Monthly Market Report

Edition:	**March 2020**
Region:	**Africa ex South Africa**
Issued by:	**Imara Asset Management Limited**
Author:	**Craig Bandason, Rainer Orth, Tony Schroenn**

Market snapshot

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

Mar Performance (%)	LCY	USD
Botswana	-1.5	-7.1
BRVM	-8.2	-8.4
Tunisia	-9.6	-10.4
MSCI World	-13.5	-13.5
Kenya	-11.2	-14.6
MSCI EM	-15.6	-15.6
Zambia	-0.4	-16.9
Nigeria	-18.8	-23.2
Morocco	-20.8	-25.1
Egypt	-26.3	-26.8
Mauritius	-27.8	-30.2

COVID-19 dominated the month, the phrases 'social distancing' and 'flattening the curve' becoming a part of everyday speech. Lockdown appears to be working in the developed world, with China, South Korea and Singapore at the forefront. Many countries have introduced stimulus programmes to sustain domestic activity. The Organisation for Economic Co-operation and Development (OECD) has estimated that for every month of containment, there will be a loss of 2ppts in annual GDP. Many economies will likely fall into recession this year.

The disease is still in the early phases in developing countries. However Hubei data indicates that with strong lockdown measures and containment, 12-13 days post-lockdown is the inflection point after which we could see new case numbers start to decline.

Africa's youthful population is advantageous, but the biggest concerns are around healthcare capacity, tight living conditions and large numbers of the population with compromised immune systems. The impact of COVID-19 has been experienced disproportionately by the services sectors such as tourism and hospitality, but the overall impact on Africa is difficult to estimate.

Economic and political overview

Nigeria – The combination of exogenous shocks is likely to hit Nigeria's ailing economy the hardest. President Buhari signed the budget in December which pegged oil production at 2.18m bpd and price benchmark of USD 57pb.This benchmark has since been adjusted to USD 30pb. The oil price, coupled with weak FX reserves (USD 36.3bn end-Feb), has put pressure on the central bank's ability to maintain the currency. On the back of this, the naira was adjusted to NGN 380 per dollar, from NGN 365 per dollar – a 4% depreciation. We see this is a positive signal, as the Central Bank of Nigeria (CBN) has been largely reluctant to adjust the currency previously. The parallel market is currently trading at NGN 420 per dollar. In another signal that we are gearing up for devaluation, banks have started curbing daily withdrawal limits abroad.

Stanbic IBTC limits withdrawals to USD 300 per day. GTB and Zenith Bank also re-setting to similar levels. We provide a more detailed analysis of how a devaluation will affect our Nigeria banks position as an addendum.

The Federal Government has declared that NGN 120bn (USD 330m) is needed to fight coronavirus, urging the private sector to make voluntary donations. The government's stimulus package stands at NGN 50bn (USD 136m) with specifics including: NGN 1bn bailout (USD 2.72m) for pharma companies, NGN 10bn (USD 27.2m) to Lagos State and USD 18.2m to strengthen the National Centre for Disease Control. The Central Bank of Nigeria's (CBN) MPC kept the policy rate unchanged at 13.5%. In addition the CBN reduced interest rates on all its intervention funds from 9% to 5% p.a.; proposed regulatory leniency for banks, aims to strengthen its Loan to Deposit Ratio (LDR) policy; provide credit to healthcare and manufacturing sectors as well as accommodate a 1-year moratorium for all CBN's facilities. Standard & Poor's (S&P) downgraded Nigeria's 2020 outlook from stable to negative, but maintained its 'B' rating. Given the immense pressure on the already frail economy, we expect Nigeria to enter into recession in 2020.

Nigeria's coronavirus cases are relatively low, officially reported as 214. However on the ground, speculation is that the number is much higher owing to insufficient testing and mistrust of the government's reporting mechanism. Civil servants have been ordered to work from home indefinitely, affecting as much as 70% of Lagos's labour force. Movement has been banned between Abuja and Lagos in order to curb the spread. The electricity price increase scheduled for 1 April was suspended, and petrol prices have been reduced.

Macro releases included (February stats):

- Inflation came in flat at 12.2% y/y (Jan: 12.13%).
- FX reserves were at USD 36.3bn and have since continued to fall, reaching USD 35.16bn as at 1 April.
- PMI fell slightly to 55 (Jan 55.9) owing to weaker expansion in private sector activity.
- 4Q19 balance of payments data showed the largest current account deficit on record, -5.4% of GDP (3Q19: -2.2% of GDP). This was due to high machine imports related to the Dangote refinery and high service imports.

Egypt – The Central Bank of Egypt's (CBE) Monetary Policy Committee (MPC) surprised with a rate cut of 300bps in an emergency meeting in March, in order to support the economy. This brings the lending rate to 10.25%. The CBE will plug EGP 20bn (USD 1.27bn) into the stock market, following funds pledged by Banque Misr and National Bank of Egypt of EGP 3bn (USD 190m). The stimulus package has been expanded to include agriculture companies who can access finance through soft loans.

Coronavirus has affected daily life, with flights suspended and the tourism sector effectively crippled by containment measures. The government has declared a 2 week curfew for workers. Schools and universities are closed into mid-April while clubs and gyms will be shut for 2 weeks. All large public gatherings have been suspended, and daily cash withdrawals limits temporarily instituted. The Health Ministry has confirmed 1,070 cases as at 5 April, and 71 deaths. The government trimmed the growth forecast to best case c.5 % and worst case c.3.3% for FY20/21, down from 6%.

Macro releases included (February stats):

- Inflation slowed to 5.32% y/y, driven by a 0.9% drop in food prices (Jan: 7.17%).

- FX reserves crept up to USD 45.51bn (Jan: USD 45.46bn).
- PMI came in at 47.1 (Jan: 46.0).
- Tourist arrivals increased +4% y/y, and the first week of March saw 210,000 visitors. This is within the normal range, and a decline is inevitable.
- Remittances rose by 5.1% y/y, up to USD 26.8bn.

Kenya – Kenya has proactively restricted travel, closed schools indefinitely and encouraged work from home as coronavirus case numbers hit 126. The IMF has pledged KES 122bn (USD 1.16bn), to support the health sector which is increasing capacity to limit the virus spread. To protect jobs, the President orchestrated an increase in disposable incomes by: PAYE reduction of 5%, income tax down by 5%, reduction of turnover tax rate from 3% to 1% for SMEs, appropriation of money to elderly, orphans and other vulnerable people, and temporary suspension of loans. A 1-year moratorium is available to borrowers and restructuring for corporates and SME's at no cost. VAT has been decreased from 16% to 14%. The tax relief will be in place until August. In addition to this, salary reductions have been declared for all government executives. Daily curfews have been introduced and state and public officers instructed to work from home. All charges for transfer between bank accounts and mobile money has been eliminated. Kenya benefits from the low oil price as an importer, but this is offset by the significant impact on tourism and horticulture exports due to coronavirus restrictions.

FX reserves dropped to USD 7.965bn on 29 March - only enough to cover the country's imports for 4.84 months. This is the lowest import cover since the December 2017 election period. The Central Bank of Kenya (CBK) announced that it will buy USD 100m per month to boost reserves between March and June, as well as min USD 1m from banks. The CBK's MPC announced a rate cut of 100bps to 7.25% on 23 March. Additionally the MPC reduced the cash reserve ratio (CRR) by 100bps to 4.25%. GDP growth forecasts by the CBK have been lowered to 3.4% from 6.2%.

Safaricom entered partnerships with the public sector, allowing commuters to pay bus fare via M-Pesa to reduce cash usage. In addition, Safaricom have waived transaction fees of under KES 1,000 (USD 9.5) for 90 days.

Macro releases included (February stats):

- Inflation crept up to 6.4% y/y (Jan 5.8%) due to food increases +10.6% y/y. Inflation for March was just released at 6.06%y/y. However the Kenya National Bureau of Statistics (KNBS) has reconfigured the CPI basket, so it is not a like-for-like comparison with February.
- PMI came in at 49.0 (Jan: 49.7), the second month of decline in the private sector.
- Remittances grew by 9.96% y/y (Jan: 5.95%) to USD 218.9m.

Morocco – GDP was 2.1% in 4Q19 (3Q19: revised to 2.2%). This is the slowest expansion since 2016, as agricultural activity declined as a result of the drought (-5.3%). Coupled with this, the non-agricultural sector slowed down at 3% compared to 3.3% in 3Q19. Growth was noted in construction (+1.3%), transport (3.2%), telecoms (+1.9%), public administration (+4.4%) and education, health and social care (+1.6%).

The Board of Morocco's central bank, Bank Al Maghrib, cut rates by 25bps to 2.00%. Reasons given include higher inflation expected in 2020, stable GDP growth and a slowdown in non-agricultural GDP growth due to COVID-19.

In the wake of the outbreak, Morocco's King Mohammed VI arranged the *creation of a fund (MAD 10bn/USD 1bn) to upgrade health infrastructure and assist vulnerable sectors of the economy. As of 31 March the Fund stood at MAD 36bn or USD 3.5bn owing to generous donations from individuals and companies! This is important as it highlights a trust surplus, as opposed to the massive trust deficit that exists in most countries.* Sectors such as tourism will benefit, assisting with job retention. Morocco currently has 919 cases, and has closed schools, suspended travel and cancelled all events. New measures have been introduced for corporates and households to access bank credit. Banks can increase their refinancing capacity with the central bank, and receive assistance in terms of liquidity, capital and loan provisioning. The measures proposed include 1) offering banks recourse to all refinancing instruments available in both local and foreign currency, 2) an extension to a range of securities and bills accepted by the central bank in return for refinancing granted to banks 3) extension of refinancing duration. A refinancing programme is being fortified for SMEs to allow for access to working capital and investment loans. The Head of Planning announced that GDP for 2020 will miss its 3.7% projection by up to one-third due to drought and the virus outbreak.

A wider floating band has been approved for the dirham, expanding to 5% on either of a reference price up from 2.5% previously. This is part of the currency reform process which should strengthen Morocco's capacity to absorb external shocks and increase competitiveness.

Other macro releases included (February stats):

- Inflation decreased to 1.1% y/y (Jan: 1.3%) with food and non-alcoholic beverages the primary driver.
- Banking industry stats show growth of 5.1% y/y, consistent with the previous months on the back of increased real estate and consumer loans.

Company updates

CIB (Egypt, Financials) Call with management following COVID-19: Seen a large slowdown in activity with the curfew from 7pm to 6am. Opening shifted to 9am from 8am and weekend shopping closed. Branches limited to 2 clients per employee and queue controlled with 2m distance. Risk of lockdown but for now curfew. CIB has a 50% work from home policy, especially for immune suppressed employees. Guidance: Slower loans at 25% guidance as most capex cancelled for now. Working capital has some disruptions and also slower. Strategy becomes a sovereign play with focus on bond and bill investing. NIM will be stable despite 300bps rate cuts. NIM moving parts: sovereign paper (55% of assets): bonds flat and bills lower by 100bps. Loans (30% of assets) lower by 300bps. So overall asset yields down by 120-150bps compared to funding which is down by about 150bps. Doing a lot of credit quality work monitoring clients. Good news it's 80% corporate and 65% multinationals. Still expect to provide aggressively as we have seen from previous experience. 1q20 results will show a healthy y/y operating increase but will report flat earnings. Any growth will be taken as provisions.

Equity Bank (Kenya, Financials) FY19 PBT +14% y/y was a solid set of numbers and in line with our expectations. We are happy to report that their interest in the Atlas Mara acquisition has waned with talks breaking down. We believe it's the renewed attraction of Kenya post caps. The COVID crisis was in full swing when management reported which gives some believability to guidance - likely to be another year of stable earnings of 10-15% at 22% ROE. Management has allowed for some softness in the macro, some NPL build-up and cost of risk up to 1.8% of their loan book which we think is suitably conservative. A key feature, post rate caps, is a reluctance to push rates up too quickly, hence a modest assumption for higher margins of c.50bps. It does point to some focus on higher margin loans as T-bills have declined substantially. Overall, we think fintech and mobile money themes are well placed during this time of public health concerns.

Label Vie (Morocco, Consumer staples) - FY19 results and outlook from management call on 3 April. A very strong year, particularly on the volume front, driven by Atacadao wholesale format. Revenues +15% (LFL 9%), GP +11% on lower mgn Wholesale, EBITDA +12% on economies of scale and PAT +10%, negatively impacted by the higher social tax charge. Revenue progression in each division was Atacadao 22% (LFL 22%), Supermarket 12% (LFL 2%) and hypermarket 8% (LFL 2%). Encouragingly, the working capital cycle was edged into negative territory, where it should be and where management feels it will continue to go.

In terms of 2020, COVID-19 and outlook - First quarter sales have surged to record highs, as shoppers across all formats prepared for isolation and lockdown. This was despite the collapse in purchases from HORECA (20% of sales), which has nearly collapsed from tourism and entertainment industry troubles. A couple of interesting points:

- In the period ahead of lockdown, traffic surged by as much as 300% across all platforms. The informal stores are struggling with their own supply chains and a number are sourcing from Atacadao.
- Many first time customers into formalized retail, as the orderliness, cleanliness and choice is superior to the informal markets. They believe the cheaper prices will be noticed by first timers, creating new future customers and accelerating formalized retail.
- Govt and Label Vie have been encouraging card or mobile payment where possible. A number of informal stores don't have PoS.
- Subsequent to the lockdown, they have seen fewer, but much larger baskets of goods being purchased by customers. Frequent movement is restricted, so when a customer gets a chance to go to a store, they fill a trolley, not a basket.
- Label Vie's entire business chain has been classified as Essential Services by the Authorities, so no disruptions in supply and sales chain.
- Carry 2.5 months of inventory on average.
- Imported products only make up 7% of inventory, each of which have a local cheaper alternative.
- Are using Jumia amongst others to deliver.
- Believe rent reductions will be double edged sword i.e. lower for them but also for Aradei their 58% owned property co.
- Donated MAD 50m (c10% of PBT) to the Moroccan COVID Fund, which interestingly now stands at MAD 36bn or USD 3.5bn from individuals and companies!
- In terms of outlook and disposable income, it is hard to predict given job/income losses. Believe the govt is being proactive and will support consumers' basic needs.

Fawry (Egypt, IT) FY19 results: Strong results, with topline growth +45% y/y aligned with expectations. ADP constituted the majority of revenues at 81.7%, while the largest growth was in banking services +176% y/y. This was driven by accelerated growth in merchant acceptance, reaching 7.6% of revenues. Active customers grew +25% y/y to 25m in FY19, with the number of point of sale (POS) devices increasing to 141 000 in FY19, +35% growth. This came on the back of a partnership with the Cairo Governorate as a means of driving financial inclusion. This initiative will likely speed up in the midst of COVID-19 with focus on establishing a cashless economy. Gross margin expanded by 707bps to 51.9% from 2018. Good opex management led to EBIT growth of +177.1% y/y. PAT +81.7% lagged EBIT growth due to share of associate losses and interest costs. Fawry has entered an agreement with the National Bank of Egypt to distribute 43 000 POS devices in various retail outlets, effectively increasing Egypt's POS capacity by over 54%. In terms of COVID-19, Fawry indicated that they can continue with business as usual to the end of 2020. They have adequate cash reserves, POS inventory for merchant growth and sufficiently established remote work for employees. Management expects to see lower volumes as a result of the slowdown, although the majority of its retail channels and services will still be open should the lockdown continue.

EIPICO (Egypt, Healthcare) Call with management following COVID-19: Management indicated that the Jan/Feb numbers will show a 10% drop in volumes due to a base effect, and COGS will decline. Minimal impact on inventory is expected for now, with 3-4 months available. They have 6 months of stock of pharmaceutical hormones. Active pharmaceutical ingredients (API) were sourced by air, with most countries still allowing cargo plane transportation. 35% of API come from India, 35% from China and 30% from Europe. Management cited that they have other approved sources for API outside of these markets. The government issued a regulation citing that local companies must prioritise local demand. This has a direct impact on exports which make up 20% of sales and 50% of profit. However only 12 of 200 APIs have been prohibited to focus on meeting local demand as per the decree. 70-80% of revenues are related to chronic diseases and this is likely to remain stable.

HPS (Morocco, IT) FY19 results and Outlook. Revenues grew by 8.6%, EBIT by 14.4% and EPS by 1.7%, as the results were impacted by a number of one-offs, in particular higher taxes in Morocco from the Social solidarity surcharge. The results are solid, but not spectacular as 2019 was a year of investment in and development of new products and regions, with the rewards only coming in late 2019 and 2020. Solutions (74% of revs) grew 13%, encouragingly upselling revenues grew by 54%. Processing (10% of revs) grew by 22% as switching revenues and take up of the SaaS model by new clients accelerated. The above two divisions make up the core payment services offering. The Services division saw revenues contract 13%.

In terms of outlook management are extremely positive as they believe the trend of cash to non-cash will be boosted by COVID-19 and that they are and will continue to see increased demand from not only banks, but a number of players in the financial sector. To put some substance to the narrative:

- **Solutions –** signed contracts with a global Top10 Bank, Saudi Payments company, clients in Singapore, Hong Kong, Sri Lanka and the Phillipines.
- **Processing –** signed contracts with the users of the Mobile Switch in Morocco, including the major banks and telcos. They also signed new contracts in Saas mode as well as successfully deploying SaaS mode for SocGen in Africa. Sold their Microfinance solution to Alafia, an African consortium of 44 micro finance companies. Last but not least, they are seeing increased activity over their Moroccan Switch, as COVID is driving increased use on non-cash payment.

- **Services –** believe 2019 poor performance was a one-off and that expired contracts have been signed for longer periods, ceilings removed, new contracts signed.

Market outlook

We will be updating this on a case by case basis as the full impact of COVID-19 becomes clearer. Our overall view is that the portfolio is mostly allocated to "essential service" businesses focused on food production and retail, communications, data and fintech which should be better positioned to absorb an economic shock and slowdown.

IMARA
Asset Management

Understanding the USD hedge – Nigeria banks position March 2020

When African currencies come under pressure, the immediate question that comes up in the banks sector is: "What is the USD net open position (NOP)".Similar to an individual that use hard currency cash to hedge his/her wealth position African banks hedge their balance sheets using USD NOPs. Of course it is not always the highest margin opportunity during "normal times" and most banks especially Tier2 banks never build up the requisite resources to even attempt it. Fortunately, there are a select few Tier1 banks that follow this route and offer protection and often opportunity during a devaluation episode. We have always made this a prerequisite for investment selection.

Now that the Brent futures contract is trading at USD 35 / bbl and the CBN needs USD 45 - 55 / bbl to defend the current level, it timeous to reflect on our Nigerian banks position USD hedge position. Parallel rates are gapping out, already indicating 14% devaluation (3 April: 420 / USD midrate, Abokifx.com). Guaranty Trust Bank (GTB) and Stanbic IBTC (SIBTC) are our two positions and based on FY19 numbers they are very well positioned for a NGN devaluation. Also, it is likely they increased their USD NOP from March 7 when Saudi and Russia decided to discount the oil market. Based on FY19 numbers:

- GTB's NOP was USD 1.4bn which is 83% of NAV
- SIBTC NOP was USD 336m which is 41% of NAV
- 75-80% of both NOP positions is pure USD cash, not asset based

So what will happen when the NGN devalues by 30% to 465 / USD ?

1. USD NOP is revalued in NGN P&L.
    - GTB +24% uplift and
    - SIBTC +12%
2. This is great for the regulatory CAR, so no need to source funding. A higher NGN NAV means capital adequacy ratio (CAR) improve – something that is not true of peers who have neutral or negative USD NOP
3. The USD NIM (typically 4-5% margin and 40% of the book) boost overall Group NIM
4. A secondary driver is a rise in local T-bills which further boost NIM and earnings
5. The positive factors tend to outweigh the negatives of higher loan provisions

The trading opportunity

As concerns and inevitability of a NGN devaluation builds, desperation to reduce NGN and equity exposure leads to price declines as we have already seen and likely to still continue. Valuation becomes dislocated as market participants are unable to see through the crisis.

In our models below, we project future exit multiples on newly devalued NGN book values. Past experience is no guarantee of future performance, but from our experience we expect a return post-devaluation to a 1.5 – 2.5x book multiple range.

What is the USD return?

At 1.5x and full devaluation impact to 465/USD:

- GTB +87%
- SIBTC +79%

At 2x exit:

- GTB +150%
- SIBTC +139%

What about the oil price?

We assumed a stressed loan book in FY20 as GTB and SIBTC tend to provision well ahead of time and write-back over-provisioning at a later stage. GTB has noted a sizable exposure that its upstream oil book production is hedged at 24 months, so we should see no actual cash flow deterioration for now but still apply a higher cost of risk for FY20 as the outlook has deteriorated per IFRS9. Clearly, continued oil prices below USD 25/ bbl is not a good thing and should the market remain depressed beyond 2021, GTB will move to a higher level of impairment and credit losses. Higher NIMs and trading profits in the meantime should offset this and we do not expect ROE to drop below 20%.

Guaranty Trust Bank			
17.9	current NGN price		implied USD price
360	old FX		0.050
465	new FX		0.038
Pre-deval position (FY19 actual)	NGN m	per share	current multiple
Net open FCY position	505 000	17.41	1.03
NOP in USD	1 403		
NOP cash	371 000	12.79	1.40
NOP cash in USD	1 031		
NAV	605 000	20.86	0.86
NAV USD	1 681		
% of NAV in USD NOP	83%		
Post-deval impact			
Net open position	652 292	22.49	0.80
Revaluation uplift	147 292	5.08	
NAV + uplift	752 292	25.94	0.69
% chng	24.3%		
NAV + uplift USD	1 618		
% chng	-3.7%		
FY20 Earnings forecast (stressed)			
PAT pre uplift, 5% CoR	142 000		
Dividend	56 800		
FY20 Retained NAV	85 200		
FY20 NAV	**837 492**	**28.88**	**0.62**
Target pricing			
Book multiple	**NGN price**	**USD price**	**upside %**
1	29	0.062	25%
1.5	43	0.093	87%
2.0	58	0.124	150%
2.5	72	0.155	212%

Stanbic IBTC			
24.0	current NGN price		implied USD price
360	old FX		0.067
465	new FX		0.052
Pre-deval position (FY19 actual)	NGN m	per share	current multiple
Net open FCY position	121 000	12.10	1.98
NOP in USD	336		
NOP cash	91 000	9.10	2.64
NOP cash in USD	253		
NAV	296 000	29.60	0.81
NAV USD	822		
% of NAV in USD NOP	41%		
Post-deval impact			
Net open position	156 292	15.63	1.54
Revaluation uplift	35 292	3.53	
NAV + uplift	331 292	33.13	0.72
% chng	11.9%		
NAV + uplift USD	712		
% chng	-13.4%		
FY20 Earnings forecast (stressed)			
PAT pre uplift, 5% CoR	64 000		
Dividend	25 600		
FY20 Retained NAV	38 400		
FY20 NAV	**369 692**	**36.97**	**0.65**
	Target pricing		
Book multiple	**NGN price**	**USD price**	**upside %**
1	37	0.080	19%
1.5	55	0.119	79%
2.0	74	0.159	139%
2.5	92	0.199	198%