Cytonn SSA Financial Services Research: January 2019 Monthly Note

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Executive Summary

During the week, data released by The Kenya National Bureau of Statistics showed that commercial banks in Kenya reduced their deposit rates to 5.7% in November 2018, the lowest in 15-months, from a high of 7.0% in February 2018. In Nigeria, Fitch ratings highlighted that the recent merger between Access Bank and Diamond Bank will amplify the two-tiered nature of the Nigerian Banking sector, which is characterized by the top 5 banks controlling a 60.0% of all the sector's assets.

Section I: Market Performance:

During the week, the equities markets had mixed performances with the NASI and NGSEASI gaining 3.8% and 2.9%, respectively, and GGSECI declining by 0.6%. This takes the YTD performance of Kenya, Nigeria and Ghana to 14.2%, 1.1%, and (3.2%), 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
Guaranty Trust Bank	Nigeria	14.7%	Stanbic Bank Uganda	Uganda	(3.3%)
Access Bank	Nigeria	10.8%	Ecobank Transnational	Nigeria	(2.5%)
NIC Group	Kenya	10.1%	CAL Bank	Ghana	(1.1%)
UBA Bank	Nigeria	7.0%	SBM Holdings	Mauritius	(1.0%)
Barclays Bank	Kenya	7.0%	Stanbic Holdings	Kenya	(0.5%)
KCB Group	Kenya	6.6%	Standard Chartered Ghana	Ghana	(0.4%)

Kenya

During the week, the equities market was on an upward trend with NASI gaining 3.8%, taking the YTD performance to 14.2%. The gain in NASI was mainly driven by gains in large cap banking stocks such as NIC Group, Barclays Bank, KCB Group and Standard Chartered Bank, which gained by 10.1%, 7.0%, 6.6% and 5.9%, respectively, on a bullish run driven by positive corporate earnings expectations.

Nigeria

The Nigerian All Share Index (NGSEASI) gained by 2.9% during the week, largely driven by gains in the banking sector, consumer goods and Insurance, with weighted gains of 8.1%, 6.7%, and 4.0%, respectively. In our universe of coverage, Guaranty Trust Bank, Access Bank and UBA Bank were the largest gainers gaining by 14.7%, 10.8% and 7.0%.

Ghana

The GSE Composite Index declined by 0.6% during the week, driven by declines in the oil and gas and financial services sectors. In our universe of coverage, CAL Bank and Standard Chartered Ghana, declined by 1.1% and 0.4%, respectively, while Ghana Commercial Bank (GCB) was the only gainer, gaining by 2.0%.

Section II: Earnings Releases:

Kenya Banks' Performance:

There were no earnings releases during the month.

Nigeria Banks' Performance:

There were no earnings releases during the month.

Ghana Banks' Performance:

There were no earnings releases during the month.

Section III: Weekly Highlights:

Kenya

Safaricom customers have borrowed Kshs 6.2 bn in one month on the Fuliza overdraft service, revealing a huge pent-up demand for instant, micro-loans in the economy. The Fuliza overdraft facility, which was launched on 5th January 2019, is a partnership involving Safaricom, Commercial Bank of Africa (CBA) and KCB Group. The banks provide M-Pesa users with top-up loans whenever they need to make a transaction, but find they lack enough money in their mobile cash wallets. The virtual loan amounts can be used to buy goods, pay bills and is also transferrable to other mobile subscribers. The service has been used by 4.2 mn customers. The Fuliza loans attract an interest rate of 1.08% a day, which translates to 395.3% per annum. An additional administrative fee of up to Kshs 30.0 is charged for each day that the loan remains unpaid. The overdraft facility has a term of 30-days beyond which a borrower is deemed to be in default. Fuliza analyses the creditworthiness of borrowers by an analysis of their transactions and borrowing history among other factors. Borrowers can take loans of upto Kshs 70,000. Fuliza joins the growing list of digital lending platforms, such as Branch and Tala, that seek to offer small loans through the internet and mobile phones. Kenyans' rising demand for quick loans has spawned the growth of unregulated microlenders with annualised interest rates ranging from 18.0% to more than 200.0%. Micro-lending is far more lucrative than mainstream banking whose margins have been restricted by the capping of lending rates. The fast paced growth is set to boost the fees collected by Safaricom, KCB and CBA. Besides the facility and administration fees, Fuliza also attracts standard M-Pesa charges, further boosting Safaricom's earnings from the mobile money platform. For CBA and KCB, Fuliza offers an opportunity for customer acquisition and an additional high-margin revenue stream.

According to data from the Kenya National Bureau of Statistics, commercial banks in Kenya reduced their deposit rates to 5.7% in November 2018, the lowest in 15-months, from a high of 7.0% in February 2018. This comes after the removal of the 70.0% of the Central Bank Rate (CBR) floor, after the assention of the Finance Act 2018 in September 2018. The removal of the floor on deposit rates and retention of a ceiling on lending rate has failed to unlock credit to the private sector with the private sector credit growth coming in at 2.4% in the 12-months to December 2018, slower than the 3.0% recorded in the 12-months to November 2018. The reduction in deposit rates is in a bid to increase net interest margins (NIM) for banks due to reduced interest expense on deposits.

Nigeria

According to Fitch ratings, the recent merger between Access Bank and Diamond Bank will amplify the two-tiered nature of the Nigerian Banking sector. The merger, which is set to be completed in June 2019, will see the 5 largest banks control more than 62.0% of the total industry deposit liabilities and more than 60.0% of the total assets. The combined entity will control 15.0% of the total sector assets, and will have the largest retail customer base in Africa, of 29.0 mn. With the five largest banks controlling more than 60.0% of the total sector, Fitch noted that banks would be able to easily access both local, and the international markets for funding, as shown in 2016-2017 when Access Bank, UBA and Zenith Bank accessed foreign Eurobond markets, even when there was a foreign-currency shortages in the country. The merger was credit positive, as larger banks were better placed in attracting retail deposits owing to their stronger brands and extensive branch networks. This consequently helps keep their funding costs in check. We note that the consolidation in the Nigerian banking sector has slowed down in pace, with the sector currently having 21 banks from 89 banks in 2004. Regulation induced consolidation has seen the number of players reduced drastically to the current 21, with the fewer players remaining having adequate capital bases. We maintain our view that with fewer well-capitalized players the banking sector on aggregate would be more stable, with the players able to absorb any systemic distress, in addition to comfortably performing the financial intermediation function of deposit mobilization and credit extension.

Ghana

Customers and financial markets participants in Ghana have regained confidence in Consolidated Bank of Ghana, according to a statement by the Managing Director Daniel Addo. The statement highlighted the banks initial difficulty in merging the operations of the banks. Consolidated Bank was formed after a merger of five banks in August, 2018: Construction Bank, Beige Bank, Royal Bank, UniBank and Sovereign Bank, after the 5 banks had their licenses withdrawn after their inability to meet the minimum capital requirements of GHS 400.0 mn, and were found to have committed regulatory breaches, which lead to the banks becoming insolvent. The bank is currently owned 100.0% by the Government of Ghana. The merger resulted in forming the second largest bank, with 148 branches. Customers of the banks are now able to access their deposits, with the bank drawing down on the GHS 7.6 bn bond, which will also be used to meet liquidity demands. The bond, was issued in November 2018, in two tranches of GHS 3.2 bn and GHS 4.4 bn. The bank highlighted that it has initiated its target operating model, which will see the bank audit its branch network and weed out branches that do not meet the standards. We note that with the Bank of Ghana enforcing the higher GHS 400.0 mn minimum capital requirement from GHS 120.0 mn, and stricter regulation, banks have been able to retain sufficient capital buffers, in addition to enforcing strict corporate governance policies in operation procedures. This should lead to a sector that is not only credit positive, but also efficient in curbing fraudulent and money laundering activities.

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:

Universe of Coverage								
Banks	**Price as at 01/02/2019**	**Price as at 08/02/2019**	**w/w change**	**YTD Change**	**Target Price***	**Dividend Yield**	**Upside/Downside****	**P/TBv Multiple**
GCB Bank***	4.1	4.2	2.0%	(9.1%)	7.7	9.3%	97.6%	**1.0x**
Diamond Trust Bank	147.5	151.0	2.4%	(3.5%)	283.7	1.8%	94.1%	**0.8x**

Access Bank	6.0	6.7	10.8%	(2.2%)	9.5	6.7%	65.0%	**0.4x**
UBA Bank	7.2	7.7	7.0%	(0.6%)	10.7	11.9%	61.5%	**0.5x**
KCB Group	40.9	43.6	6.6%	16.4%	61.3	7.3%	57.2%	**1.3x**
Zenith Bank***	22.9	24.4	6.6%	5.9%	33.3	11.8%	57.3%	**1.0x**
CAL Bank	0.9	0.9	(1.1%)	(9.2%)	1.4	0.0%	55.6%	**0.8x**
CRDB	135.0	135.0	0.0%	(10.0%)	207.7	0.0%	53.9%	**0.5x**
I&M Holdings	95.0	95.0	0.0%	11.8%	138.6	3.7%	49.6%	**1.0x**
NIC Group	34.8	38.3	10.1%	37.6%	48.8	2.9%	43.3%	**0.9x**
Ecobank	7.5	7.5	0.0%	(0.1%)	10.7	0.0%	43.3%	**1.6x**
Equity Group	40.9	42.3	3.4%	21.4%	56.2	4.9%	42.3%	**2.0x**
Co-operative Bank	15.8	16.0	1.6%	11.9%	19.9	5.1%	31.4%	**1.4x**
Union Bank Plc	6.3	6.3	0.0%	11.6%	8.2	0.0%	30.4%	**0.7x**
Stanbic Bank Uganda	30.0	29.0	(3.3%)	(6.5%)	36.3	3.9%	24.8%	**2.1x**
Barclays Bank	11.5	12.3	7.0%	11.9%	12.5	8.7%	17.9%	**1.6x**
Guaranty Trust Bank	33.7	38.7	14.7%	12.2%	37.1	7.1%	17.2%	**2.1x**
SBM Holdings	6.0	5.9	(1.0%)	(0.3%)	6.6	5.0%	14.3%	**0.9x**
Bank of Kigali	278.0	278.0	0.0%	(7.3%)	299.9	5.0%	12.9%	**1.5x**
Standard Chartered	195.0	206.5	5.9%	6.2%	196.3	6.4%	7.1%	**1.6x**
HF Group	6.6	7.0	5.8%	25.6%	6.6	5.3%	5.6%	**0.3x**
Stanbic Holdings	91.3	90.8	(0.5%)	0.0%	92.6	2.5%	3.9%	**0.9x**
Bank of Baroda	134.0	134.2	0.1%	(4.1%)	130.6	1.9%	(0.7%)	**1.2x**
FBN Holdings	7.4	8.0	8.8%	0.6%	6.6	3.4%	(6.4%)	**0.4x**
Standard Chartered	21.1	21.0	(0.4%)	0.0%	19.5	0.0%	(7.7%)	**2.6x**
Stanbic IBTC Holdings	45.3	47.0	3.8%	(2.0%)	37.0	1.3%	(17.0%)	**2.3x**
National Bank	6.0	6.0	(0.3%)	12.4%	4.9	0.0%	(18.3%)	**0.4x**
Ecobank Transnational	14.1	13.7	(2.5%)	(19.4%)	9.3	0.0%	(34.0%)	**0.5x**

** 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 "NEUTRAL" on equities since the markets are currently trading below historical P/E averages. However, pockets of value continue to exist, with a number of undervalued sectors like Financial Services, which provide an attractive entry point for medium and long-term investors, and with expectations of higher corporate earnings this year, we are "POSITIVE" for investors with a long-term investment horizon.