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) –

May Performance (%)	LCY	USD
Tunisia	2.3	2.2
Botswana	-1.5	-2.1
Morocco	-1.7	-2.3
Mauritius	-0.4	-3.2
Zambia	0.5	-3.2
Nigeria*	-3.7	-3.3
Kenya	-4.7	-4.7
Egypt	-7.7	-5.7
MSCI World	-6.1	-6.1
MSCI EM	-7.5	-7.5
BRVM	-7.9	-8.0

**MSCI Nigeria*

May was a negative month impacted by a global risk off environment in most of African markets. FX impact was significant. Against the Euro, the Egyptian pound strengthened by 2.7% while the Zambian kwacha and Mauritian rupee declined by 3.3% and 2.3% respectively.

Economic and political overview

Nigeria – GDP recovery remains at a moderate level. National Bureau of Statistics (NBS) reported real 1q19 GDP of +2% y/y versus 2.4 and 1.9% in last two quarters of 2018. April inflation remains at the same level at 11.4% y/y. Limited food supply due to the current planting season amid insecurity concerns likely impacted food inflation which was at 13.7%. April Manufacturing PMI + 0.1 points to 57.8 while the non-manufacturing PMI +0.2 points to 58.9. Central bank of Nigeria (CBN) governor Emefiele said they used recent oil strength to add more FX reserves which we tracked in previous reports. CBN held its benchmark interest rate at 13.5%.

Egypt – Central Bank of Egypt (CBE) left policy rates unchanged this month. MPC noted that GDP was +5.6% y/y in 1Q19 (5.5% in 4Q18). The MPC takes in consideration some price pressure in the next few months in its decision. Residential electricity prices could increase by 30-60% after the next round of subsidy cuts that will take place in July 2019. The MPC also mentioned that domestic demand is lagging external demand which has been strong. Domestic consumption recovery probably has more to run considering PMI remains at a moderate 50-level. Emirates NBD Egypt PMI rose to 50.8 in April (49.9 March). Tourism shows strong growth. Revenue per available room (RevPAR) growth in Egypt's hotel market grew 34% y/y during 1q19, according to a report by Colliers International. RevPAR is forecast to grow by an average 21% through 2019, with hotels in Cairo growing 99%, Alexandria 69%, Hurghada 42%, and Sharm El Sheikh 30%.

Kenya – Kenya's Central Bank of Kenya (CBK) reported remittances grew +23% y/y to USD 2.75bn in April. CBK held the policy rate at 9%. Monetary policy committee says it held rates in an environment where inflation is contained and foreign exchange market is stable. Kenya has sold a USD 2.1 bn Eurobond, the third in five years, and was 4.5x oversubscribed. Priced at 7% for 7yr and 8% for 12% for 12yr maturity. Bond will refinance USD750m 2014 bond that matures in June. Inflation eased to 5.5% in May after moving to 6.6% due to some drought related food supply resources.

Morocco – Morocco's Inflation still weak, +0.2% y/y in April, 0.1% y/y in March. Morocco's unemployment rate eased to 10% at the end of March, from 10.5% a year earlier. Agriculture and fisheries shed 152,000 jobs over the year to March. Farm incomes are volatile in the semi-arid north African country, hinging on rainfall levels. The Moroccan government is forecasting that a 23% drop in rainfall this year will shrink the cereal harvest by more than 40% to 6.1mt. Job losses in the farming sector were offset by the creation of 144,000 jobs in services, 4,000 in industry and 19,000 in construction.

Company updates

Commercial International Bank (Egypt, Financials) 1Q19 PBT +31% y/y was an excellent result. We also like that the result is driven by loan growth supporting an economic recovery. Loan growth for the quarter was 5.6% continuing the trend of about 20-25% loan growth which started in 2018. The main PBT driver is margin expansion that comes from increased leverage and higher priced loans. Loans have +3-4% better pricing than fixed income on both EGP and USD books. It has meant NIMs moving from 4.5% in 1Q18 to 6% currently, a 33% improvement. ROE trajectory at 26-27%, book value growth high at 29.4% and 20.3% for FY19 and FY20. We have upgraded our PBT forecast by 5% to reflect a very strong start which is expected to continue.

IDH (Egypt, Healthcare) 1Q19 results update: A very good performance, albeit it with some aesthetic distortion. Revenues came in 22%, EBITDA +42%, EPS +11% and cash flow up 75%. Adjustments came from first time adoption of IFRS 16, capitalization of leases and the 100 Million Healthy Lives Campaign, which offered certain tests at substantially lower rates. The underlying metrics remain strong, where ex-Campaign tests and revenue per test were up 8% and 9% respectively. Scale benefits and purchasing power gained traction with COGS/test down 4% and excluding IFRS 16, EBITDA was +33%. On the development side, the company noted that the new radiology venture with Al-Borg Scan is already delivering positive results and contributing to growth and profitability.

EIPICO (Egypt, Healthcare) 1Q19 results update: Good results, in line with expectations. Revenue was up 25% y/y and HEPS was up 19%. Local sales were up 29% and export sales were up 10%. OPEX growth continues to grow faster than topline, up 37% y/y (a trend we saw throughout 2018), resulting in EBIT margins contracting from 29.5% in 1Q18 to 26.6% in 1Q19. We believe the growth in OPEX is due to promotional activity and a greater reliance on 3rd party distributors. We noted in the FY18 results that EIPICO lost market share, with the pharmaceutical sector growing 25% y/y by value whilst EIPICO grew 18%. In 1Q19 we believe that EIPICO started regaining lost market share with local sales up 29% y/y. We expect continued strong growth in the sector and the company, with most of the growth being volume driven (a key part of their strategy), they have sufficient room for growth with capacity utilisation currently at c60%. However, improved GP margins will be dampened by OPEX as they continue to spend aggressively on marketing and distribution. They remain net cash despite the rise in short term borrowings used to finance working capital. The sharp rise in inventory last year was due to bulk purchasing of API and we have started to see that inventory number come down, however, receivables continue to grow and so does working capital. There are plans underway to establish a 10k sqm plant to produce biosimilar drugs (oncology and hormone products) but we have not received enough information on this yet.

Safaricom (Kenya, Communications services) Year to 31 March 2019 results update: Overall good set of results, with a special dividend declared. Revenues came in +7.1%, EBIT +12.2% and topping guidance on digitalization efficiencies and opex control and EPS +13.0% to KES 1.56. A strong FCF performance of +14.1% gave management the comfort to recommend a dividend of KES 1.25 and a special dividend of KES 0.62. MPESA continues to be the key driver of revenue as well as profitability as both number and value of transactions rose, with increased in-wallet usage also reducing agent commissions on withdrawals and top-ups. The main area of concern was a competition driven slowdown in mobile data revenues, as a 57% decline in price per Mb and slowing customer growth, offset rapid consumption growth. We are comfortable that organic and quality driven customer acquisition, increased 4G coverage and robust consumption; as well as the bulk of price declines already taken, data revenues will rebound.

Equity Bank (Kenya, Financials) 1Q19 PBT +6% y/y a decent set of results at an attractive 27.1% ROE, higher than guidance. Key highlight was the return to growth in fee-based income +6.9% y/y. In FY18 a decision to offer low/no promotional fees on mobile banking meant weak fee-based performance. Management guided to return to normal fees in FY19 which 1Q19 results confirm. The one negative area of the results was a deterioration in the NPL ratio from 7.5% to 9% coming from a bad debt in Tanzania. Local SMEs were affected by 1) the ban on cashew nut exports and 2) the shift in government offices from Dar to Dodoma which caused late payments. Management still confident they can manage NPL ratio to below 5.5% in 2019. Good ROE result of 27.1% which underpins attractiveness of 1.3x FY19 book valuation.

Sonatel (BRVM, Communications services) 1Q19 results update: This release marked the first set of quarterly results, as the coming narrows its reporting cycle. Revenues came in +9.9%, EBITDA +6.7% and EPS +3.3% as the base effect of the increased PST turnover tax in Senegal to 5%, effective 1 July 2018, dragged. As of the third quarter, this tax will not only be in the base, but is being reduced to 4.5% on 1 July. This is a significant moment as it could mark an end to the ever increasing taxes and fees levied by governments and regulators in the region. In a further positive move the Senegalese regulator allowed asymmetric interconnect rates to expire, ending a competitive disadvantage to Sonatel. Data, Orange Money and internet subscribers grew 15%, 22% and 21% respectively.

Mauritius Commercial Bank (Mauritius, Financials) 3Q19 to March PBT +20% y/y. Continue with faster trend of growth we witnessed in 1H19. Credit growth of 13% YTD and 19% y/y still the main driver through higher NIM and credit related fees. Management noted that it was a slower quarter (only 0.2% credit growth) after a strong first half but that their pipeline of trade and structured finance opportunities remain strong into June year end. While Mauritius is moderately positive, it is not the driver of its recent growth spurt. MCB is largely a play on its niche growth area of offering investment-grade counter-party banking and confirmation for large trade finance tickets in Africa. The positive spin off from higher growth is an expanding ROE from 14% to 16.7% which should be supportive to valuation multiples. FY19 PB multiple of 1.2x and dividend yield of 4.6%. 5yr average PB at 1.4x. We have a fair PB multiple of 1.5x.

Attijariwafa (Morocco, Financials) produced a decent set of 1Q19 results. PBT +5% y/y. Margins were slightly higher while the loan book was flat for the quarter. Translated into +8% interest income which was higher than cost growth of 6%. The main source of recent growth, Barclays Egypt, is undergoing an investment period, so it's higher ROE tailwind has lessened for now. Morocco's loan performance was disappointing after some encouraging datapoints in 2018.

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.

IMARA
Asset Management

Overall strategic review of Financials allocation (May 2019)

The culmination of FY19 and 1Q19 results offers a good opportunity to reflect on company selection in our strategic allocation meetings. For this month we give feedback on the Financials portion of the portfolio. We have reviewed our overall allocation and see no reason for selection changes at this stage. Egypt and to a lesser extent Mauritius is where the momentum play is. The emergence of more credit growth from an improving Egypt macro is maintaining margins and fee growth. We are comfortable that the earnings momentum there will be maintained. In addition to CIB we like Credit Agricole Egypt which produces similar margins at slightly higher ROEs through the cycle. However, we believe CIB has a more focused management team and ability to take risk in an improving environment. Credit Agricole is 4-5x smaller than CIB and has historically been slower and more conservative in taking on more risk in a below investment grade Egypt. The rest of the universe is made up by low profitability and/or illiquid names.

While the Mauritius macro is moderately positive, it is not the driver of its recent growth spurt for our MCB holding. MCB is largely a play on its niche growth area of offering investment-grade counter-party banking and confirmation for large trade finance tickets in Africa. State Bank Mauritius is a poor competitor with India-focused strategy that we do not think will work and a low ROE/excess capital position.

Our core value and growth play in Financials is centered on Nigeria and Kenya. We think Equity Bank, GTB and Stanbic IBTC are fundamentally undervalued at 1.3, 1.6x and 1.7x book if one considers they are likely to return 25% to 30% through the cycle. GTB and Stanbic IBTC tends to outperform its closest competitors Zenith and Access through products and gaining deposit market share. While Equity Bank for us remains far superior to KCB, Barclays Kenya and Co-op Bank. Its technology, management and focus is better. Recently, KCB which is a reasonable bottom-up stock selection and value play at 1x book for 21% ROE was forced into a low-synergy acquisition of NBK by its influential and mutual government shareholder. The best alternative to Equity in Kenya will now be faced with a year of merger issues.

Both GTB and Equity management teams expect credit growth of c.10% in 2019. However, it is still early stage after a slowdown in both countries. Kenya is at the end of adjusting to rate caps where credit growth focus was on SMEs. Nigerian banks on the other side have been draconian in crushing NPLs with a much steeper contraction effect.