Cytonn FY'2021 Equities Markets Review Note

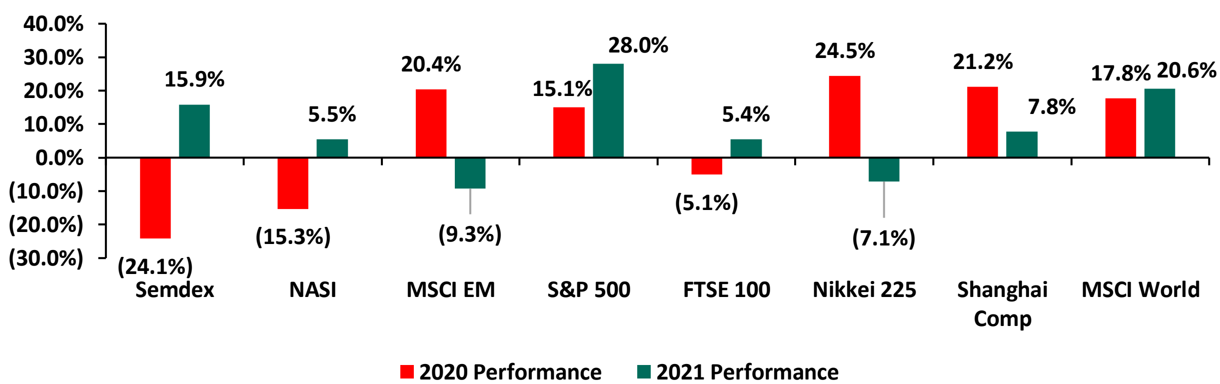
In 2021, the global equity markets continued to recover, with most indices being on an upward trajectory mainly driven by the improved investor sentiments following the gradual economic recovery seen in most nations. However, indices such as the MSCI Emerging Markets and Nikkei 225 declined; recording losses of 9.3% and 7.1%, respectively, attributable to increased sell off of tech stocks following new strict regulations introduced in China which aimed to intensify the government's influence over tech companies. Despite the positive recovery, the discovery of new strains of COVID-19, uneven vaccine rollout and supply chain constraints will lead to some economies recovering slower than others. In this note, we will analyze the 2021 Equities Markets Performances in the following sections;

i. Global Markets Review,
ii. SSA Regional Review,
iii. Kenya's Equities Market, and,
iv. Conclusion

Section I: Global Markets review

The global equity markets registered mixed performance in 2021, with MSCI Emerging Markets and Nikkei 225 being the only decliners among the major world indices. The losses recorded by MSCI EM and Nikkei 225 can be attributed to increased sell off of tech stocks following new strict regulations introduced in China which aimed to intensify the government's influence over tech companies. The tech stocks had rallied during the third and fourth quarters of 2020, leading to the indices gaining at a period when most world indices were recording losses brought about by the adverse effects of the pandemic. Growth in the global equities markets mainly been driven by the economic recovery from the COVID-19 pandemic, accommodative monetary policies and increased rollout of vaccines which has improved the control of the pandemic. Below is a chart highlighting the performance of select stock indices;

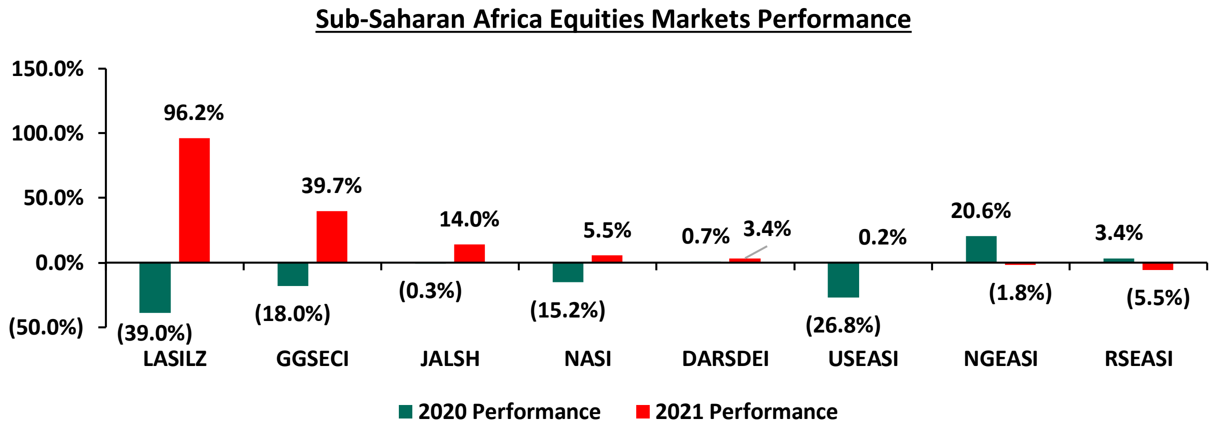
Global Equities Performance



Source: S&P Capital IQ (Dollarized)

Section II: Sub-Saharan Africa Review

In 2021, the Sub-Saharan Africa (SSA) stock markets recorded mixed performance in 2021, with most of the markets recording positive returns, attributable to the improved investor sentiments in the region. The Zambia Stock market (LASILZ) was the best performing with a 96.2% index gain, attributable to the recovery of copper prices. On the other hand, Rwanda's RSEASI was the worst-performing index, recording losses of 5.5%, mainly attributable to a deterioration in the business environment following the sustained lockdowns put in place to curb the spread of COVID-19, hence lowering investor sentiments. Below is a summary of the performance of key indices:

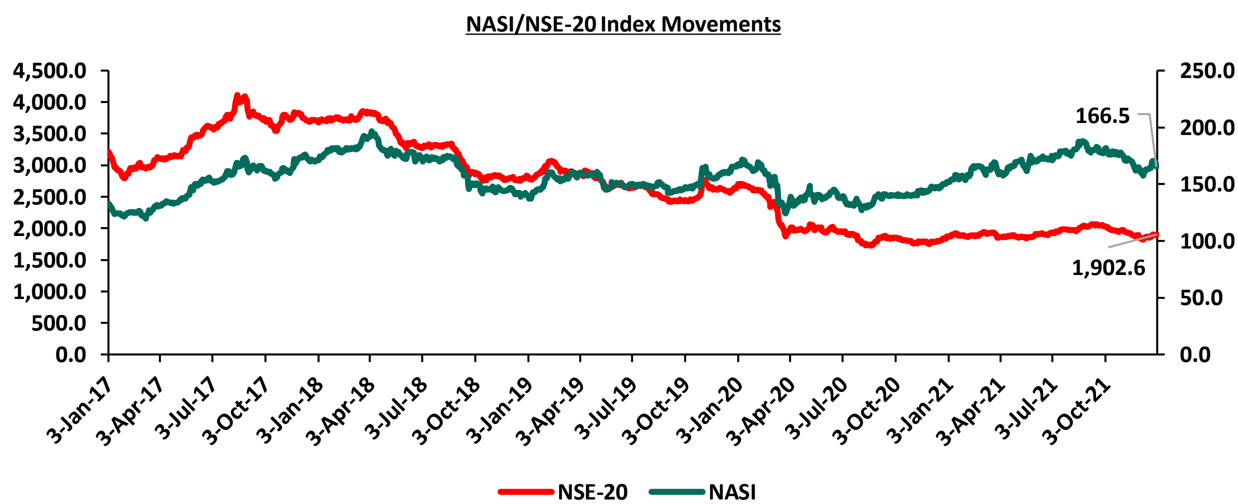


Source: S&P Capital IQ (Dollarized)

Section III: Kenya Equities Markets Review

a. Stock Performance

In 2021, the equities market was on an upward trajectory, with NASI, NSE 25 and NSE 20 increasing by 9.5%, 9.8% and 1.6%, respectively. The equities market performance was driven by gains recorded by large cap stocks such as Equity Group, ABSA Bank Kenya, BAT Kenya, KCB Group and Safaricom of 45.5%, 24.5%, 22.3%, 18.4%, and 10.8%, respectively. The gains were however weighed down by losses recorded by other banking stocks such as DTB-K, Standard Chartered Bank Kenya (SCBK), and NCBA Bank Kenya which declined by 22.5%, 11.2% and 5.3%, respectively. Equity turnover during the year declined by 11.2% to USD 1.3 bn, from USD 1.4 bn in FY'2020. Foreign investors remained net sellers, with a net outflow of USD 91.9 mn in FY'2021, compared to net outflows of USD 280.9 mn recorded in FY'2020. The graph below highlights the performance of the NASI and NSE 20 indices during the year;



Source: NSE

The table below highlights the performance of the some of the large cap stocks in the Kenyan stock market in 2021;

Kenyan Equities Performance – Large Cap Gainers and Losers 2021					
No.	Company Name	Year Open Share Price-2021 (Kshs)	Year End Share Price-2021 (Kshs)	2020 Performance	2021 Performance
1	Equity Group	36.25	52.75	**(33.5%)**	**45.5%**
2	ABSA Bank Kenya	9.52	11.85	**(27.6%)**	**24.5%**
3	BAT Kenya	361.00	441.50	**(23.5%)**	**22.3%**
4	KCB Group	38.40	45.45	**(30.7%)**	**18.4%**
5	Safaricom	34.25	37.95	**8.6%**	**10.8%**
6	East African Breweries Limited (EABL)	154.00	165.00	**(21.9%)**	**7.1%**
7	Co-operative Bank Kenya	12.55	12.95	**(24.5%)**	**3.2%**
8	Bamburi Cement	39.95	38.00	**(52.7%)**	**(4.9%)**
9	NCBA Bank Kenya	26.60	25.20	**(28.3%)**	**(5.3%)**
10	Standard Chartered Bank Kenya	144.50	128.25	**(29.4%)**	**(11.2%)**
11	Diamond Trust Bank Kenya (DTB-K)	76.75	59.50	**(31.8%)**	**(22.5%)**

The key take outs from the above table include:

i) The Banking sector recovered during the year, with Equity Group, ABSA, BAT Kenya and KCB Group recording gains of 45.5%, 24.5%, 22.3%, and 18.4%, respectively. The performance was driven by significant improvement in the listed banking sector earnings, recording a weighted average increase in their core earnings per share of 102.0%, compared to a weighted decline of (32.4%) in Q3'2020. The increase in EPS is mainly attributable to the reduced provisioning levels by the sector, as the Loan Loss Provisions declined by 32.6% in Q3'2021, from the 322.3% growth recorded in Q3'2020, following the relatively stable business operating environment during the period,

ii) The Manufacturing sector also recorded growth during the year, with BAT's share price growing by 22.3% while EABL recorded a gain of 7.1%. BAT's performance is partly attributable to improved investor confidence in the counter as the firm's gross revenue increased by 21.8% to Kshs 20.2 bn in H1'2021, from Kshs 16.6 bn H1'2020, on the back of a recovery in domestic sales volumes, excise duty-led price increases and sustained momentum in exports. On the other hand, EABL's performance is mainly due to improving investor sentiments as investors expect the easing of COVID-19 related restrictions, including the lifting of the nationwide curfew in October 2021, to boost the firm's performances as operating hours for bars and restaurants in Kenya revert to normal,

iii) On the Construction front, Bamburi's share price declined by 4.9% during the year, as a result of investors' maintaining cautious stance with regards to the counter as the cement industry in Kenya continues to face overcapacity issues with the latest figures showing a consumption level of 6.0 mn metric tonnes in the country, equivalent to be at 45.8% of the total production of 13.1 mn metric tonnes as of 2019. We however expect improved performance in the short term as the current government continues to prioritize affordable housing and road infrastructure projects in its final year in 2022. In its H1'2021 results, Bamburi Cement reported a significant increase of 420.7% in Profits before tax to Kshs 1.1 bn in June 2021, from Kshs 228.0 bn in June 2020. The increase in profits was partly attributable to increased demand in Cement for the construction of the Nairobi Expressway project and Thwake Dam along the Kitui - Makueni border, and,

iv) In the Telecommunication Sector, Safaricom continued to exert its dominance in the bourse, with its market cap closing the year at 59.5% of the entire bourse as at 31st December 2021. The counter gained by 10.8% during the year driven by the increased investor demand for the stock following the recent acquisition of a Telecommunications Operator License by the Global Partnership for Ethiopia, coupled with a 12.1% increase in the firm's core earnings per share to Kshs 0.9 in H1'2022, from Kshs 0.8 in H1'2021. The increase in the earnings growth was attributable to the 45.8% increase in M-PESA revenue to Kshs 52.3 bn, from Kshs 35.9 bn in H1'2021, following the lifting of the waiver by the Central Bank of Kenya on all charges for transactions below Kshs 1,000.

b. Listings and Suspensions

During the year, the Nairobi Securities Exchange (NSE) delisted National Bank of Kenya (NBK), effective 25th November 2021. This came after the successful takeover by KCB of 100.0% of all the ordinary shares of National Bank of Kenya (NBK) in September 2019. NBK became the 13th firm since 2001 to be de-listed in the NSE with Kenol/Kobil being the most recent exit in August 2019.

c. Profit Warnings

In 2021, 4 companies issued profit warnings to investors compared to [15 companies in 2020], as a result of the improved business environment following the lifting of COVID-related restrictions. Companies are required to issue profit warnings if they project a more than 25.0% decline in profits year-on-year. The four companies are Centum Investment Company PLC, Umeme Limited, Williamson Tea Kenya PLC, and, WPP ScanGroup PLC. For more information, see our [2021 Annual Review].

Section IV: Conclusion

As the global economy continues to rebound gradually in 2021, we expect to see increased investor flows into the Equities Markets as investors aim to boost their returns by taking advantage of the relatively cheap valuations in most stocks. We expect investors to continue to be biased towards stocks that continue to register quick recovery and robust earnings growth on the back of their strong fundamentals. However, the Equities market performance will continue to be weighed down by the threat of a resurgence in COVID-19 infections and related restrictions. The Kenyan equities market recorded a 9.5% growth in 2021 mainly due to the strong performance of some large cap stocks in the banking, telecommunications and construction sectors. We expect prices to continue exhibiting growth in 2022, albeit at a slower pace, due to risks posed by the elections on corporate earnings and profit taking measures by investors who registered large gains last year.

Overall, we are "Neutral" on equities for investors with a medium-term investment horizon as the upcoming general elections coupled with emergence of new COVID-19 strains dampen the equities market outlook in 2022. We expect constrained activity and subdued inflows from foreign investors as they adopt a wait and see approach in anticipation of the outcome of the general elections. However, in our view, there still remain pockets of value still exist in the equities market, with NASI's Price to Earnings ratio (P/E) currently at 11.0x, 14.7% below the historical average of 12.9x.