Monthly Market Report

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Region:	Africa ex South Africa
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Market snapshot

Markets (MSCI indices in USD/currencies vs the USD) –

July Performance (%)	LCY	USD
Morocco	2.9	2.5
Tunisia	0.2	1.0
MSCI World	0.4	0.4
Mauritius	1.5	0.0
Zambia	0.1	-0.6
Botswana	-0.9	-1.4
MSCI EM	-1.7	-1.7
BRVM	-0.3	-2.3
Kenya	-0.9	-2.7
Egypt	-5.0	-4.2
Nigeria	-7.5	-8.1
Zimbabwe	-8.6	-8.6

July was a tough month for our key markets Nigeria (-8.1%), Egypt (-4.2%) and Kenya (-2.7%). For Morocco, the positive month was mostly a reversal of the weakness in June, where local investors moved to cash to take advantage of the government sale of 8% of Maroctel at a discounted price of MAD 125. Interestingly, most African currencies weakened marginally vs the USD.

Economic and political overview

Nigeria – The Monetary Policy Committee (MPC) of Nigeria's central bank (CBN) kept its monetary policy rate at 13.5%, giving time to evaluate the impact of its interventions to support lending to priority sectors. The CBN's primary objective is FX and inflation stability. It believes it can achieve secondary objectives such as financial inclusion and economic growth by using customized, interventionary tools. The operative word being "tool", as they sometimes resemble a wrench or even a sledgehammer. The latest attempt is to stipulate a minimum 60% loan-to-deposit ratio (LDR) for deposit money banks (DMB's), forcing banks to lend instead of buying government securities. A monthly review of bank LDR's begins in September, to assess compliance. We do not anticipate a material impact on our bank holdings, GT and IBTC. We also do not anticipate any adverse impact on the local money market, as government issuances are typically oversubscribed, with ample demand from local pensions and a firm foreign bid, even before the Fed cut.

Macro releases included:

- Inflation dropped to 11.2% y/y in June from 11.4% y/y in May.
- The Stanbic IBTC Nigeria PMI increased to 54.8 in June from 52.9 in May. This signals improved business conditions in the Nigerian private sector, with increases in both new orders and output.

Egypt – Egyptian inflation eased unexpectedly to 9.4% y/y in June, its lowest rate in over three years. This indicates a potential resumption of easing monetary policy in the coming months. The deceleration in prices appeared linked to a slowdown in the cost of food and beverages, as well as a high base effect. The Emirates NBD Egypt PMI increased to 49.2 in June from 48.2.

The IMF Executive Board completed the 5th and final review of Egypt's economic reform program. This permits Egyptian authorities to draw the final USD 2bn loan tranche of the USD 12bn loan approved in November 2016. The Board's view was that fiscal reform has progressed and the macroeconomic situation has distinctly improved since 2016.

In an expected and well-communicated move, the government cut fuel subsidies in July, increasing diesel and 80-octane gasoline price by c.23% to EGP 6.75/litre, 92-octane gasoline by c.19% to EGP 8.0/litre and 95-octane gasoline by c.16% to EGP 9.0/litre. This is the last round of subsidy related price hikes.

Kenya – The MPC of the Central Bank of Kenya (CBK) retained its benchmark lending rate at 9.0% for the seventh time in a row. The MPC noted private sector credit growth of 5.2% y/y in June, well below the CBK's target rate of 12-15%.

The Stanbic Bank Kenya PMI rose to 54.3 in June from 51.3 in May. This marks the second straight expansion in private activity and the fastest since August 2018. Employment growth reached a 30-month high. According to the Kenya Social Protection and Job Programmes Public Expenditure Review by the World Bank, Kenya has to create at least 900,000 jobs annually between now and 2025 to absorb the high number of youths joining the job market.

Inflation rose to 6.27% y/y in July, an 8-month high, despite a decrease in the cost of some food products. This was mainly due to higher taxes, fuel increases and high input demand.

Morocco – GDP growth slowed to 2.6% in 2Q19, citing a drop in agricultural activity. Agricultural output (15% of GDP) fell 2.7% in the second quarter after a drop of 3.2% in 1Q19. Lack of rainfall cut cereal production to 6.1m tonnes, down 40.7% from 2018. Non-agricultural growth slowed to 3.4% in 2Q19, down from 3.8% in 1Q19, mainly because of the mining sector.

Morocco's inflation rate eased to 0.2% y/y in June from 0.3%y/y in May, while annual core inflation was unchanged at 1.3%.

Company updates

Nigerian Breweries (Nigeria Breweries, Consumer staples) 1H19 results: A mixed set of numbers from Nigerian Breweries (NB). 1H19 net sales were down 1.4% y/y and 2Q19 down 3.1% y/y, however on a quarterly basis 2Q19 revenues were up 4.37% q/q. On the Heineken parent call, management mentioned that volumes in Nigeria registered mid-single digit growth, with double digit volume growth in premium and mainstream. AbInbev subsidiary International breweries grew volumes double digit over the same period which suggests to us that the market as a whole is back to growth. The numbers are encouraging because there is a growth underpin and now it is about price points shifting up, given the c17% increase in excise duties. GP margins were good at 42.1% which is closer to normalized levels and OPEX grew 6% which is below inflation, this number is likely to be sticky downwards and may even rise higher due to intensive competition and promotional activities. Overall NB registered a 14.1% EBIT margin which is higher than competition but still below 18-20%

levels we would expect. We are encouraged by NBs cost containment initiatives and smart pricing strategy but we feel that the industry will only return to profit once competition raises prices. Overall 1H19 EBITDA was down 14% y/y and EPS down 28% y/y.

Nestlé Nigeria (Nigeria, Consumer staples) 1H19 results update: Decent results from Nestlé Nigeria with topline slightly behind expectations but operating profits in line. Nestlé's 1H19 revenues were up 4.9% y/y, with the beverage segment up 6.9% y/y and the food segment up 3.6%y/y. COGS were down 4.9% y/y, mainly due to lower prices for Cocoa, Sugar and Wheat. Opex however was up 9.5% y/y, in line with the trend we saw in 1Q19. Overall EPS was up 22% y/y (including the impairments in the base for 1H18). Nestlé launched an extension of the Maggi brand (seasoning/bouillon) - Maggi Signature in the South region in 1Q, but this did not translate into growth for the food segment. The overall performance is better than peers and indicative of a difficult macroeconomic environment. We note that receivables continue to grow higher than turnover, which shows a push towards generating sales growth by giving better terms.

East African Breweries Limited (Kenya, Consumer staples) FY19 results: Top line growth in line with expectations but bottom line ahead of expectations. Lapping a weak base, so the y/y numbers look good. Volumes were up 11%, net sales up 12% and operating profits up 40%. There were no major one-off expenses in FY19. There was margin expansion all the way down the income statement. Gross margin expansion +2.1% driven by volumes, price mix and productivity savings (procurement, local sourcing, distribution costs). Operating profit margin expansion +5.1% due to operating efficiencies, excluding the FY18 tax provision, operating margins expanded by +2.4%. The investment in margin accretive brands also started to pay off with strong growth in the spirits category as well as premium and mainstream beer. Balance sheet structure should improve going forward, past the Kisumu capex hump, the EUR loan (EUR 60m) that was used to fund Kisumu to be replaced by a KES loan.

Delta Zimbabwe (Zimbabwe, Consumer Staples) 1Q20 trading update: As we flagged on the last update, the numbers are starting to get meaningless now due to hyperinflation. Demand has dropped following price increases and down trading to subsistence offerings. Delta notes that their product pricing hasn't fully factored in the depreciation of the exchange rate. Management mentioned that the ring-fencing initiatives of the RBZ for legacy liabilities (FX payables) haven't paid off yet, with foreign suppliers cautious about country risk, which compromises supply of imported materials. Lager beer volumes were down 57%, sorghum volumes were up 2% and sparkling beverage volumes declined 79% following an extended shutdown due to a shortage of imported raw materials. Group revenue was up 92%, however the base is USD, when RTGS was 1:1 with the USD. The trading update was in line with expectations, perhaps slightly better than we expected based on our meeting with management in May.

Sonatel (BRVM, Communications services) 1H19 results update: An encouraging performance at the top line level, offset by one-off depreciation charges and higher y/y duties and excises. Revenues came in +7.2%, EBIT -1.0% and PAT -9.9% on higher finance and income tax charges. The higher duties and excises were imposed last year and should lap in 2H, in addition to lapping, effective 1 July 2019, the levy in Senegal is being reduced to 4.5% from 5%. The underlying growth drivers of data and mobile money remain strong. Data revenues +24.9% (subs +14.4% and ARPU +9.2%), with 35.5% of the total subscriber base penetrated. Orange Money revenues +42.5% (subs +21.5% and ARPU +21.0%), with total transaction value +36.4%. Data is now 21.7% of revenues, while Orange Money is 7.5%.

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Equity Bank (Financials, Kenya) 1H19 PBT +10% y/y was in line with our expectations. The main theme was good loan growth +17% y/y and 8% YTD while fee growth underpinned by mobile, merchant acquiring and remittance business lines +13% y/y. Mobile app transactions still growing strong at +24% y/y. Costs were reasonable at +9.5% y/y. Guidance is for credit loan growth to continue as the Kenyan economic rebound is strong and lower Kenyan yields makes lending more attractive. Core focus remains SMEs in FMCG, trading and logistics and large corporate tickets. Asset quality still noticeably high. NPL ratio at 8.9%. However, some large contractor loans are current again but can only be reclassified after a 6 months waiting period. Attractively priced at 1.4x FY19 book and 6.5% dividend yield given 25% ROE achieved at 1H19 stage.

Commercial International Bank (Egypt, Financials) 1H19 PBT +26% y/y. A decent set of results although we were surprised by the overall loan growth at 4% YTD. On our call with management they clarified that loan growth theme is still in place. The 2nd quarter saw some pay down in USD facilities as the EGP strengthened. The USD book (40% of total book) declined by 7%. LCY loans up a solid +13% and LCY deposits +11% YTD. Margins were stable and CoR at 75bps which is very low considering their past aggressive provisioning model.

Market outlook

Nigeria – Results confirm a slow recovery and a path to normalisation of the economy. For the most part, consumer companies are able to shift volume and we expect pricing to improve on the back of consumer income recovery, with the new minimum wage adjustments, we should see this happen in 2H19. We maintain a large allocation to banks and the top consumer names in the food and beverages sector. Valuations are deeply discounted and attractive. Our preferred banks are well positioned to make money from fees. Overall, banks will make less profit from yields as the curve drops, but higher NGN liquidity, strong growth in trade facilities (LCs) and mobile bank fees will still mean good growth in earnings. Since we are past the election hump we hope to see more expansionary monetary policy and credit creation to stimulate growth and spur the economy out of this early recovery phase.

Egypt – The economic recovery is continuing as expected and most management teams are positive and expect conditions to improve further. We see volumes recover as wages catch-up to inflation and this is further supported by corporates restocking as demand picks up. Upside risk to inflation from subsidy removal and rising oil prices, but there is enough positive momentum to maintain the growth trajectory. The earlier than expected 1Q19 cut in rates should further support growth for 2019.

Kenya – The political decision not to remove interest rate caps removes the opportunity for an asymmetric trade on the banking shares and reduces economic momentum. However, low inflation and a multi-year investment in infrastructure have created a platform for strong real GDP growth. On a bottom up basis, we remain very optimistic on the payments and fintech growth theme which we play through telco and banking.

Mauritius – Our investment in Mauritius, MCB, is doing extremely well, with very strong momentum in trade finance. MCB continues to grow earnings above GDP and expand NIMs, increasing the ROE further above the cost of capital and creating scope for further rerating.

Morocco – We continue to search for attractively priced growth investment opportunities with our existing investments showing moderate growth and attractive dividend yields. We recently added Label Vie (supermarket, hypermarket, cash n carry), which we believe is well positioned to benefit from low formalized retail penetration in the country.

Zimbabwe – We have always taken a long term view to Zimbabwe, preferring to look through the political noise and focusing on identifying corporate champions that can generate shareholder wealth no matter the environment. OMIR allows us to get both liquidity and a reasonable valuation as we wait. Key to Zimbabwe's economic recovery is a fresh capital injection and debt forgiveness/restructuring, we believe that announcements signalling progress in this regard will be catalytic for our investments in the country.