Cytonn SSA Financial Services Research: CAFF Weekly Note #25/2019

Executive Summary

In Kenya, during the week, Safaricom and Equity Bank reached a financing deal enabling Safaricom's suppliers, dealers and agents to access up to Kshs 200.0 mn unsecured short-term loans to manage cash flow positions ahead of payment. In Nigeria, Moody's highlighted in its report that it was maintaining a stable outlook on the Nigerian banking system to reflect its resilient capital buffers and stable deposit bases, with high risks likely to subside as the economy is expected to strengthen. In Ghana, the Bank of Ghana released a Banking Sector Report highlighting the developments and performance of Ghana's banking sector during the first four months of 2019. According to the report, asset growth of the industry remained strong, underpinned by increased deposit mobilization, reflecting increased confidence in the banking sector following the recent clean-up exercise and recapitalization reforms.

Section I: Market Performance

During the week, the equities markets recorded a decline with NASI, NGSEASI, and GGSECI declining by 1.7%, 0.7%, and 0.7%, respectively. This takes the YTD performance of NASI, NGSEASI, and GGSECI to 5.0%, (5.0%) and (7.3%), respectively.

Below is a summary of top gainers and losers in our financial services universe of coverage for the week:

Weekly Top Gainers and Losers					
Top Gainers			Top Losers		
Company	Country	Change	Company	Country	Change
CAL Bank	Ghana	14.8%	Ecobank	Ghana	(21.8%)
Ecobank Transnational	Nigeria	13.5%	National Bank	Kenya	(9.1%)
GCB Bank	Ghana	8.7%	Bank of Kigali	Rwanda	(5.2%)
Access Bank	Nigeria	7.3%	Standard Chartered	Ghana	(5.2%)
CRDB	Tanzania	4.3%	Stanbic IBTC Holdings	Nigeria	(5.0%)

Kenya

During the week, the equities market was on a downward trend with NASI, NSE 20 and NSE 25 declining by 1.7%, 2.2%, and 2.2%, respectively, taking their YTD performance to gains/(losses) of 5.0%, (6.6%), and 0.2% for NASI, NSE 20 and NSE 25, respectively. The performance in NASI was driven by declines in EABL, NIC Group, and Bamburi that declined by 5.1%, 4.1%, and 2.5%, respectively. In our universe of coverage, the top gainers were Stanbic Holdings and Barclays bank, which recorded gains of 2.0% and 1.0%. The largest decliners, on the other hand, were National Bank, NIC Group, HF Group, Diamond Trust Bank, Equity Group and Co-operative bank that recorded declines of 9.1%, 4.1%, 3.4%, 3.3%, 1.9%, and 1.6%, respectively.

Nigeria

The Nigerian All-Share Index (NGSEASI) declined by 0.7% driven by losses in consumer goods which declined by 1.6% offsetting gains recorded in Insurance (8.3%), Industrial goods (3.2%), Banking (2.5%), Pension (0.8%) and Oil and Gas (0.7%). This takes the YTD performance of the NGSEASI to a decline of 5.0%.

In our universe of coverage, the largest gainers were Ecobank Transnational and Access Bank, which recorded gains of 13.5% and 7.3%, respectively. The largest decliner was Stanbic IBTC Holdings, which recorded a decline of 5.0%.

Ghana

The GSE Composite Index recorded a decline of 0.7% taking the YTD performance to a decline of 7.3%. In our universe of coverage, the largest gainers were CAL Bank and GCB Bank that recorded gains of 14.8% and 8.7%, respectively. The largest losers, on the other hand, were Ecobank Ghana and Standard Chartered Ghana which recorded declines of 21.8% and 5.2%, respectively.

Section II:

There were no earnings released during the week.

Section III:

Kenya

During the week, Safaricom and Equity Bank reached a financing deal enabling Safaricom's suppliers, dealers and agents to access up to Kshs 200.0 mn unsecured short-term loans to manage cash flow positions ahead of payment. Safaricom had 1,164 suppliers and 440 active dealers in the financial year ended March 2019 and 156,000 M-Pesa agents. The size of the loan to be accessed and terms will be subjected to an individual firm's credit grading. Suppliers, dealers, and agents who provide information on local purchase orders or contractor financing, bid bonds, performance guarantees, advance payment guarantees and back-to-back letters of credit before they start supplying will access a maximum unsecured loan of Kshs 100,000. In our view, the financing deal will benefit Safaricom as the thousands of Safaricom suppliers, dealers and agents targeted will be able to provide the telco better services as a result of better cashflows and hence an increase in their operational efficiency. The financing deal will also be beneficial to Equity Bank as it will enable them to grow their loan book, which grew by 12.7% to Kshs 305.5 bn in Q1'2019, from Kshs 271.1 bn in Q1'2018, as well as grow their Non-Funded Income (NFI) which grew by 6.8% to Kshs 7.2 bn in Q1'2019, from Kshs 6.7 bn in Q1'2018. The financing deal is an indicator of Equity Bank's aggressiveness evidenced by Equity Bank having the second highest NFI contribution to total operating income. We expect banks to continue focusing on revenue diversification in the current regime of compressed interest margins. Focus on Non-Funded Income (NFI) is likely to continue, as banks aim to grow transactional income via alternative channels such as agency banking, internet, and mobile technologies.

KCB Group served National Bank of Kenya (NBK) with take-over documents to acquire a 100% stake of ordinary shares of the Company upon conversion of the preference shares into ordinary shares. Under the take-over documents, KCB intends to satisfy the offer price consideration through a share swap of 1 ordinary share of KCB for every 10 ordinary shares of NBK. National Bank of Kenya (NBK) says it will negotiate to ensure that staff do not lose their jobs in the looming takeover by KCB. NBK currently has 1,356 staff. KCB said that part of the takeover will involve streamlining human resource in the post-acquisition period, raising fears of staff-layoffs of NBK employees. The exact number of staff who will be retained is yet to be determined as the takeover documents are yet to be filed with the Competition Authority of Kenya (CAK), who are mandated to consider the public interest that includes jobs and substantial lessening of competition. There are instances when CAK has compelled firms to retain staff of target companies for a certain period. The regulator in May 2019 approved the Commercial Bank of Africa (CBA) and NIC Group Plc merger on condition that they retain their respective staff for at least a year. The agency in 2014 ordered Britam to retain at least 85 employees of its acquisition target Real Insurance's 105 staff. In our view, the merger if it goes through, will result in the closing of branches and staff layoffs as KCB restructures the business to achieve operational efficiency. NBK's staff costs increased by 5.3% to Kshs 1.0 bn in Q1'2019, from Kshs 0.9 bn in Q1'2018. We expect banks to continue focusing on operational efficiency with cost containment likely to continue being a focus area. We thus expect continued restructuring, possible leading to staff layoffs, as staff headcount demands reduce, on the increased usage of mobile and internet channels.

Nigeria

During the week, Moody's highlighted in its report that it was maintaining a stable outlook on the Nigerian banking system to reflect its resilient capital buffers and stable deposit bases, with high risks likely to subside as the economy is expected to strengthen. Moody's projects that Nigerian banks' asset risk and profitability will remain key rating challenges, but expect these challenges to gradually decline in 2020 as the economy picks up. According to the report, real GDP is forecasted to expand by 2.3% in 2019 and 2.8% in 2020 up from 1.9% recorded in 2018. Lending growth is expected to recover in the second half of 2019 following a contraction in 2018, but it will remain subdued, and will not appreciably boost banks' revenue. Capital buffers are projected to remain steady with system-wide tangible common equity stable at 16.0% of risk-weighted assets at year-end 2018, sufficient to absorb losses. Moody's expects subdued loan growth and prudent dividend payouts to support banks' capitalization metrics. As a result of subdued loan growth coupled with increasing cost pressure derived from investments in IT, and increases in loan loss provisions charges following the implementation of IFRS 9, profitability will be strained. Further, funding and liquidity are expected to remain stable underpinned by solid deposit bases and moderated foreign-currency lending by banks. Lastly, Moody's reports that the Nigerian government's capacity and willingness to support systemically important banks in times of stress will remain strong, given the significant consequences of a bank collapse to both the payments system and to the wider economy. We take note of how the continuous restructuring of the sector has led to improved stability, aided by various consolidation and stringent policies by the CBN, such as lenders being required to set up capital conservation and counter-cyclical buffers to protect them against domestic and foreign shocks.

Ghana

During the week, the Bank of Ghana released a Banking Sector report underlining the developments and performance of Ghana's banking sector during the first four months of 2019. The report highlighted the composition of the banking sector, which consists of twenty-three (23) banks with a total number of 1,225 branches spread across the sixteen (16) regions of the country as of April 2019. The report highlighted the reduction in the number of branches by 20.7% to 1,225 in FY'2019, from 1,546 in 2018, with the reduction attributed to branch rationalization following Ghana's banking sector reforms. The report highlighted that asset growth of the industry remained strong, as they grew by 12.4% to GHS 109.9 bn in FY'2019, from GHS 97.8 bn in FY 2018, underpinned by increased deposit mobilization, where deposits rose by 19.6% to GHS 73.1 bn in April 2019 from GHS 61.1 bn in April 2018, reflecting increased confidence in the banking sector following the recent clean-up exercise and recapitalization reforms. Total investment in bills and securities grew by 26.5% to GHS 44.4 bn at end of April 2019 from GHS 35.1 bn at end of April 2018, reflecting an investment portfolio mix in favor of high-yielding long-term securities. Bank borrowings however contracted by 11.0% from GHS 16.4 bn in April 2018 to GHS 14.6 bn in April 2019, as banks relied less on borrowings to fund their assets. According to the report, Ghana's banking industry's capital base remains strong on account of the recently completed recapitalization exercise. Paid-up capital grew strongly by 70.5%, from GHS 5.2 bn to GHS 8.90 bn, while total shareholders' funds (paid-up capital and reserves) increased by 12.9% to GHS 15.5 bn in April 2019. The Bank of Ghana maintained a positive outlook for the sector on the back of improved profitability indicators of the banking sector, coupled with improved operational efficiency indicators, improved asset quality and a gradual decline in the NPL Ratio. We note the adoption of Basel II/III framework, recapitalization of the sector and other policy reforms, which are expected to improve risk management practices and capital adequacy of banks, and thus contribute to reducing non-performing loans and promote credit expansion, growth, and profitability within the industry.

Section IV: Equities Universe of Coverage:

The week-on-week performance, valuation and expected return of the companies in our SSA universe of coverage is highlighted in the table below.

Banks	Price as at 14/06/2019	Price as at 21/06/2019	w/w change	YTD Change	*Target Price	Dividend Yield	**Upside /Downside	P/TBv Multiple	Recommendation
Diamond Trust Bank	120.0	116.0	(3.3%)	(25.9%)	228.4	2.2%	99.1%	**0.6x**	Buy
Zenith Bank	20.1	20.0	(0.5%)	(13.2%)	33.3	13.5%	80.1%	**0.9x**	Buy
UBA Bank	6.2	6.4	3.7%	(16.5%)	10.7	13.2%	79.6%	**0.4x**	Buy
CRDB	115.0	120.0	4.3%	(20.0%)	207.7	0.0%	73.1%	**0.4x**	Buy
KCB Group***	39.5	39.0	(1.3%)	4.1%	60.4	9.0%	63.9%	**1.0x**	Buy
GCB Bank	4.6	5.0	8.7%	8.7%	7.7	7.6%	62.0%	**1.2x**	Buy
I&M Holdings	55.0	54.3	(1.4%)	27.6%	81.5	6.5%	56.7%	**1.0x**	Buy
CAL Bank	0.8	0.9	14.8%	(5.1%)	1.4	0.0%	50.5%	**0.8x**	Buy
Co-operative Bank	12.3	12.1	(1.6%)	(15.4%)	17.1	8.3%	49.2%	**1.0x**	Buy
Access Bank	6.4	6.9	7.3%	1.0%	9.5	5.8%	44.1%	**0.4x**	Buy
NIC Group	31.8	30.5	(4.1%)	9.7%	42.5	3.3%	42.6%	**0.6x**	Buy
Equity Group	40.0	39.3	(1.9%)	12.6%	53.7	5.1%	41.8%	**1.7x**	Buy
Ecobank	10.0	7.8	(21.8%)	4.3%	10.7	0.0%	37.2%	**1.7x**	Buy
Barclays Bank	10.3	10.4	1.0%	(5.0%)	12.8	10.6%	33.6%	**1.3x**	Buy
Guaranty Trust Bank	30.9	31.2	1.1%	(9.3%)	37.1	7.7%	26.5%	**2.0x**	Buy
Stanbic Bank Uganda	30.0	30.0	0.0%	(3.2%)	36.3	3.9%	24.8%	**2.1x**	Buy
SBM Holdings	5.7	5.7	0.0%	(4.4%)	6.6	5.3%	20.4%	**0.8x**	Buy
Stanbic Holdings	98.0	100.0	2.0%	10.2%	113.6	5.9%	19.4%	**1.1x**	Accumulate
Union Bank Plc	6.9	7.0	0.7%	24.1%	8.2	0.0%	17.3%	**0.7x**	Accumulate
Bank of Kigali	290.0	275.0	(5.2%)	(8.3%)	299.9	5.0%	14.1%	**1.5x**	Accumulate
Standard Chartered	194.0	192.0	(1.0%)	(1.3%)	200.6	6.5%	11.0%	**1.4x**	Accumulate
Bank of Baroda	128.0	129.0	0.8%	(7.9%)	130.6	1.9%	3.2%	**1.1x**	Lighten
FBN Holdings	7.0	7.0	0.1%	(12.5%)	6.6	3.6%	(1.1%)	**0.4x**	Sell
National Bank	4.4	4.0	(9.1%)	(24.8%)	3.9	0.0%	(1.4%)	**0.2x**	Sell
Standard Chartered	21.6	20.5	(5.1%)	(2.4%)	19.5	0.0%	(5.1%)	**2.6x**	Sell
Stanbic IBTC Holdings	42.0	39.9	(5.0%)	(16.8%)	37.0	1.5%	(5.8%)	**2.1x**	Sell
Ecobank Transnational	10.0	11.4	13.5%	(33.2%)	9.3	0.0%	(18.2%)	**0.4x**	Sell
HF Group	4.4	4.3	(3.4%)	(23.3%)	2.9	0.0%	(31.8%)	**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*
*****Stock prices indicated in respective country currencies*

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.