IMARA Asset Management

Monthly Market Report

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Africa Fintech Overview

It would be remiss to open without a note on the strong relative performance in January, where we were down only one percent in a month that turned into a bloodbath. The Nasdaq was down 9% and the ARK Fintech ETF (comprised of a number of high profile global players) was down 20%. We attribute this to our well funded, highly profitable yet also high growth positions, which make up the majority of the portfolio.

Recent news and deal flow – ***Follow the smart money, it's going to Africa!*** As the age old investment mantra goes, follow the smart guys in the room. Well those are the VC guys and guess where they are headed, Africa and particular Fintech. What is most eye-catching are the names, Sequoia, Andreessen Horowitz, Google, Lux just to name a few. Those firms are all staffed and backed by incredibly smart people, with stellar track records. What is particularly encouraging, is that funding is ramping up, despite Omicron and then the Fed. 2021 VC funding in Africa was up on 2020 and January 2022 is up significantly on January 2021.

Company Results and Operating Statistics

The only release so far is **MTN Nigeria** 2021 results, where the main highlight was Fintech revenues growing by 57% for the full year, but 63% in the fourth quarter, showing a nice acceleration. With the award of the PSB license, 9m customers and 700k agents, we are only entering the first innings of a very long game for this company. We detail the results in the company section below.

Staying with MTN, the parent, **MTN Group**, they received a material improvement in their ESG rating by FTSE Russell, allowing the group to be included in the FTSE/JSE Responsible Investment (RI) Top 30 Index (a ZAR denominated equally-weighted index). The FTSE Russell gives company-specific ESG ratings and investigates detailed data analytics regarding a company's exposure to ESG issues in multiple dimensions. The ratings incorporate over 7200 companies covering 47 Developed and Emerging markets with an emphasis on materiality. MTN's overall ESG rating is now 4.3 out of 5 as of December 2021 (Prev: 2.9), a significant uplift for the Group from the 34th percentile to the 97th.

Economic and political overview

Nigeria – The World Bank projects 2.5% economic growth in 2022, and 2.8% in 2023. The IMF retained its GDP projection at 2.7% for 2022 while raising 2023 to 2.7% (Prev: 2.6%).

The government delayed a plan to end fuel subsidies for 18 months, citing the economic impact on households. Moody's retained its B2 rating upgrading its outlook to stable from negative due to higher oil prices but criticised the delay in subsidy reform as fiscally harmful.

The government has placed the telecoms sector on the priority list for FX access in order to accelerate deployment of 5G. This should allow telcos to fulfil international obligations and invest in infrastructure. Nigeria needs c.USD 500m and 6,000 base stations to roll out 5G in 10 cities.

Macro releases (December stats):

- Inflation showed a slight uptick to 15.6% y/y (Nov: 15.4%).
- FX reserves declined marginally to USD 40.52bn (Nov: USD 41.2bn).
- PMI was 56.4 (Nov: 55.0).
- M3 growth slowed to 13.8% y/y (Nov: 15.2%).
- Private sector credit growth was 18.5% y/y (Nov: 20.1%).
- Active mobile lines reached 195m, implying a 98% penetration rate, while internet subscriptions hit 142m with a 71% penetration rate (population estimate of 200m).

Egypt – The Ministry of Planning is anticipating 6% GDP growth for the fiscal year ending June 2022. The IMF raised its 2022 GDP number to 5.6% (Prev: 5.2%). The World Bank also raised its forecast to 5.5% (Prev: 5.0%).

Legislation drafted by the Financial Regulatory Authority (FRA) to regulate the fintech industry received approval in parliament. It outlines the issuing of licences, approvals, services and tech-enabled consumer finance. To apply for a fintech licence, businesses must submit a request form, proof of capital and proof of onboarding an auditor. Start-ups can also apply for short-term licences for 2 years, renewable subject to specified conditions. Additionally, the FRA is under a mandate to expand banking and non-banking financial services.

Mobile wallets grew +27% y/y to 25m in 2021. Mobile wallet transactions doubled to 227m in 2021, with throughput up +160% y/y. Banks will be allowed to launch digital loans via mobile wallets late 2022, according to the CBE.

Macro releases included (December stats):

- Inflation rose to 5.9% y/y (Nov: 5.6%).
- FX reserves remained flat at USD 40.94bn
- PMI was 49.0 (Nov: 48.7), falling to 47.9 in January.
- M2 growth was 18.3% y/y (Nov: 18.5%).
- Egypt has reached a 40% adult vaccination rate - 23.6m having received both doses.
- Non-oil exports rebounded +26% y/y, hitting USD 32bn in 2021.
- Tourism revenues surged in the first quarter of the current fiscal year (3q21) by 253.3%; while tourist receipts returned to pre-pandemic levels of USD 13bn in 2021.
- AstraZeneca's Evusheld, as well as locally-produced Molnupiravir have been approved by the Egyptian Drug Authority for COVID-19 as emergency use. COVI-VAX, also locally manufactured, should be ready for assessment by early 3q22.

Kenya – GDP grew +9.9% y/y in 3q21 (2q21: +10.1% and 3q20: -2.1%). The expansion was driven by a rebound in services, specifically transport and education, as well as manufacturing. Agriculture declined by -1.8% y/y (3q20: +4.2%). The Central Bank of Kenya (CBK) sees GDP growth of 5.9% y/y in 2022.

Cash managed by mobile money agents grew +36% y/y to KES 6.2trn (USD 54.6bn) in the 9m to end-November. While registered mobile money accounts reached 67.2m, up from 65.8m a year earlier. Active agents grew to 299,053, up 8.4% y/y.

Macro releases (December stats):

- Inflation slowed to 5.7% y/y (Nov: 5.8%) and came in at 5.4% y/y in January.
- FX reserves were USD 8.82bn (Nov: USD 8.74bn).
- PMI rose to 53.7 (Nov: 53.0). Since then, PMI slid to 47.6 in January as Omicron cases surged and new orders declined.
- Remittances reached USD 350.6m, a growth of +17.0% y/y (Nov: +24.2%). This brings total remittances to USD 3.75bn for 2021, up +21.3% y/y (2020: USD 3.1bn, +10.7%).
- Tourism arrivals grew +53.3% y/y in 2021 to 870 465, and earnings rose by +65.4% y/y, as the sector recovers.

Morocco – 3q21 GDP came in at 10.9% y/y (2q21: 15.2%). The non-agricultural sector boosted growth at a strong +17.7% y/y, while agricultural growth was +6.4% y/y.

Ratings Agency Fitch revised Morocco's forecast to 3.2% (Prev: 3.4%) due to the impact of Omicron on tourism and movement. The country's measures are among the strictest in the MENA region. As such, the government has approved a MAD 2bn (USD 212m) emergency plan to support the tourism sector. The World Bank expects GDP of 3.2% y/y. The Moroccan government anticipates growth of +2.9% in 2022.

The banking industry grew +3.0% y/y in December, driven by +10.3% y/y growth in debtor accounts and overdrafts and +2.7% y/y increase in real estate loans. Mortgages expanded by +4.9% while real estate loans declined -7.0%. NPLs were MAD 83.5bn (USD 8.9bn), up +4.0% y/y.

Macro releases included (December stats):

- Inflation grew to 3.2% y/y (Nov: 2.6%).
- FX reserves were USD 35.65bn (Nov: USD 34.9bn).
- Tourist numbers via air travel were up +38.9% y/y reaching over 9.9m in 2021.
- Remittances for 2021 grew by +36.8% y/y to MAD 93.3bn.

Company updates

Obour Land (Egypt, Consumer staples) FY21 results update: A very solid set of results in the face of rising soft commodity prices. Revenues came in +10%, however rising input costs saw GP only rising 6%. A concerted cost-cutting effort saw EBITDA slightly better at +8% and surging FCF, allowed interest expenses to fall, yielding a 13% growth in EPS. The dividend was raised from EGP 0.6 per share to EGP 0.65 per share, implying a 10.5% yield. A closer inspection of the P&L and cash flow statement, show there were quite a few moving parts this year and that management has done exceptionally well to produce these results. Firstly, savvy buying has allowed them to flatten the curve below, thereby mitigating the impact on their customers as well as gross margins. Secondly, the investments in new production lines have allowed them to mostly offset raw materials price increases with packaging efficiencies. Management gave a breakdown of COGS and it is interesting to see that in 2018, raw materials were 75% of COGS but are now 79%, yet packaging was 19% and is now 15%. These benefits are not available to competition, so enable Obour to lead the market on pricing and margin management. On the overheads side, a ratio we track is CTI or cost to income, measured by taking opex as a percentage of Gross Profit i.e. showing what portion of GP you give away to overheads. Obour has reduced this from high 30's to low 30's over the last five years. Looking forward, challenges clearly remain, but the company is in a very strong position, particularly as it is now net cash, with the bulk of its capex in the rear view mirror. The 2021 numbers put the company on a very unchallenging 7.9x 21 PE and a 4.6x 21 EV/EBITDA, with a RoE of 44%.

CIB (Egypt, Financials) management meeting feedback. We had a meeting with CIB management. FY21 results are yet to be released but the discussion was centered more on their FY22 outlook. We came away confident that a substantial upgrade in our earnings forecast is necessary. Firstly, the yield curve is shifting up while low cost EGP deposit growth is still in place which will expand margins. Secondly, the revenue authority in Egypt is taking a more conservative view on provisions. Historically, CIB provided aggressively to reduce taxable income. The CEO, Hussein Abaza, said that cost of risk will likely average closer to 1% annually and in 2022 vs. our estimate of 2.2% average CoR in the last 10 years. The change in provisioning policy could boost earnings by as much as 10% and ROE by 1.7%. The combination of a higher yield outlook and lower CoR means we adjust our earning outlook for FY22 from +17% to +42% y/y. There will also be a further knock-on effect of a higher payout ratio. Lower provisions mean a higher ROE and a lower need to reserve capital for bad debt. While funding growth from capital will still remain high - we estimate it at 20% y/y - the payout ratio should adjust from the low 15% to about 30%. In addition to the higher payout ratio, management believes they should pay a catch-up dividend for missing a payout in FY20 due to Covid-19. They will not call it a special but simply adjust the payout for FY21 higher. Guidance is for a 40% payout ratio, payable in April or May this year. That means a likely DPS of EGP3.82 - that is a 7.6% yield. We believe that there is a strong case of share price gains in 2022 based on a short-term high dividend and better than expected outlook adjustment on earnings and ROE. We expect the market to digest a better outlook probably after 1q22 and 1H22 earnings releases.

EABL (Kenya, Consumer staples) 1H22 results: Stronger-than-expected topline of +23.5% y/y growth driven by solid volume recovery as restrictions eased in all markets. Double-digit topline growth in all categories across all markets which is quite an achievement given the challenging macro. Kenya (68% of sales) led with +27% y/y growth driven by a +49% bounceback in Senator. Uganda (18% of sales) showed +18% y/y growth driven by mainstream beer up +46%. Tanzania (15% of sales) grew +15% y/y bolstered by significant upswing in Guinness at +157%. Overall, new frontiers, the smallest contributor to topline with the newest innovative products, grew +49% y/y. This was followed by mainstream spirits which grew +25% y/y. Premium and beer also grew +18% and +17% respectively. Despite global supply chain challenges, COGS grew a muted +13.1% y/y, leading to GP margin expansion of 473bps to 48.2%. Effective cost management supported EBIT growth of +48.3% y/y. EBITDA margin expanded by 457bps to 35.7% (1H21: 31.1%). PBT growth was +121% y/y and bolstered by reduced interest payments. PAT grew +130.4% y/y. Dividend per share declared of KES 3.75. Management has indicated that they expect 2022 to be a year of recovery as growth momentum continues, as well as anticipated margin recovery.

MTNN (Nigeria, Communications services) – FY21 results update: MTNN produced an exceptionally good set of 2021 numbers. Revenues were +22.9%, EBITDA 27.9% and Net profit +45.5%. Operating cash flow was up 21%, despite a massive 37% increase in capex to support 4 and 5G roll out, as well as catch up from 2020. The company declared a total dividend for the year of 13.12 kobo, or 6.5%. Data revenues were particularly encouraging at+55% and it is interesting to note that only 50% of the voice customer base is penetrated, leaving lots more room for growth in uptake. An area that has traditionally lagged, Fintech, is now starting to get traction. MTN Fintech now has 9.4m subscribers, 770k MoMo agents and revenue grew 57.3% for the year. We expect this to strongly accelerate, especially given the recent award of the PSB license approval in principle. To give an indication of the potential of this revenue stream, Fintech represents only 7% of voice revenue, starkly contrasted against Safaricom, where MPESA is 125% the size of voice revenue!

Market outlook

We continue to allocate to high quality businesses; those that score highly on our internally developed, Likert Q-scoring system, both currently and over time. We have two additional quantitative overlays, valuation and growth. We also have two qualitative overlays being management and ESG. What is particularly exciting is that we have a number of businesses across Africa that fit these criteria. The key transformational trends of financial inclusion, urbanisation and economic formalisation underpin a robust African consumer story that is taking shape regardless of global volatility. We allocate to the best companies in the sectors that tap into this transformation. At the moment, we have a bias towards financial inclusion and fintech themes as they do particularly well on our growth metrics. **Nigeria –** Nigeria's outlook is improving with substantially higher oil prices making painful but necessary economic reforms more likely. However, the latest plan to delay fuel subsidy reform again shows institutional weakness. We still wait for a signal from the CBN for a free flow and float of the Naira which is for us the real trigger for economic recovery. The communications, fintech and banking sectors are growing strongly, yet high quality companies exploiting these, are at all time low valuation multiples. **Egypt –** The outlook for Egypt remains positive especially towards the end of 2022 when a new capex cycle is expected to kick off. The exceptional progress made under the IMF program from 2017 to 2020 has been evidenced in a stable FX and net reserve position. Moving from gas importer to exporter helped cushion the blow from lost tourism revenues and the CBE's sound monetary policies have kept the bond carry trade alive. With 98% of household consumption in cash, the investment opportunity for us in fintech is immense in this 100m population country and it will also drive economic formalisation and increased government revenue through widening of the tax net. Management teams are signalling a new capex cycle. We expect an acceleration of capex projects towards the end of 2022 as capacity becomes stretched. **Morocco –** Morocco's key economic drivers are mining, agriculture and tourism. Strong commodity prices and a good rainy season should help to offset weakness from tourism. In terms of outlook it remains a stable, mid-growth country with excellent opportunities in retail and fintech. **Kenya –** Kenya missed its key tourist season of July-August, owing to travel restrictions. Some support will be provided by a good agriculture season and high soft commodity prices, where Kenya is a large exporter of tea, coffee, flowers and vegetables. Overall, we are satisfied by the performance of our financial inclusion focus here and expect growth to be steady. **Mauritius –** Mauritius remains very dependent on the timing of large-scale tourism recovery. Unless tourism comes back strongly in the peak December 2021 season, which is now under threat from the Omicron variant, the macro and MCB will be under pressure. **Vaccine roll-out** is making strong progress in our core markets, with Morocco almost fully vaccinated.