launched a new joint power platform. CDC will invest up to USD 70 mn (Kshs 7.2 bn) in the formation of the joint venture and subsequently the partners will invest a further USD 140 mn (Kshs 14.4 bn) and mobilize project funding of USD 1 bn (Kshs 103.1 bn) for new power projects. The aim of the partnership is to boost power generation in Sub Saharan Africa. The joint venture will also house IPS's existing power projects, which include Tsavo Power

Company in Kenya and Bujagali Hydropower Project in Uganda. The partnership is beneficial to both parties as (i) CDC will tap into the AKFED Group's expertise in power generation, and its excellent local relationships, and (ii) AKFED will benefit from CDC's access to funding and its global backing.

On the fundraising front:

- Frontier Investments Management, a Danish private equity firm, raised USD 116.0 mn in the first close of its second fund, Frontier Energy II. The Fund is to finance greenfield renewable energy projects across the Sub-Sahara Africa region. The fund will be implemented in a similar way as its predecessor, a USD 63.8 mn fund, DI Frontier Market Energy and Carbon Fund, which is fully deployed in six different investments with the objective to generate 139.0 MW from the mix of geothermal, solar and hydro power projects in East Africa. Frontier Energy II is meant to achieve an Internal Rate of Return (IRR) of above 20.0% to the investor in the fund by investing between USD 3.0 mn and USD 30.0 mn, in the form of equity, debt or mezzanine, in projects that require capital ranging from USD 5.0 mn up to USD 300.0 mn. For more information, see our Cytonn Weekly #15/2017,
- AfricInvest, the Tunis based private equity wing of the investment financial services Group Integra, is targeting to raise USD 211.5 mn through a new fund (AFSH). The funds will be invested in the financial services sector. AFSH is AfricInvest's second financial sector private equity fund. This fund was launched to take advantage of growth opportunities in the continent. Africa's financial sector is undergoing a profound transformation, through the strategic expansion of financial institutions and digitalization of operations. AfricInvest leverages on the track-record and experience of its first financial sector fund, AfricInvest Financial Sector (AFS) which successfully invested in 21 financial institutions across 16 countries. For more information, see our Cytonn Weekly #16/2017 .

On Exits:

- AfricInvest and Mediterrania, a private equity firm supporting developments in Morocco, Tunisia and Algeria, exited Grupo San Jose & Lopez (SJL) by the sale of their 100% stake to Investec Asset Management (IAM), an asset manager based in South Africa with approximately USD 114.0 bn under its management. Mediterrania Capital and AfricInvest jointly acquired an undisclosed minority stake in SJL in June 2013 and eventually acquired the remainder in August 2015 becoming the sole owners. For more information, see our Cytonn Weekly #15/2017

Private equity investments in Africa remains robust as evidenced by the increased deals and deal volumes in the region's key note sectors; financial services, FMCGs, energy and telecommunication services. The increasing investor interest is attributed to (i) rapid urbanization, a resilient and adapting middle class and increased consumerism, (ii) the attractive valuations in private markets compared to global markets, and (iii) better economic projections in Sub Sahara Africa compared to global markets. Going forward, the increasing investor interest and stable macro-economic environment will continue to boost deal flow into African markets. We thus remain bullish on PE as an asset class in Sub-Sahara Africa.

Real Estate

During the month, KNBS released The Economic Survey 2017, which reported that the real estate sector grew by 8.8% in 2016 compared to 7.2% in 2015, with its contribution to GDP being 8.4% from 8.2% the prior year. Building works completed increased by 7.5% to Kshs

76.2 bn in 2016 from Kshs 70.9 bn in 2015, with the Nairobi County Government building approvals increasing by 43.3% from Kshs 215.2 bn in 2015 to Kshs 308.4 bn in 2016. The improved performance in the sector was driven by increased institutionalization in the sector, increased FDI's and government incentives such as lower tax rates and infrastructural development.

The performance and activities in the various themes during the month are as covered below:

Commercial

The commercial office sector witnessed reduced activity in April 2017, with the key highlights of the month being:

i. Knight Frank released the Africa Report 2017, which focused on real estate performance in 2016 in the continent. According to the report, Kenya's commercial office segment witnessed a slight softening in rents and occupancy levels following increased supply. This is in line with the recently released Cytonn Commercial Office Report 2017, which also revealed that the market is currently oversupplied, constraining performance. It has hence transitioned to a buyers' market with specific pockets of value such as in Grade A offices,
ii. In addition, the Africa Report 2017 highlighted that the retail theme in Kenya is holding stable despite the addition of 100,000 square meters of retail space in 2016, findings of which were in line with the Broll Kenya Office, Retail and Industrial Report released earlier in the month. The Broll report also revealed that retail developers continue to add more retail space to the Nairobi Metropolis market, with approximately 3.7 mn square feet expected to begin construction in 2017. It also claimed that local retailer expansion plans were unable to match the current retail space supply, and hence a decline in occupancy rates with the more established centers having occupancy levels more than 90%, while for the newer centers the occupancy rates are currently averaging at less than 75%,
iii. Infomineo, a global business research firm also released a report that showed there was a 17.0% increase in the number of Fortune 500 Companies in the region in 2016 as compared to 2015. Nairobi is preferred by multinational firms seeking to expand their presence in Africa due to its central location as well as an enabling business environment. Kenya, which has evolved as a regional hub for financial and technology services also remains the biggest economy in East and Central Africa and combined with a stable macro-economic environment, is expected to continue attracting multinational companies that are looking to set up operation within the region.

We thus expect to witness reduced development activity in the theme as investors react to the lower uptake and stagnating returns. In a bid to reduce competition and attract clients, we will also witness an improvement in the quality of services, increased advertising and differentiation in both the retail and office segments.

Residential

The residential sector has continued to grow with increased demand for housing across the country. The World Bank released the Kenya Economic Update 2017 report during the month that highlighted the need for investment in housing, which will create jobs and improve economic growth, mainly achievable by unlocking the residential housing market through the development of the housing finance market. The key take outs were:

- There is an estimated accumulated housing deficit of over 2 million units, with 244,000 housing units needed against a supply of approximately 50,000 housing units per

annum, against an urbanization rate of 4.4%, leading to approximately 61% of urban households living in slums,
- 48.0% of the residential supply is in the upper middle-income segment, 35.0% in the high income segment, 15.0% in the lower middle-income and 2.0% in the lower income,
- Nairobi was ranked as the highest priced city in Africa, with prices beyond the reach of more than 90.0% of Kenyans, with the cheapest homes in the capital Nairobi now priced at Kshs 4 mn, up from Kshs 500,000 in the year 2000.

The report highlighted solutions for the housing finance challenges in Kenya, including (i) use of housing finance subsidies, (ii) housing guarantee mechanism for low or informal income borrowers, (iii) creation of Mortgage Refinance Companies/Mortgage Liquidity Facilities, whereby a mortgage lender issues a bond to raise equity capital from investors, and (iv) adaptation of a Housing Microfinance (HMF), which is similar to a traditional microfinance to provide small loans for self-help housing or progressive building among low income communities. While the proposed solutions may address the question of affordability for the end-user, in our view, they do not address the challenges affecting developers, which include high land prices, steep infrastructure and construction costs and lack of access to funding.

Jumia Kenya released a report highlighting the opportunity in student housing. According to the report, there are 280,000 bed spaces available across the country against a student population of 760,000 and rising. A business case conducted by JLL in 2016 revealed that the student housing provides a good investment opportunity for the following reasons: (i) steady income from solid rental growth and resilience from tough economic times, (ii) high occupancy, backed by a strong demand, (iii) low risk profile given the multi-tenant nature of student housing, and (iv) increased propensity to spend with the growth of the middle class. In our view, developers ought to target student strongholds such as Thika Road and Langáta Road, minimize on construction costs and sizes in order to optimize on rental yields and ensure above average property and facilities management for better service.

Other highlights in residential real estate include;

i. Uriithi Co-operative Society announced plans to construct a high-end gated mixed use development dubbed 'Osten Terrace Gardens' on 10-acres in Nairobi-Tala, along Kangundo Road,
ii. Tata Housing development, a subsidiary of Tata Group, entered into a deal with Indian National Housing Bank and an unnamed real estate firm to develop more than 4.5 mn square feet of mixed-use townships in Kenya and Tanzania targeting middle-income earners,
iii. Tatu City announced plans to construct a residential development, dubbed Tatu Waters, in Ruiru, which will comprise of 2,715 townhouse and apartment units at an approximate cost of Kshs 35.0 bn, and,
iv. The Industrial and Commercial Development Corporation (ICDC) entered into a Memorandum of Understanding with Standard Chartered Bank to ease purchase of its Coast-based homes. Potential buyers into Nyali Zamia Heights apartments in Mombasa shall benefit from an extended loan repayment tenor of up to 25-years from the bank, which translates to lower monthly charges on home loans.

We expect the residential sector to continue witnessing increased development activity mainly due to huge undersupply of cumulatively 2 mn houses growing by 200,000 p.a. against a meagre supply of 50,000 units p.a.

Hospitality

During the month, Kenya was ranked the third most preferred travel destination by high-net-worth individuals (HNWI) in Africa in 2016 according to a report released by AfrAsia Bank, in

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collaboration with New World Wealth. According to the report, Kenya was visited by 4,000 multimillionaires in 2016. The most preferred location for the HNWI was South Africa, which was a destination for 15,000 multimillionaires. In Kenya, the most preferred holiday destinations by the HNWI were Nairobi and Maasai Mara due to the Safari experience offered in both places, which host world famous National Parks. The report is a testament to Kenya's recovering tourism sector after a slowdown due to insecurity. The number of visitors increased by 10.4% from 1.2 mn visitors in 2015 to 1.3 mn in 2016, and with the stability in security in the country we expect the numbers to continue growing.

Also during the month, Mombasa Beach Hotel announced its plans to undergo a Kshs 200 mn face-lift. The renovation entails modernizing the hotel's 151 rooms and public areas including a popular bar on its seafront and an indication of the industry players' readiness to the improving prospects.

With continued improvement in infrastructure, increased Meetings Incentives Conferences and Exhibitions (MICE) tourism, increased marketing by the government through the Kenya Tourism Board (KTB), and improved security leading to reversal of travel advisories, we expect the hospitality theme to continue on the growth path, though the tourist numbers may be constrained in the second and third quarters of 2017 due to the upcoming elections.

Land

The land sector has continued to record high returns and sustained growth. According to the recently released Hass Consult Land Price Index, land prices in Juja, 32 kilometers from Nairobi, for instance, appreciated by 45.2% in the year to March 2017, with an acre selling for an average of Kshs 11 mn. Ruiru, which is also along Thika Road, recorded a 44.0% increase in the same period, with the price of an acre at Kshs 23 mn.

The key take outs from the report were:

- Nairobi's inner city suburbs and satellite towns continued to record positive returns, as land prices increased during Q1'2017, mainly due to improved infrastructure,
- The report also highlighted Tigoni as the best performing satellite town with a 5.9% increase in land prices. Ruiru, Juja and Limuru also experienced tremendous growth due to road construction projects, which have made them more accessible for institutional grade development, and,
- The other areas that recorded the highest land price increase were Donholm (3.6%), Langata (3.1%) and Karen (2.5%), all benefitting from road developments.

On legal matters, the Cabinet waived fees for land title searches during the month. The process of title searches in Kenya, which has often been described as bureaucratic, has often caused delays characterized by cases of bribery, missing titles or duplicate titles, among others. With the costs on land title searches being scrapped off, it is expected that more Kenyans will take the initiative of conducting searches on their titles before dealing in property as part of proper due diligence.

On the fundraising front, Shelter Afrique received Kshs 597 mn from two of its shareholders, Cameroon and Africa Re Insurance. The Development Finance Institution is expecting to receive a total of Kshs 4.9 bn from other 9 of its financiers by June of 2017. It has been plagued by cases of corruption and inefficiencies that have seen 50% of its loan book being declared non-performing and hence needs cash injections to facilitate liquidity and business continuation.

With increased financing and institutionalization in the sector, our outlook for the sector remains positive, especially for long-term investments. We expect reduced development activity in the second and third quarters of the year due to the anxiety over the upcoming elections but returns will hold steady picking up in the last quarter of 2017 and in 2018.

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