Cytonn FY'2021 Kenya Listed Insurance Sector Report

Cytonn

3rd June 2022

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1. Introduction to Cytonn

About Us

Cytonn Investments is an alternative investment manager, with real estate development capability, and a primary focus on private equity and real estate investments in the high growth Kenyan Region. Cytonn has a unique strategy of coupling two compelling demand areas - the lack of high yielding investment products and the lack of institutional grade real estate. We provide high yielding investment instruments to attract funding from investors, and we deploy that funding to largely pre-sold investment grade real estate. With offices in Kenya and Washington, DC - USA, we are primarily focused on offering alternative investment solutions to global and local institutional investors, individual high net-worth investors, and diaspora investors interested in the East-African region. Real estate investments are made through our development affiliate, Cytonn Real Estate, where we currently have over Kshs. 82 billion (USD 820 mn) of projects under mandate across ten projects. In private equity, we invest in banking, education, and hospitality.

82 Over Kshs. 82 billion worth of projects under mandate

3 Three offices across 2 continents

500 Over 500 staff members, including Cytonn Distribution

10 10 investment readyprojects in real estate

A unique franchise differentiated by:

Independence & Investor Focus

Focused on serving the interest of clients, which is best done on an independent platform to minimize conflicts of interest

Alternative Investments

Specialized focus on alternative assets - Real Estate, Private Equity,and Structured Solutions

StrongAlignment

Every staff member is an ownerin the firm. When clients do well, the firm does well; and when thefirm does well, staff do well

CommittedPartners

Strong global and local partnerships in financing, land and Cytonn Real Estate, our development affiliate

Why We Exist

Africa presents an attractive investment opportunity for investors seeking attractive and long-term returns. Despite the alternative markets in Africa having high and stable returns, only a few institutional players serve the market. Cytonn is focused on delivering higher returns in the alternative markets, while providing the best client service and always protecting our clients' interests.

WE SERVE THREE MAIN CLIENT SEGMENTS:

- High Net-worth Individuals through Cytonn Private Wealth. This is done through our captive Distribution Network
- East Africans in the Diaspora through Cytonn Diaspora
- Global and Local Institutional Clients. These clients are served from our Investment & Fundraising Team

WE INVEST OUR CLIENT FUNDS IN:

- Real Estate, and Real Estate Related Businesses
- Private Equity
- Fixed Income Structured Solutions
- Equities Structured Solutions

Cytonn Business Structure

Cytonn Investments Management Plc

- **Cytonn Investments** (Private Markets)
  - Private Offers (CPN, CHYS & CREN)
  - Cytonn Hospitality
  - Superior Homes Kenya
- **Cytonn Asset Managers** (Regulated by CMA and RBA)
  - Collective Investment Schemes (CMMF, CBF, CEF, CAFF & CHYF)
  - REIT Management
  - Cytonn Advisory
  - Pension Fund Management (CURBS, CPRBS & CIDDF)
- **Cytonn Real Estate**
  - Real Estate Projects (Alma, Ridge, Taraji, Situ, Applewood, Newtown, Riverrun & Kilimani)
  - Research and Deal Origination
  - Project Management
  - Quality Assurance/Quality Control
  - Facilities and Property Management
  - Cytonn Centre for Affordable Housing
- **Strategic Support Services**
  1. Finance
  2. ICT
  3. Legal & Compliance
  4. Brand (PR& Communication)
  5. Client Service
  6. HR & Business Admin
  7. Risk
  8. Internal Audit
  9. Distribution

2. Kenya Economic Review and Outlook

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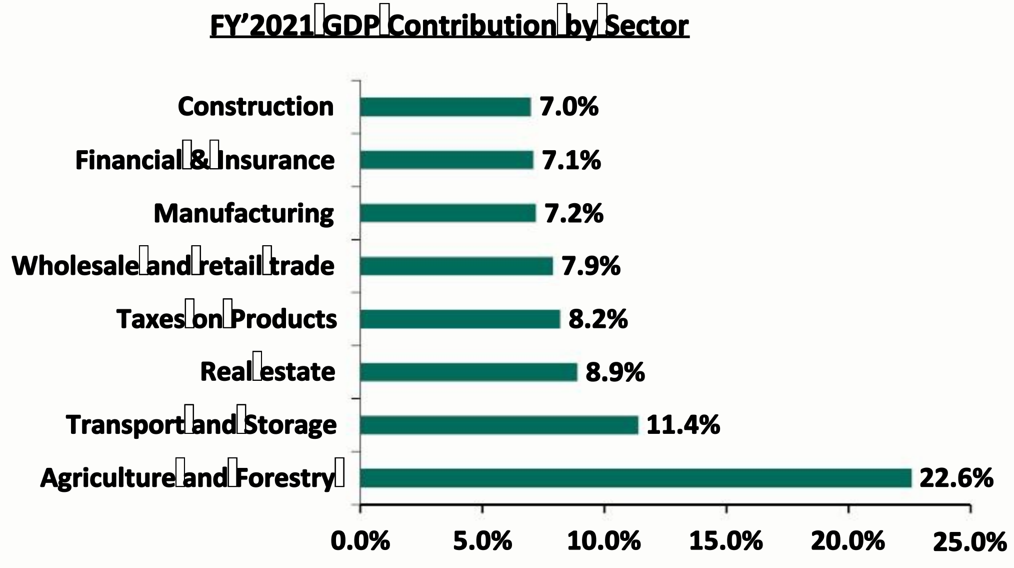
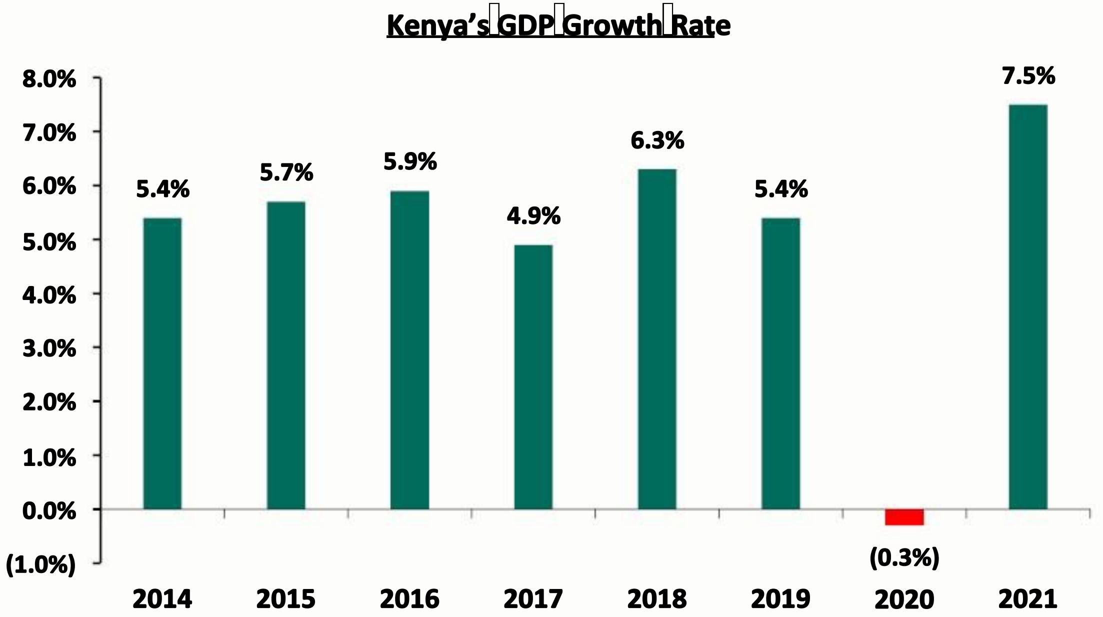
The Kenyan economy expanded by 7.5% in 2021





**Source: KNBS*

- The Kenyan Economy grew at a rate of 7.5% in 2021, up from the 0.3% contraction recorded in FY'2020. The growth was mainly driven by the resumption of most economic activities following the lifting of COVID-19 containment measures put in place in 2020 to curb the spread of the virus, which led to the recovery of most sectors of the economy
- As of 2021, the biggest gainers in terms of sectoral contribution to GDP was transport and storage increasing by 0.7% points to 11.4%, from 10.7% in FY'2020
- We expect the economy to grow by 4.5% in 2022, on the back of global recovery

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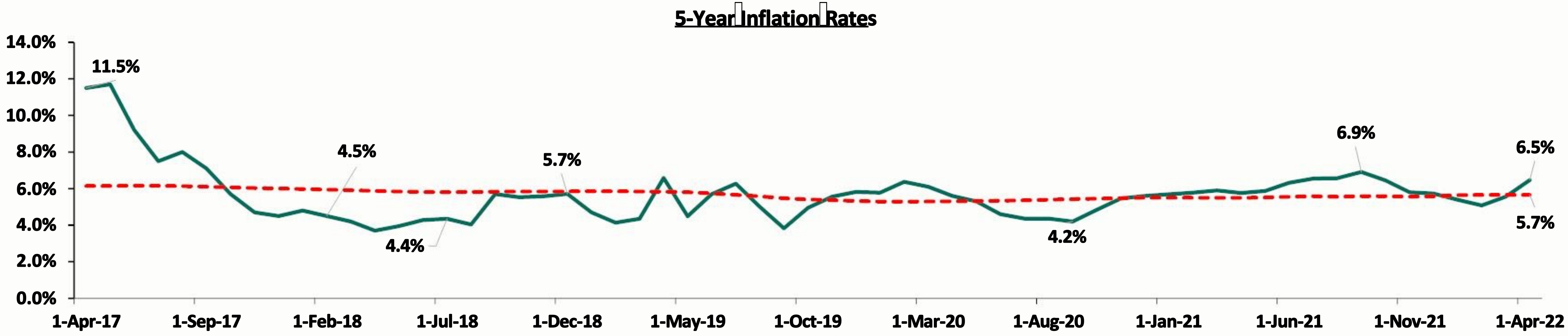
Inflation

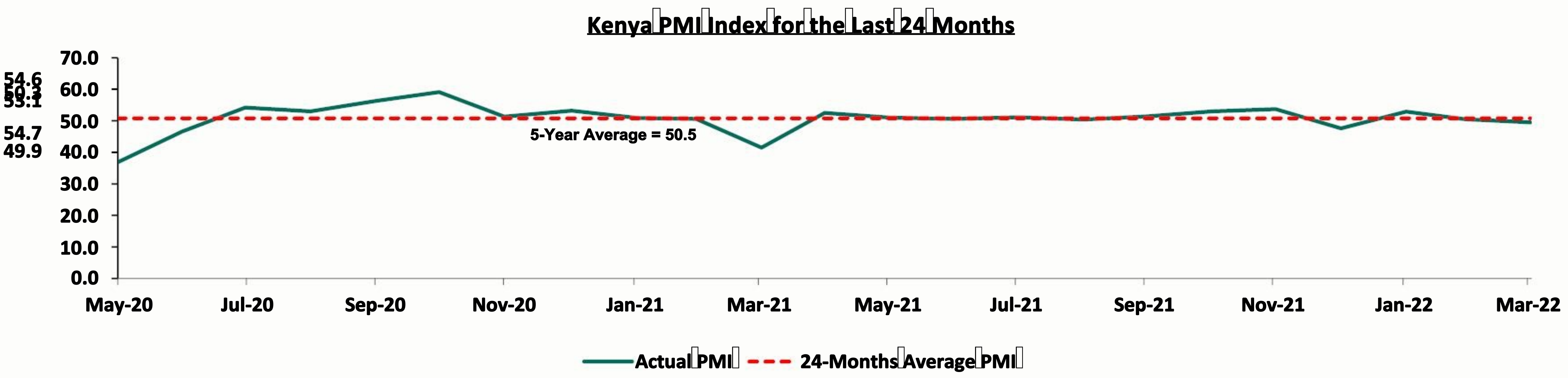
Inflation averaged 5.6% in the first four months of 2022



**Source: KNBS*

- Inflation for the month of April 2022 increased to 6.5%, from the 5.6% recorded in March 2022, mainly attributable to the increase in the y/y Food and non-alcoholic beverages, household equipment, transport as well as housing, water, electricity, gas and other fuels, which increased by 12.2%, 7.2%, 6.9% and 5.5%, respectively
- Going forward, we expect the inflation pressures to remain elevated but within the government's set range of 2.5% - 7.5%. However, concerns remain high on the rising food and fuel prices which are expected to put more pressure on inflation, given that these are major contributors to the inflation basket

Stanbic PMI Index

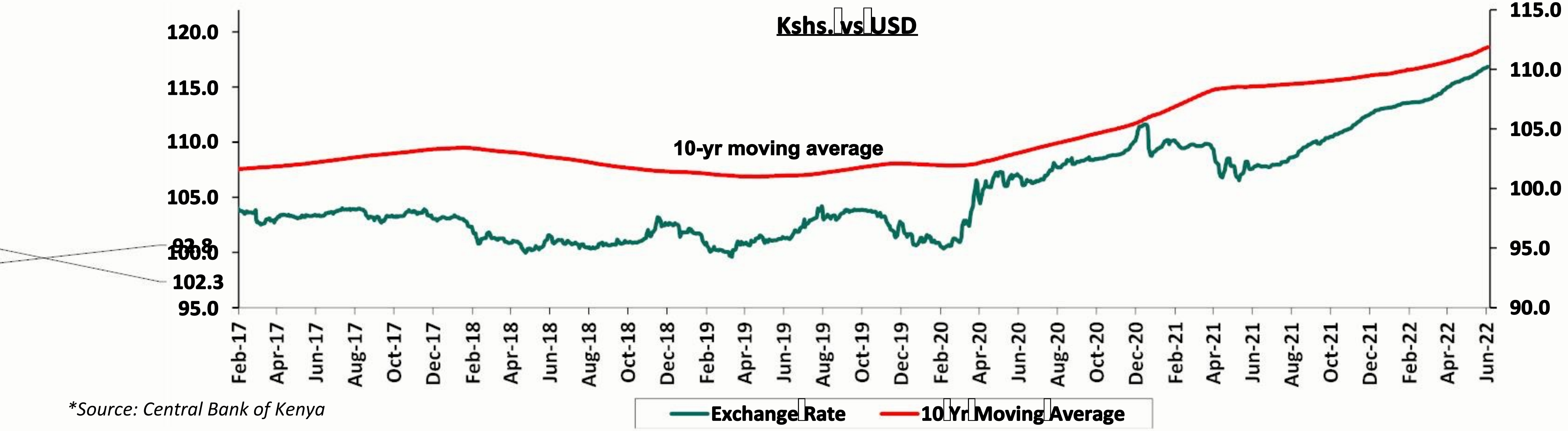


**Source: Markit Economics*

- The Stanbic Purchasing Managers Index(PMI) for the month of April 2022 declined to 49.5 from 50.5 recorded in March 2022 pointing towards a deterioration of the business environment in the Kenyan private sector, mainly attributable high cost of living occasioned by the rising fuel prices and production costs
- Key to note, a PMI reading of above 50 indicates improvements in the business environment, while a reading below 50 indicates a worsening outlook. Despite the stronger growth seen in the period under review, the level of sentiments was weak, as firms were concerned that the economy could face a setback from the pandemic

Currency

Year-to-date, the Kenyan shilling has depreciated by 3.3% against the US Dollar



**Source: Central Bank of Kenya*

- On a YTD basis, the Kenya Shilling depreciated against the US Dollar by 3.3%, to close at Kshs 116.8. The depreciation is mainly driven by the increased dollar demand from oil and merchandise importers on the back of increased global oil prices against slower recovery in exports and in the tourism sector
- In our view, the shilling will come under pressure due to rising global crude oil prices on the back of supply constraints and geopolitical pressures. The local currency is however expected to be supported by the Forex reserves, currently at (USD 8.2 bn (equivalent to 4.9-months of import cover), which is above the statutory requirement of maintaining at least 4.0-months of import cover

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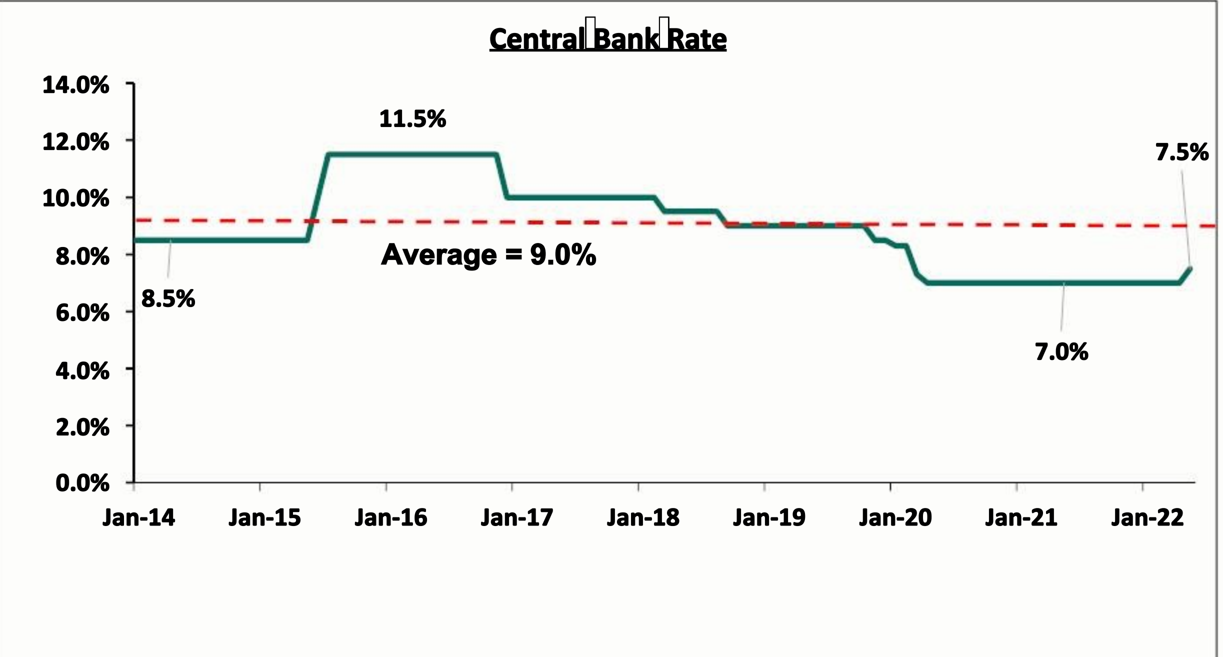
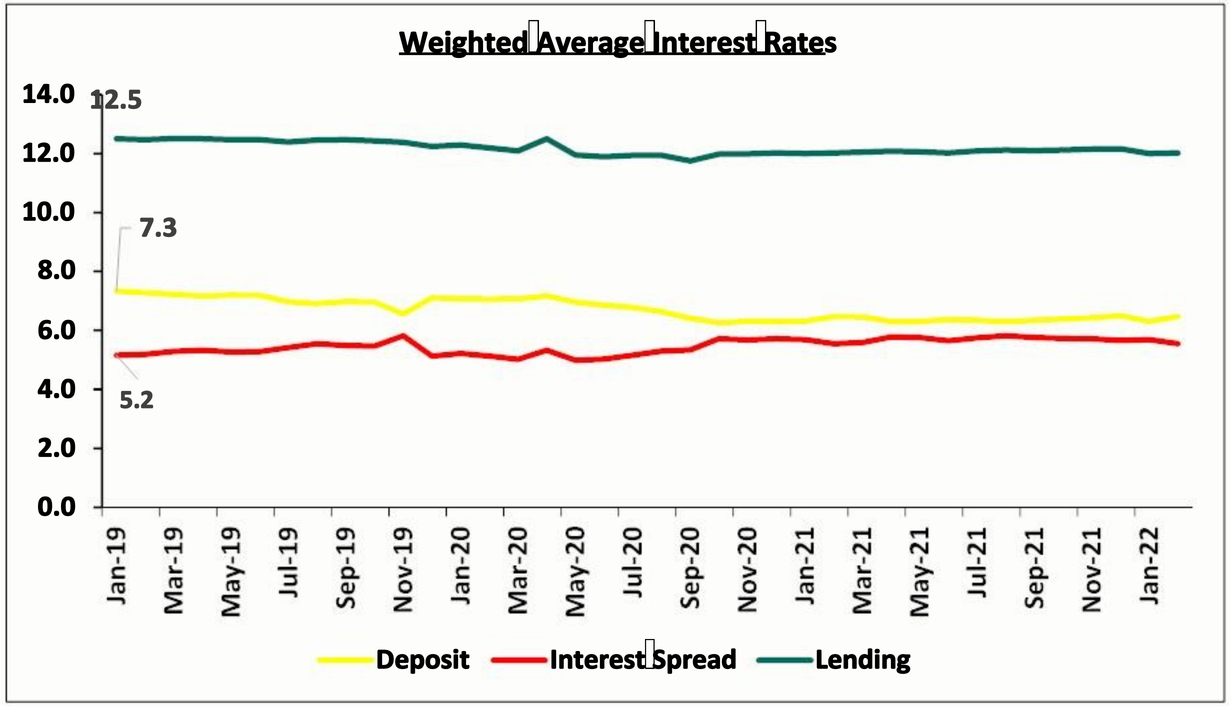
Interest Rates and Monetary Policy



*Source: CBK



- In the last sitting in May 2022, the Monetary Policy Committee increased the benchmark MPC rate to 7.5%, from 7.0% in an attempt to curb the rising and increasing inflation which reached 7.1% in May 2022. The Cash Reserve ratio however remained unchanged at 4.25%
- The Committee noted the elevated risks to the inflation outlook due to increased global commodity prices and supply chain disruptions, and concluded that there was scope for a tightening of the monetary policy in order to further anchor inflation expectations within th governments target range of 2.5% - 7.5%

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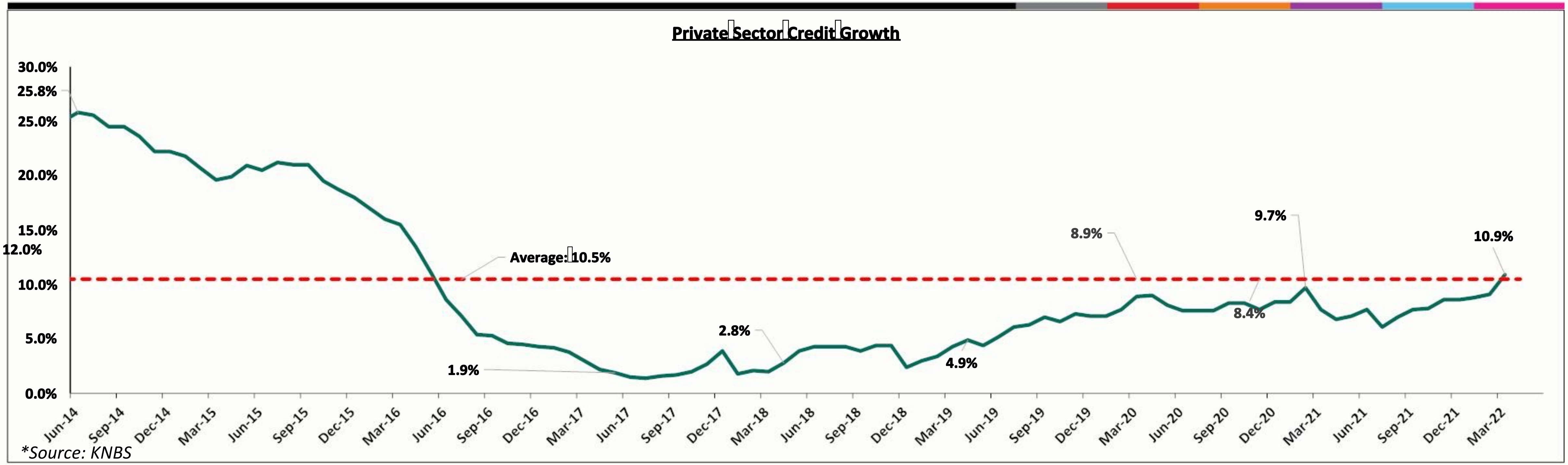
Private Sector Credit growth



- In the 12 months to April 2022, growth in private sector credit stood at 11.5%, an increase from the 9.1% recorded in January 2021 and 6.8% recorded over the same period in 2021, reflecting the increased lending to the private sector on the back of improved business environment as a result of gradual economic improvement
- We expect to see continued caution on lending as credit risk remains elevated amidst uncertainties in the business environment brought about by increased inflationary pressures and the looming August 2022 elections

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3. Kenya Insurance Sector Overview

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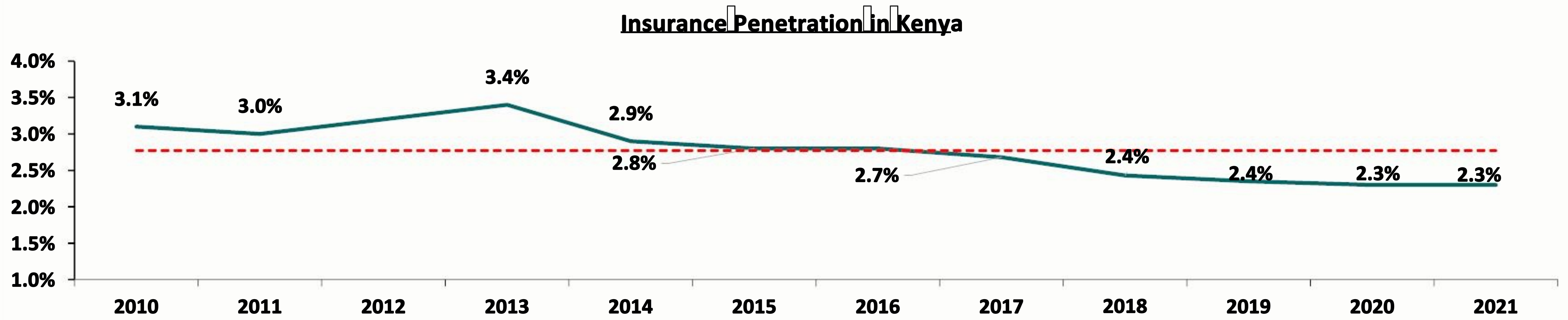
Kenyan Insurance Sector Overview

The Insurance penetration in Kenya stood at 2.3% as at the end of 2021

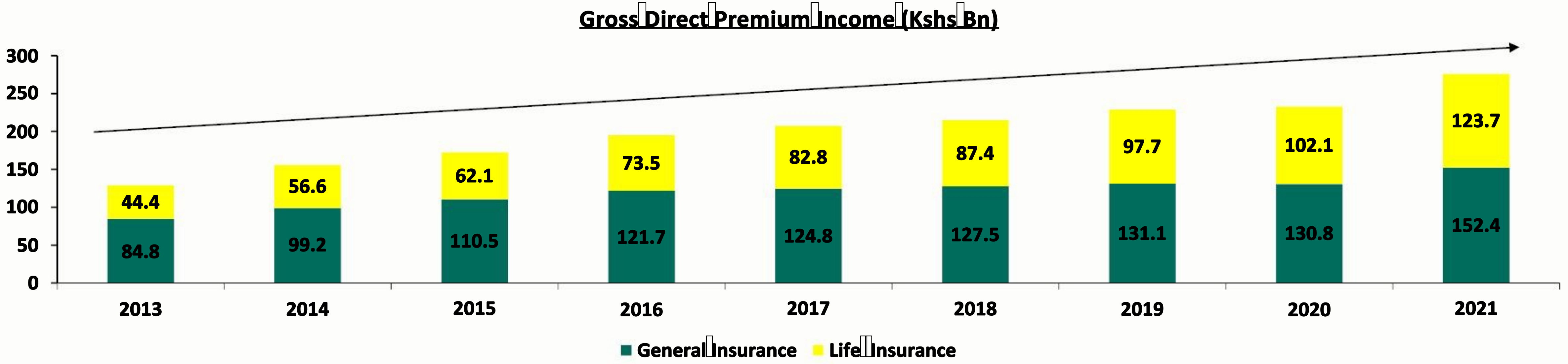
- The industry is regulated by Insurance Regulatory Authority which is responsible for licensing, regulating and developing the insurance sector
- In the last five years, the life insurance market in Kenya has experienced growth in both the level of direct premiums as well as in the equity held by the industry constituents
- In FY'2021, Kenya had 56 insurance companies, 5 reinsurance companies, 220 insurance brokers and 10,522 insurance agents (which includes 26 Bancassurance agents)
- Insurance penetration in Kenya stood at 2.3% of Gross Domestic Product (GDP) in 2021, unchanged from what was recorded in 2020, on the back of price undercutting in an industry where players are facing increasingly tough competition



Source: Central Bank of Kenya, FinAccess report

Kenyan Insurance Sector Overview

General insurance business remains the largest contributor to industry insurance activity at 55.2%



- Industry gross written premium stood at Kshs 276.1 bn as at end of FY'2021, representing an increase of 18.5% from Kshs 233.0 bn in FY'2020. Long term insurance segment grew by 21.1%, while general Insurance recorded a growth of 16.4%
- General insurance business remained the largest contributor to industry insurance activity contributing 55.2% of the total premium. Motor insurance and medical insurance classes of business account for 64.8% of the gross premium income under the general insurance business
- In the long term insurance segment, pensions and life assurance classes were the biggest contributors to the life gross premium income, accounting for 67.4% in FY'2021, compared to the 68.8% contribution by the two classes recorded in FY'2020

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Insurance Sector Growth Drivers

Alternative channels for both premium distribution and claims verification and disbursement is driving the sector

The drivers of growth in the insurance sector in FY'2021 include;

a) **Technology and Innovation**: The industry players continue to innovate products while leveraging on technology to remain competitive. The onset of the COVID-19 pandemic in FY'2020 saw the adoption of digital distribution of insurance products become a matter of necessity. Consequently, many insurance companies increasingly took advantage of the available digital channels to drive growth and increase insurance penetration in the country. An example is Liberty Holdings which has been using AI to rollout e-policy documents, self-services for retail customers and collect customer feedback

b) **Adoption of Alternative Distribution Channels**: Insurance companies have been dynamic and fast in adopting new alternative channels for both distribution and premium collection with financial sector deepening leading to an improved method of distribution of insurance products, collection and payment of premiums like bank assurance, online and mobile payment

c) **Growth of the Middle Class**: In a region with one of the fastest population and economic growth rates, the rise in disposable income is a great driver for the sector. Demand for insurance products and services has grown, for instance, motor insurance, driven by the high rate of car importation into the country recently

Insurance Sector Growth Drivers

New regulations and the use of block chain have also contributed to growth in the insurance sector

d) **Regulation:** The newly introduced regulations in the insurance sector have helped most companies improve their capital management systems. The new compliance requirements as stipulated in IFRS 17 come at a high implementation cost but they also assist companies manage their risks and capital in a better way

e) **Redirection in Core Operations-** With the limited growth of the insurance industry, insurers are moving their focus to growing investment income which involves and increase in the assets under management segments and investments in property. Most insurance companies are now moving into asset management to boost their group revenues

Recent Developments in the Kenyan Insurance Sector

The following are the most recent developments witnessed in the Insurance sector;

1. **IFRS 17 Implementation:** The standard, having replaced IFRS 4, is expected to give better information on profitability by providing more insights about current and future profitability of insurance contracts. Separation of financial and insurance results in the income statement will allow for better analysis of core performance for the entities and allow for better comparability of insurance companies. However, as a way to protect the insurance industry from the negative effects of the pandemic the International Accounting Standards Board (IASB) deferred its implementation to be effective from January 2023 or earlier

2. **Increasing Price Wars**: Insurers have seen a decline in group life business as well as ordinary business as a result of price wars that have been prevalent among the players in the industry. Price wars have negatively impacted performance in the insurance sector. The price wars are as a result of low penetration rate in the country which has led to players in the market undercutting product pricing in order to gain market share. The undercutting continues to be a major challenge in the industry as well as increasing the risk that comes with product mispricing

Recent Developments in the Kenyan Insurance Sector

The insurance sector has seen mergers and acquisitions mainly with companies trying to protect their market share in a competitive environment

3. **Increasing Demand for Life Insurance Products:** There has been a continuous growth in the life insurance market relative to GDP and life insurance premiums have been increasing. Life business was generally less affected by the economic downturn of the past few years

4. **Merger & Acquisition activity:** The insurance sector is booming with mergers and acquisitions mainly with companies trying to protect their market share in a competitive environment. Some of the M&A deals include Jubilee Holdings announcing a strategic transaction with Allianz, a German multinational Underwriter and asset manager, in September 2020, for the sale of 66.0% stake in the general business excluding medical for a total consideration of Kshs 10.8 bn. We expect that this amount will be ploughed back in to the company as part of the capital boost to grow other business lines

5. **Revenue Diversification -** There has been need for diversification necessitated by the slow growth in premiums against an increase in underwriting expenses, leading to insurers pursuing non-traditional asset classes. For example the FY'2020 saw Jubilee Holdings invest Kshs 4.2 bn in Bujagali Power Plant in Uganda, thus increasing the ownership stake to 18.2% from 8.8%

Insurance Sector Market Share

UAP Old Mutual leads in General Insurance business, while Britam dominates in Long term Insurance market

Market Share as at FY'2021			
Insurer	General Insurance Business Market Share	Insurer	Long-Term Insurance Business Market Share
UAP Old Mutual	8.7%	Britam Holdings	20.9%
CIC Group	7.5%	ICEA Lion Insurance	16.2%
GA Insurance	7.2%	Jubilee Insurance	11.3%
APA Insurance	7.0%	Kenindia Assurance	9.0%
Britam Holdings	6.5%	Sanlam Insurance	6.9%
Others	63.1%	Others	35.8%
Total	**100.0%**	**Total**	**100.0%**

Source: IRA Q2'2021 report

- The top 5 insurance companies control 36.9% of the General Insurance market share
- In terms of long term insurance, the top 5 insurers control 64.2% of the market share

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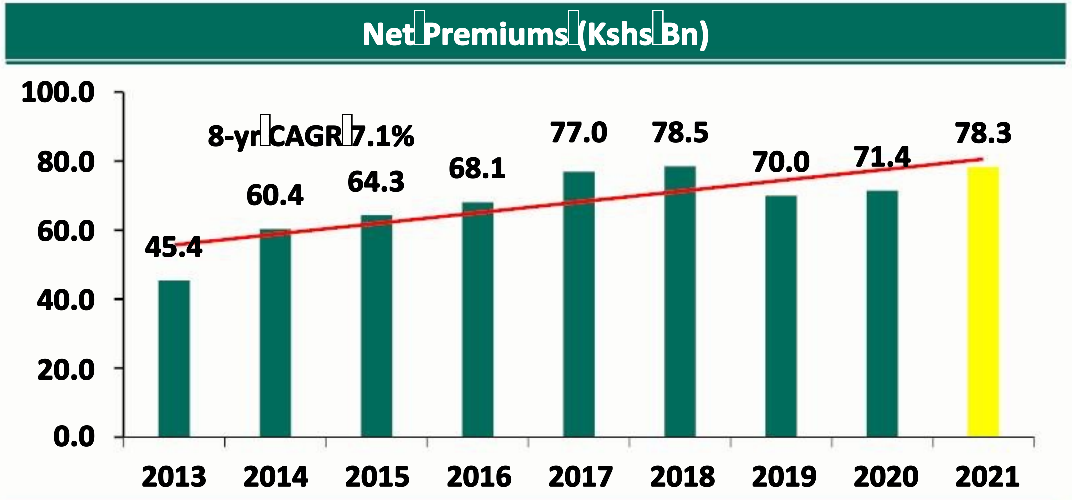
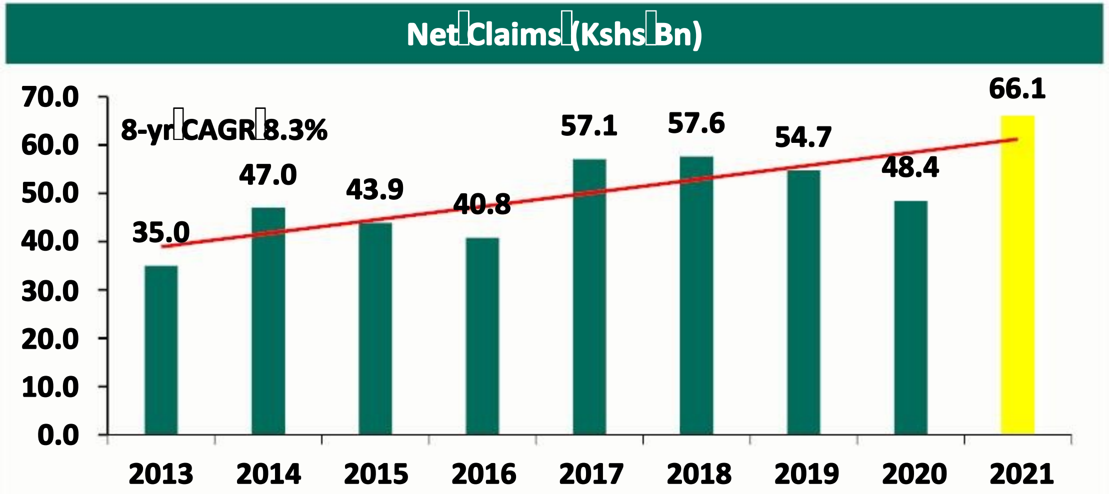
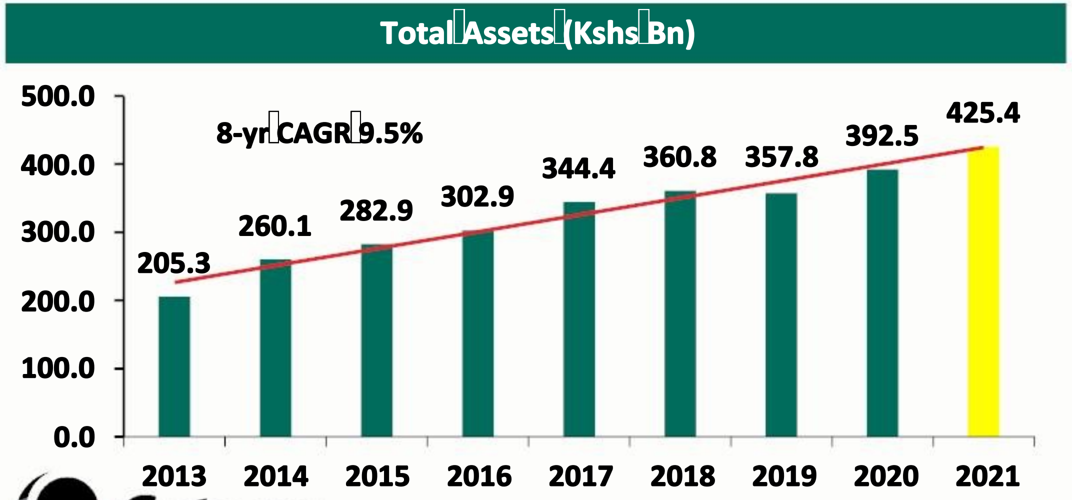
4. Listed Insurance Sector Metrics

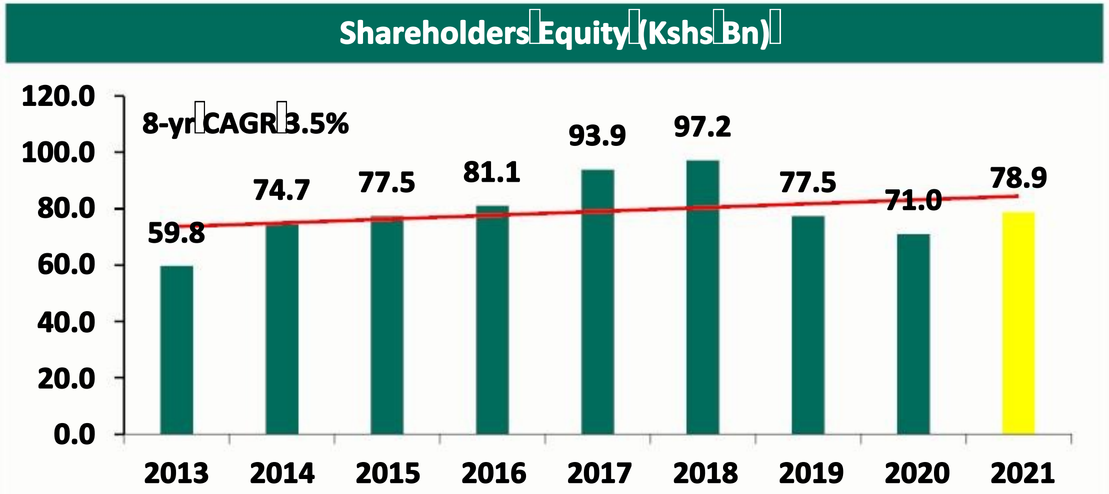
Listed Insurance Sector Metrics

Net premiums, Net Claims, Total Assets and Shareholder Equity have recorded a steady growth over the years









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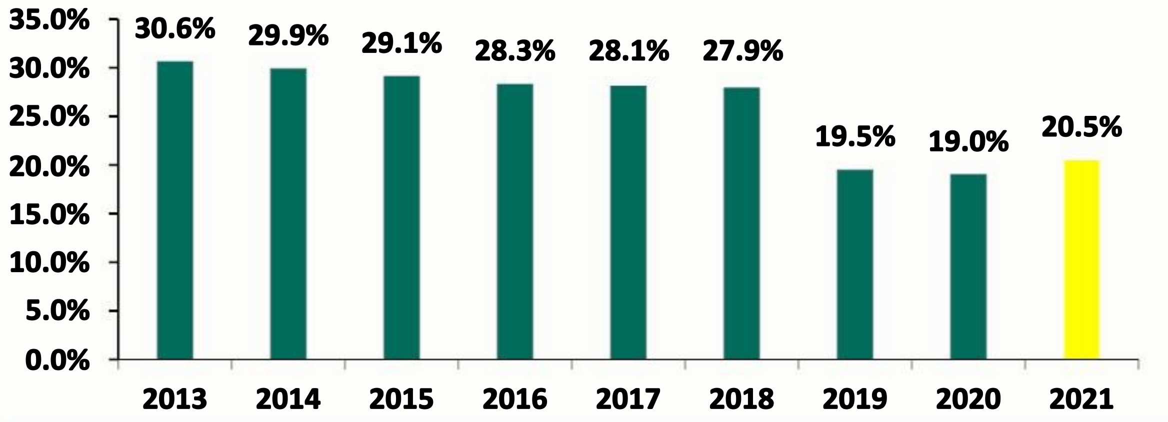
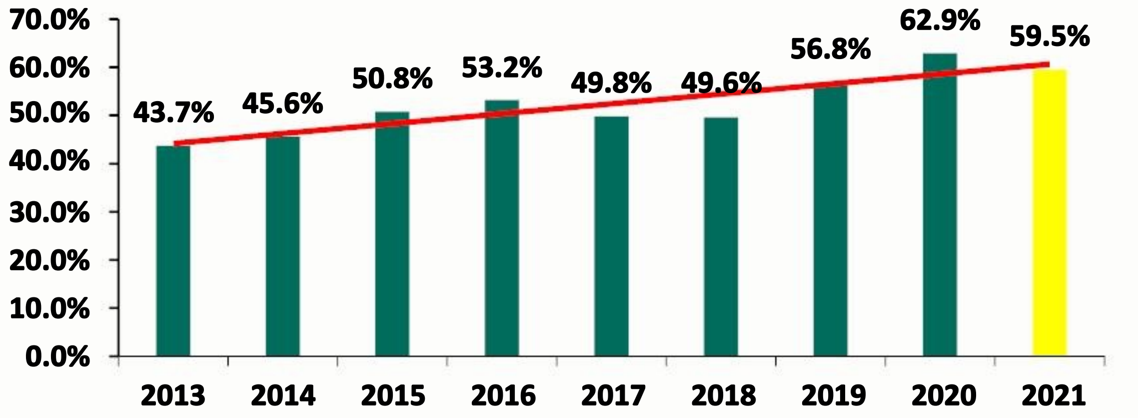
Listed Insurance Sector Metrics

Loss ratio and solvency ratios remain under control

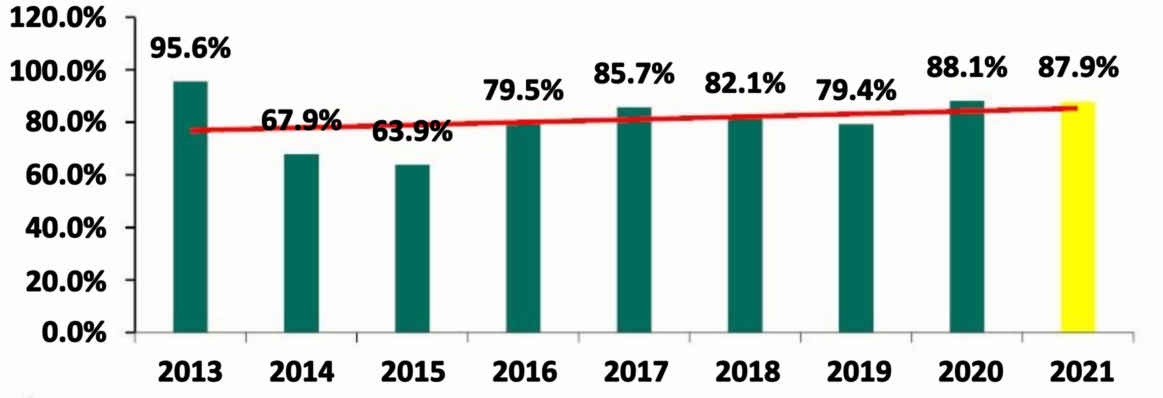
Solvency Ratio



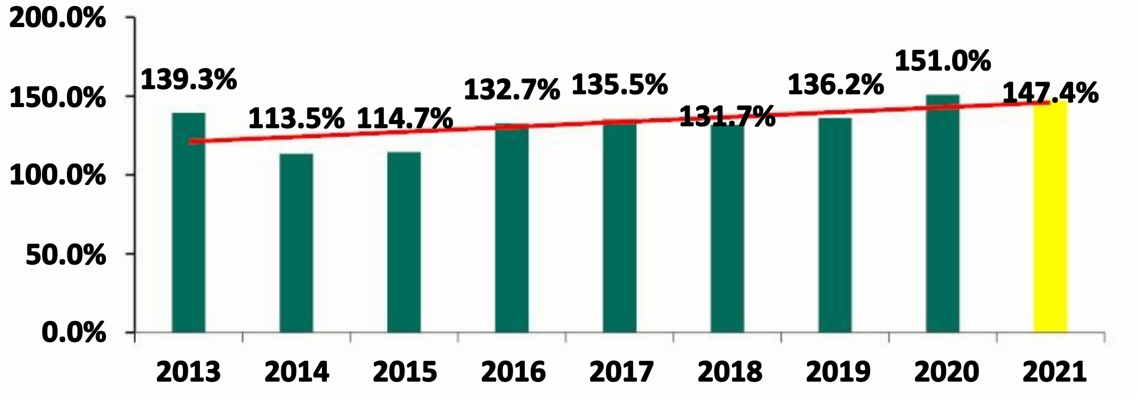
Expense Ratio



Loss Ratio



Combined Ratio



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Listed Insurance Earnings and Growth Metrics

The Loss and Expense ratios declined across the sector

Listed Insurance Companies FY'2020 Earnings and Growth Metrics								
Insurance	Core EPS Growth	Net Premium growth	Claims growth	Loss Ratio	Expense Ratio	Combined Ratio	ROaE	ROaA
CIC	301.3%	5.5%	5.8%	71.6%	52.2%	123.8%	3.4%	1.6%
Britam	100.8%	8.1%	(4.3%)	69.4%	82.1%	151.5%	0.4%	0.05%
Jubilee Insurance	57.0%	9.0%	18.2%	108.4%	41.3%	149.7%	17.6%	4.5%
Sanlam	13.7%	34.8%	50.3%	93.3%	45.7%	139.0%	(46.0%)	(1.7%)
Liberty	(87.9%)	0.6%	42.8%	78.3%	79.3%	157.6%	0.9%	0.2%
***FY'2021 Weighted Average**	**89.2%**	**8.9%**	**11.9%**	**87.9%**	**59.5%**	**147.4%**	**6.0%**	**2.1%**
****FY'2020 Weighted Average**	**(157.9%)**	**1.6%**	**9.5%**	**88.1%**	**62.9%**	**151.1%**	**(9.4%)**	**(1.3%)**

**Market cap weighted as at 03/06/2022*

***Market cap weighted as at 21/05/2021*

Listed Insurance Sector Trading Metrics

Kenya's Insurance sector is trading at an average P/TBV of 0.8x and a P/E of 9.3x

Insurance Company	Share Price*	No of Shares	Market Cap	P/TBV	P/E
Jubilee Holdings	266.00	0.1	19.3	**0.5x**	2.8x
Sanlam Kenya	13.90	0.1	2.0	**3.8x**	12.9x**
Liberty Holdings	5.50	0.5	2.9	**0.4x**	5.4x
Britam Holdings	6.28	2.6	15.8	**1.0x**	18.0x**
CIC Group	2.00	2.5	5.2	**0.8x**	7.8x**
Median				**0.8x**	**7.8x**
Weighted Average FY'2021* **				**0.8x**	**9.3x**

*Share Price as at 3rd June 2022
** 5 year normalized P/E
*** The weighted average is based on Market Cap as at 3rd June 2022

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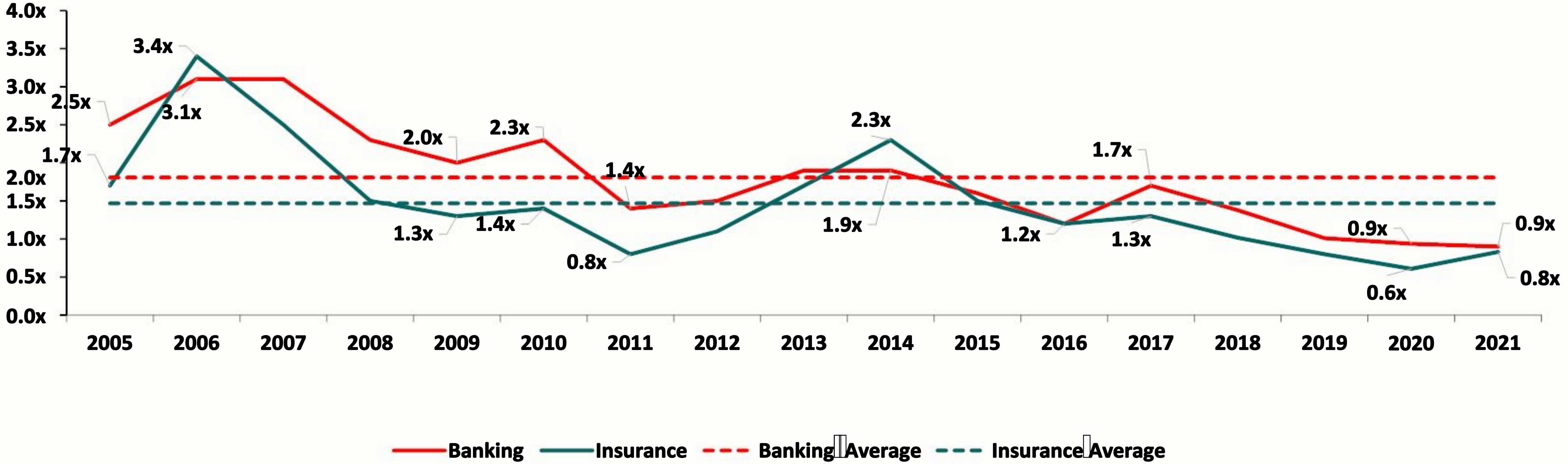
Listed Insurance and Banks Trading Metrics

The listed Insurance sector is trading at an average P/B of 0.8x, lower than the banking sector which is priced at 0.9x. Both sectors are trading below their 16-year averages of 1.5x and 1.8x, respectively

Price to Book Comparison - Listed Banking vs Insurance Sectors



On a price to book valuation, listed Insurance companies are currently priced at a PBV of 0.8x, lower than listed banks 0.9x, with both lower than their historical averages of 1.5x for the insurance sector and 1.8x for the banking sector

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5. Cytonn’s Insurance Sector Report

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Executive Summary

- All listed insurance companies in the Kenyan market were analyzed by the Cytonn Investment Team
- The analysis was brought about by a need to be able to offer our investors, especially global investors, which insurance companies in our view are the most stable from a franchise value and from a future growth opportunity perspective
- The analysis covers the health and future expected performance of the financial institution, by highlighting their performance using metrics to measure Profitability, efficiency, diversification, risk appetite and solvency
- For insurance companies which are part of a group structure, the financials of the group were utilized to take into consideration the listed counter which an investor will purchase
- Ranking based on a weighted average ranking of Franchise value (40.0%) and Intrinsic value (60.0%)
- All the listed insurance companies are composite insurance companies, offering both life and general business

Regulation and Consolidation to Drive Attractiveness

Focus Area	Summary	Effect on Insurance Sector
Regulation	• **Risk Based-Supervision:** The IRA is implementing risk-based supervision which looks at the risk exposure of a company • **IFRS 17**: Effective January 2023 or earlier, changes will encompass separation of financial and insurance results in the income statement	• Regulatory changes are foreseen to impact the sector positively in line with international best practices, thus buoying investor confidence in the capitalization and future position of the Insurance sector • IFRS 17 will affect the volatility of profits, net assets and equity in the Insurance sector
Digital Innovations	• **Digital Innovations:** High mobile phone penetration rates in Kenya have aided in the digitization of distribution channels, shifting focus to the customer. Insurtechs and bancassurance partnerships to continue to disrupt competition in the industry	• Leveraging more on technology will transform how the insurance business is conducted. The use of Blockchain technology, AI and Big Data will also help prevent fraudulent claims by enabling early detection and audit trails
Consolidation	• **Increase in Mergers & Acquisitions:** Most of the smaller players in the insurance industry are lacking adequate capital to finance operations and meet regulatory requirements	• Will be driven by capital adequacy requirements coupled by erosion of capital buffer erosion following the tough pandemic year FY'2020. We expect the more M &A activity as smaller players look to strengthen their capital and market positions
Insurance Fraud	• **Fraudulent claims:** It is estimated that 25.0% of the insurance industry's income fraudulently claimed. In FY'2021, 120 fraud cases were reported to the Insurance Fraud Investigation Unit, with Motor Insurance Claims being the most prevalent	• Fraudulent claims have had the effect of hurting the profitability, translating into high premium rates and huge claim reserve ratios. As a result, verification of claims has resulted in the slowing down of the settlement pace

Regulatory trends in the Insurance sector will very much determine growth and investments prospects. Newer minimum capital requirements are expected to set off mergers and acquisitions in the sector, with many insurers failing to meet the minimum. The regulatory reforms also present an opportunity to international firms to enter into the Kenyan market, given it has strong economic growth prospects

Rankings by Franchise Value

Jubilee Holdings presents the most attractive insurance franchise, with a Score of 14

Insurance Company	Loss Ratio	Expense Ratio	Combined Ratio	ROACE	ROaA	Total	Rank
Jubilee Holdings	5	1	3	1	1	14	1
CIC Group	2	3	1	2	2	19	2
Sanlam Kenya	4	2	2	5	5	22	3
Britam Holdings	1	5	4	3	4	24	4
Liberty Holdings	3	4	5	4	3	26	5

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Valuation Summary of Listed Insurers

Jubilee presents the highest upside with an expected total return of 45.6%

Insurance Company	Current Price	Target Price	Upside/(Downside)	Dividend Yield	Total Potential Return
Jubilee Holdings	266	379.4	42.6%	3.0%	45.6%
Liberty Holdings	5.5	7.84	42.6%	0.0%	42.6%
Britam Holdings	6.28	7.7	22.6%	4.8%	27.4%
Sanlam Kenya	13.9	15.9	14.4%	0.0%	14.4%
CIC Group	2	2.1	5.0%	0.0%	5.0%

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Cytonn Insurance Report – Comprehensive Rankings

Jubilee Holdings emerged top of the rankings, leading in both Franchise & Intrinsic Valuation

CYTONN FY'2021 COMPREHENSIVE RANKINGS TABLE				
Bank	Franchise Value Score	Intrinsic Value Score	Weighted Score	FY'2021 Ranking
Jubilee Holdings	1	1	1	**1**
Liberty Holdings	5	2	3.2	**2**
Britam	4	3	3.4	**3**
Sanlam Kenya	3	4	3.6	**4**
CIC Group	2	5	3.8	**5**

- Jubilee Holdings took the Top Position, ranking top in the franchise score category on the back of a strong combined ratio, indicating better capacity to generate profits from its core business,
- Liberty Holdings took 2nd Position, on the back of a weak franchise score, driven by the highest Combined ratio,
- Britam and Sanlam Kenya came in 3rd and 4th Position, respectively, with weaker franchise scores, as a result of lower returns on assets and equity (Sanlam) and high loss and expense ratios (Britam),
- CIC Group came in 5th Position on the back of weak intrinsic rankings scores

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6. Appendix – Valuation Summaries

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Valuation Summary – Jubilee Holdings

Jubilee Holdings is undervalued with an upside of 42.6%

Valuation Summary:	Implied Price	Weighting	Weighted Value
Residual Income	306.9	40.0%	122.7
Dividend Discount Model	463.7	40.0%	185.5
PBV Multiple	338.7	15.0%	50.8
PE Multiple	292.7	5.0%	14.6
Fair Value			**379.4**
Current Price			**266.0**
Upside/(Downside)			**42.6%**
Dividend Yield			3.0%
Total Upside/(Downside)			**45.6%**

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Valuation Summary – Sanlam Insurance

Sanlam Insurance is Undervalued with an upside of 13.8%

Valuation Summary	Implied Price	Weighting	Weighted Value
Residual Income	18.3	75.0%	13.7
PBV Multiple	7.9	20.0%	1.6
PE Multiple	10.9	5.0%	0.5
Fair Value		**100.0%**	**15.9**
Current Price			**13.9**
Upside/(Downside)			13.8%
Dividend Yield			0.0%
Total Return			**13.8%**

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Valuation Summary – Liberty Holdings

Liberty Holdings is Undervalued with an upside of 42.6%

Valuation Summary:	Implied Price	Weighting	Weighted Value
Residual Income	7.7	40.0%	3.1
Dividend Discount	6.2	40.0%	2.5
PBV Multiple	11.3	15.0%	1.7
PE Multiple	12.2	5.0%	0.6
Fair Value		**100.0%**	**7.8**
Current Price			**5.5**
Upside/(Downside)			42.6%
Dividend Yield			0.0%
Total Return			**42.6%**

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Valuation Summary – Britam Holdings

Britam Holdings is overvalued with a downside of 22.2%

Valuation Methodology	Implied Price	Weighting	Weighted Value
Dividend Discount	8.2	40.0%	3.3
Residual Income	8.8	30.0%	3.5
PBV	5.9	15.0%	0.6
PE	2.8	15.0%	0.3
Fair Value			**7.7**
Current Price			**6.3**
Upside/(Downside)			22.2%
Dividend Yield			4.8%
Total Return			**27.0%**

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Valuation Summary – CIC Group

CIC Group is Overvalued with a downside of 6.6%

Valuation Summary:	Implied Price	Weighting	Weighted Value
Dividend Discount Model	2.4	40.0%	0.9
Residual Income	2.1	40.0%	0.8
PBV Multiple	1.5	15.0%	0.2
PE Multiple	2.4	5.0%	0.1
Fair Value		**100.0%**	**2.1**
Current Price			**2.0**
Upside/(Downside)			6.6%
Dividend Yield			0.0%
Total Return			**6.6%**

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Thank You!

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Q&A / AOB

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