



Commercial Bank of Africa (CBA) issues a cash buyout offer to acquire Jamii Bora Bank

CBA Group has issued a Kshs 1.4 bn cash buyout offer to owners of Jamii Bora Bank, in a bid to acquire 100.0% of the lender. If successful, this will be the second bank acquisition in 2019, after the acquisition of a 24.2% stake in Prime Bank Kenya by AfricInvest and Catalyst Principal Partners, in line with our expectation of increased consolidation in the Kenya banking sector following the enactment of the Banking (Amendment) Act, 2015, and the fact that Kenya is overbanked, as highlighted in our [Q3'2018 Banking Sector Report](#).

Jamii Bora is a Tier III bank with an overall market share of 0.3% according to the Central Bank of Kenya's Annual Supervisory Report, 2017, and has 0.2% of total deposits in the banking sector. The bank focuses on the Small and Medium Enterprises (SME) banking segment, and has 17 branches in Kenya. CBA Group, on the other hand, has a 5.7% market share, 6.2% of the total deposits in the banking sector, and has also begun merger negotiations with listed NIC Group, as analysed in our [Nairobi Metropolitan Area Serviced Apartments Report - 2018, & Cytonn Weekly #47/2018](#).

CBA Group has issued Jamii Bora owners with the buyout offer of Kshs 1.4 bn, to acquire a 100.0% stake in the lender. Jamii Bora's financial performance has been deteriorating since Q1'2017, possibly caused by the implementation of the Banking (Amendment) Act 2015, which capped interest chargeable on loans at 4.0% above the Central Bank Rate (CBR), with the bank's loan declining to Kshs 8.3 bn as at FY'2017, from Kshs 10.5 bn, in FY 2016, in the first full year of the interest rate cap implementation. The declining loan book consequently saw the interest income decline by 36.2% to Kshs 1.4 bn in FY 2017, from Kshs 2.2 as at FY'2016. Consequently, operating income declined 57.8% to Kshs 0.5 bn from Kshs 1.3 bn in FY'2016. With the decline faster than the decline in total operating expenses of 28.0% to Kshs 1.3 bn from Kshs 1.8 bn, and consequently, the bank recorded losses, and the loss making trend continued. The declining performance impacted its liquidity, with its liquidity position declining to (11.1%) as at Q1'2017, indicating its inability to meet any short-term obligations. With Jamii Bora's equity at Kshs 3.4 bn, without further injection, it would imply the transaction would happen at a P/Bv ratio of 0.4x.

The summary of the transaction is as below:

1. CBA Group will acquired a 100.0% stake in Jamii Bora through the buyout of existing shareholders, of Kshs 1.4 bn, and possibly an additional unspecified capital injection,
2. As at Jamii Bora's last reporting in Q1'2018, the bank had a book value of Kshs 3.4 bn,
3. As such, the transaction is being carried out at a price-to-book value (P/Bv) of 0.4x, which is a 60.0% discount to the bank's book value, and 69.2% discount to the current listed banks trading P/Bv multiple of 1.3x.

The significant discount to the book value may be due to (i) the possibility of an additional capital injection by CBA, with Jamii Bora operating at a negative liquidity position, and (ii) the high Non Performing Loans ratio of 22.4% as at Q1'2018, with gross NPLs of Kshs 2.2 bn. We are of the view that the bank's acquisition presents the best case scenario, to navigate the relatively tougher, and competitive operating environment, amid expectation that Mshwari may be spun off and operate under Jamii Bora, with possibly the intention of shaping management's focus on the corporate and Small and Medium Enterprise (SME) banking in the merged entity after the NIC-CBA merger.

The table below indicates previous banking acquisition deals and their transaction multiples in the Kenyan banking industry;

Acquirer	Bank Acquired	Book Value at Acquisition (Kshs bns)	Transaction Stake	Transaction Value (Kshs bns)	P/Bv Multiple	Date
CBA Group	Jamii Bora Bank	3.4	100.00%	1.4	0.4x	1/11/2019*
AfricInvest Azure	Prime Bank	21.2	24.20%	5.1	1.0x	19-Jan
NIC Group	CBA Group	30.6**	Undisclosed	Undisclosed	N/A	Dec-18*
KCB Group	Imperial Bank	Unknown	Undisclosed	Undisclosed	N/A	18-Dec
SBM Bank Kenya	Chase Bank Ltd	Unknown	75.00%	Undisclosed	N/A	18-Aug
DTBK	Habib Bank Kenya	2.4	100.00%	1.8	0.8x	17-Mar
SBM Holdings	Fidelity Commercial Bank	1.8	100.00%	2.8	1.6x	16-Nov
M Bank	Oriental Commercial Bank	1.8	51.00%	1.3	1.4x	16-Jun
I&M Holdings	Giro Commercial Bank	3	100.00%	5	1.7x	16-Jun
Mwalimu SACCO	Equatorial Commercial Bank	1.2	75.00%	2.6	2.3x	15-Mar
Centum	K-Rep Bank	2.1	66.00%	2.5	1.8x	14-Jul
GT Bank	Fina Bank Group	3.9	70.00%	8.6	3.2x	13-Nov
Average			76.10%		1.6x	
* Announcement date						
** Book Value as of the announcement date						

From the table, we can see that our local bank acquisition price-to-book average is at 1.6x, down from the previous 1.7x due to the deal, which has the lowest multiple at 0.4x, behind the DTBK-Habib bank deal at 0.8x. The average stake acquired is at 76.1%, up from 73.5%. Previously, transactions have taken place at a premium, (i) SBM and Fidelity at 57.0% above market, (ii) I&M Holdings and Giro at 30.8% above market, and (iii) M Bank and Oriental at 9.0% above market. Thus going forward, we expect acquisition transactions to take place at cheaper valuations.

Key take-away from this transaction are:

- i. Kenya's banking sector consolidation will continue to happen and it will lead to a more stable, safer banking sector,
- ii. Smaller banks constrained in capital, and struggling in their operations are likely to continue receiving take-over offers, which would present the best case scenario to navigate the current competitive banking sector landscape, and,
- iii. Transactions are happening at significantly cheaper valuations, perhaps due to the smaller banks' relatively poor performance, leading to cash and liquidity constraints, which may warrant even further capital injections, hence the cheaper acquisition costs.

This is a further case of consolidation in the banking sector with banks such as Jamii Bora Bank, who are uncompetitive in the market, being bought out. It continues to echo our sentiments on the attractive investment opportunity in financial services in Kenya, indicating that it is the best time to be an acquirer.