Equities investment strategy

Overall, the stock market currently presents a buying opportunity for companies with solid fundamentals. We believe investors should take up positions in value stocks that are trading at discounts to their intrinsic value. We expect the banking sector to report improved performance in 3Q2022 in a higher interest rate environment, which is bound to boost its revenues.

Opportunities

- **Price discounts:** The current market Price to Earnings (P/E) multiple of 6.9x translates to a discount from the 10-yr historical average of 12.9x and presents a suitable opportunity to buy the dip for future capital appreciation.
- **Re-balancing of portfolios:** A balanced portfolio is the best defense against a bear market. Diversification of a portfolio seeks to curb exposure to risk, prioritizing investment in companies with strong and well-capitalized balance sheets.
- **Dividend stocks:** Dividend-paying stocks are an efficient way to hedge the effects of a bear market while providing a stream of income to investors.

Threats

- The stock market has been volatile amid concerns about rising inflation and interest rates.
- Geopolitical risks in Europe are expected to lead to dyspeptic market reactions as experienced in the past month.

Counter	52-Weeks High	52-Weeks Low	Current Price	M/M Performance	Target price	Upside	Recommendation
Banking							
ABSA	12.95	9.02	11.25	(1.75%)	17.10	52.0%	BUY
COOP	14.00	10.30	11.80	(0.42%)	17.30	46.6%	BUY
SCBK	148.75	121.00	138.25	1.10%	169.60	22.7%	BUY
KCB	46.00	34.00	37.65	(9.17%)	50.00	32.8%	BUY
I&M	22.00	16.50	17.00	0.00%	21.40	25.9%	BUY
Stanbic	106.00	90.00	96.25	(3.75%)	107.30	11.5%	ACCUMULATE
Equity	53.00	38.75	46.70	0.54%	50.00	7.1%	HOLD
Insurance							
Britam	7.10	5.14	5.58	(6.38%)	6.24	11.8%	ACCUMULATE
Telecommunication							
Safaricom	45.25	23.00	25.10	0.60%	34.22	36.3%	BUY
Energy & Petroleum							
Kengen	4.00	3.35	3.38	(3.43%)	5.37	58.9%	BUY
Kenya power	1.70	1.30	1.86	(1.1%)	2.00	7.53%	HOLD
Manufacturing & Allied							
EABL	194.00	110.00	167.25	17.78%	179.63	7.40%	HOLD

Source: Bloomberg, NCBA IB Research, NSE

October in a snapshot

The local equities market remained relatively unchanged with NASI and NSE-25 gaining by 0.3% and 0.6%, respectively, while NSE-20 shrank by 2.3%. The market sustained its bear run, with the NASI sinking 24% below its January peak.

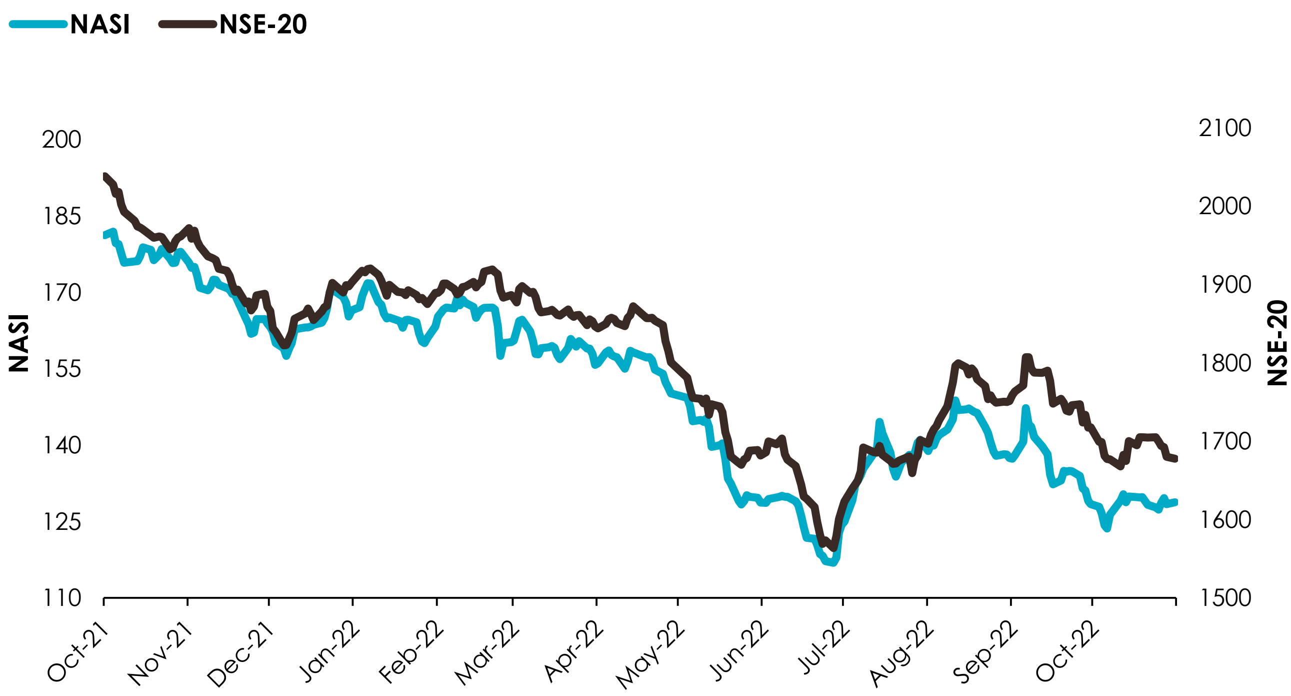
Foreign investors accounted for 41.1% of total turnover and were net sellers withdrawing KES 3.22Bn last month. The market has remained clouded by negative risk sentiment which has seen a sustained sell-off by foreigners.

The month of October recorded the highest level of inflation at 9.6% driven by increase in prices of food & non-alcoholic beverages (15.8% from 15.5%) and fuel (12.6% from 10.2%). Inflation is expected to remain elevated in Q4 2022.

The global economic growth outlook for 2022 was maintained at 3.2% in October 2022 by the International Monetary Fund (IMF) as a result of the ongoing Russia-Ukraine war that has continued to exert pressure on energy and food prices. This impact is expected to have a bigger negative ripple effect in 2023.

The chart below highlights the movement of main market indices for the last 12-month period:

NASI vs NSE 20 Movement - Last 12 months



Source: NSE, NCBA IB Research

INVESTMENT CONSIDERATIONS

ABSA Bank Kenya: BUY with a TP of KES 17.10

- ABSA released its H1'22 financial results posting a 13.0% y/y increase in PAT to KES 6.3Bn.
- The increase in PAT is mainly attributable to the 17.2% increase in Net interest income (NII) which was boosted by a significant 19.5% growth in the loan book and an impressive 5x growth in Timiza customers. Timiza is a mobile banking app that allows subscribers to apply for instant loans.
- Loan loss provisions increased by 52.2% thus slowing down the bottom-line gains, as the bank sought to correct the significant low loan provisions in H1'2021.
- Asset quality: The group posted an improved NPL ratio of 7.1% supported by prudent credit risk management policies.
- Going forward, the bank's continued focus on channel diversification, impressive asset quality, and, entrance into business lines namely custody business and private wealth management will continue to generate long-term profitability.

Britam: ACCUMULATE with a TP of KES 6.24

- Britam has a strong and a large asset base (KES 153.4Bn) that it can leverage to fund expansion as well as take advantage of the latest technology to get an edge in the industry.
- The insurer's sound and organic premium growth, the just concluded staff reorganization, strategic partnerships and reduced exposure to volatile equities market provide a basis for long-term stability of the company.
- The company is expected to remain resilient and dynamic provided that it adapts to the ever-evolving consumer preferences and integrate insurance tech more broadly.
- Operational inefficiencies pose a key risk. Britam's Expense ratio, inclusive of commissions payable, was 82.1% in 2021 compared to the industry average of 60.1%.
- At the current market price, the stock is trading at par to its value but presents a value pick for long-term investors.

Coop Bank: BUY with a TP of KES 17.30

- Coop bank released its H1'22 financial results posting a 55.7% increase in PAT to KES 11.5Bn. The performance is attributed to two prongs; a) Increased operating income especially NFI, and, b) Reduced provisioning level despite growth in NPLs.
- The bank's asset quality improved, with the NPL ratio declining to 14.1% in H1'22, from 15.2% in H1'21 attributable to a faster growth in total loans relative to gross NPL level.
- Key downside risk is Kingdom bank's performance as it recorded reduced operating income, NPL ratio of above 60% and expected servicing of the CBK overdraft facility of KES 21.0Bn that is expected to be serviced for 10 years effective 2023.
- We expect the bank to continue exhibiting stable growth, gradual improvement in the loan book and NFI growth owing to levies from SACCO-related services.

EABL: BUY with a TP of KES 179.63

- EABL announced a 123.7% y/y increase in Profit after Tax (PAT to KES 8.73Bn. Revenue grew by 27.3% to KES 109.4Bn largely driven by investment in marketing coupled with innovations in response to behavior shifts by consumers.
- The impressive growth was also driven by economic recovery following the lifting of pandemic-related restrictions.

- Growth in the regional subsidiaries was fairly distributed with sales in Kenya expanding 27%, Uganda by 24% and Tanzania by 21%, driven by growth in volumes.
- The company announced a final DPS of KES 7.25 (Total dividend = KES 11.0 following an earlier interim dividend of KES 3.75). Book closure is on 15th September 2022.

Equity Group PLC: HOLD at a TP of KES 50.00

- Equity Group released its H1'2022 Results, recording a 36.1% y/y growth in Profit after Tax (PAT) to KES 24.4Bn from KES 17.9Bn in H1'2021, driven by impressive growths in both non-funded income and net interest income.
- Net loans grew by 28.9% y/y anchoring the Group's impressive asset growth to KES 1.3Tn.
- Notably, the Group's asset quality improved, recording an NPL ratio of 8.5%, which is below the industry average of 14.7%. On the other hand, customer deposits increased by 18.5% to KES 970.9Bn.
- We expect Equity Group to continue registering strong performances with the DRC subsidiary raising prospects of achieving sustainable long-term growth.
- The geographical diversification strategy has continued to pay off. The Group is expected to leverage its regional footprint, strong financial capability, and brand trust to accelerate growth in MSMEs.

I&M Bank: BUY at a TP of KES 21.40

- I&M Bank reported a 16.0% y/y increase in PAT to KES 4.7Bn in H1'2022 attributable to the 21.6% increase in operating income.
- Operating expenses increased significantly by 19.3% to KES 8.6Bn weighing down on the earnings.
- Loan loss provisions increased by 24.4% to KES 1.3Bn as the bank aimed to increase its NPL coverage – this was against a back drop of improving asset quality.
- NPL ratio improved to 9.3%, from 10.4% recorded in H1'2021 indicated prudent risk management
- Going forward, the bank seeks to leverage on the digital transformation strategy as well as its regional presence to increase profitability.

KCB Group PLC: BUY at a TP of KES 50.50

- KCB Group released its H1'2022 Results, recording a 28.4% y/y PAT growth to KES 19.6Bn from KES 15.3Bn in H1'2021, driven by a 16.8% increase in the operating income.
- Net loans grew by 20.3% y/y anchoring the Group's impressive asset growth to KES 1.2Tn.
- Of concern was the Group's asset quality with the NPL ratio increasing to 21.4% from 14.4% last year. This was largely driven by the Kenyan subsidiary which recorded an NPL ratio of 22.8% and anchored the 81.2% growth in Gross Non-Performing Loans.
- Despite the worrying jump in NPL ratio and increase in operating expenses, we expect the Group's recent acquisition in DRC subsidiaries to support the bank's medium term performance.

KenGen: BUY with a TP of KES 5.37

- KenGen recorded a 9% increase in profit before tax to 7.52Bn y/y supported by income from revenue diversification initiatives and overall growth in electricity demand. This is according to their last financial results.
- Revenue increased by 14% to 24.8Bn. Operating expenses increased in tandem (up 8%) owing to increased business activity in Ethiopia, repairs and maintenance costs.
- In the year ahead, we are looking at a sustained buoyant financial performance on the back of increased geothermal capacity and additional contractual revenues from well-drilling and geothermal contracts in Ethiopia and Djibouti.
- At the current market price, the stock is a value pick for long-term investors.

Kenya Power: Under Review

- Kenya Power released their financials recording profit after tax of KES 3.5Bn attributed to a rise in revenue derived from the reopening of the economy and a larger consumer base.
- Finance costs increased by 40.2% to KES 12.69Bn as a result of a strengthening dollar as majority of the its debt is dollar denominated.
- Fuel costs increased by 22.3% to KES 115.21Bn due to an increase in units purchased from thermal plants as a result of low hydrology and an upsurge in fuel prices.
- Unclear dividend policy dampening investor appetite. The company did not declare a dividend and has not paid dividends in the last five years.
- Negative working capital position. The company has remained in a net current liability position for the fifth consecutive year. Working capital remained adverse in FY22 at KES 55.74Bn. This is however an improvement of 19.3% from the previous financial year.

Safaricom: BUY at a TP of 34.22

- There were no new financials reported in the last month – Safaricom' s price has however exhibited volatility due to its high liquidity.
- The share price declined by 5.8% in August 2022 to KES 28.0 which presents a great entry point for long term investors.
- In August, Safaricom announced that it had begun a large-scale customer pilot of its network in Dire Dawa City, Ethiopia. The program which will be launched nationally in October 2022, aims at availing Safaricom' s network in 25 cities by April 2023. This will boost the firm's path in meeting its target of EBITDA breakeven in Ethiopia by 2026. We view the Ethiopian expansion as a good long term prospect that will sustain high profit levels in the future and reduce reliance on the Kenyan market.

Stanbic Bank: ACCUMULATE with a TP of KES 107.3

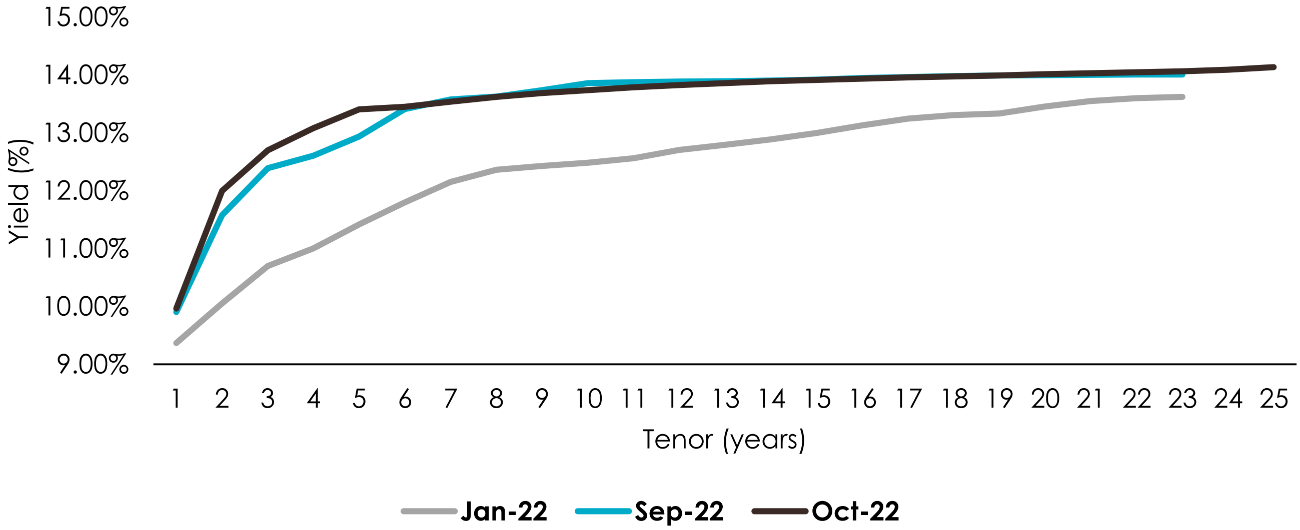
- Stanbic Holdings released its H1'2022 Results, recording a 36.9% y/y growth in Profit after Tax (PAT) to KES 4.8Bn.
- Notably, the bank's deposits declined marginally to KES 258.2Bn from KES 260.0Bn in H1'2021 taking the Loan to deposit ratio to 94.5% from 79.9%
- Asset quality remained relatively unchanged at 9.4%.
- We expect Stanbic to sustain the performance in H2'2022 with a key focus on boosting non-funded income and improving its NPL ratio as the uncertain election cycle comes to an end.

Standard Chartered: BUY with a TP of KES 169.60

- Stanchart released its H'122 results posting a 10.9% increase in PAT to KES 5.4Bn.
- Cost to Income Ratio without loan loss provisions deteriorated to 50.6%, from 47.3% in H1'2021.
- Deposit mobilization capability remained in question with deposits growing by 3.1%, the lowest among Tier 1 banks.
- Asset quality: NPL ratio remained unchanged at 15.4% in H1'2022 same as recorded in H1'2021, and above the industry's average of 14.7% as of June 2022. This remains a key concern especially taking into account the loan book size which shrunk y/y.
- Loan loss provisions declined to KES 0.1Bn but NPL coverage remained the highest amongst its peers at 83.9%.
- The bank's NFI line is expected to be a key growth driver with the bank having a strong presence in the investment advisory and wealth management services.

FIXED INCOME

Government Securities Yield Curve



Source: NSE, NCBA IB Research

On a year-to-date basis, yields across all tenors remain signficantly high owing to the deteriorated macros. In addition to that, the monetary policy hike in May from 7.0% to 7.5%, has filtered into the market, leading to higher yields. In September, the Central Bank of Kenya hiked the policy rate further to 8.25% - as a result, we expect the upwards pressure on the yield curve to persist for the remaining part of 2022.

In the primary market, both bonds and treasury bills had low subscription rates in the previous month with the October bond auctions recording a subscription rate of 56.2% of the KES 60Bn on offer and treasury bills' average subscription coming in at 91.9% during the month.

We expect interest rates to keep rising owing to the rising inflation rate, tighter external credit markets and recent policy hike.

November Bond Offer

In the primary market, the Central Bank of Kenya is offering an opportunity to participate in the auction of an infrastructure bond, seeking to raise KES 60.0Bn for budgetary support.
See below a summary of the offer:

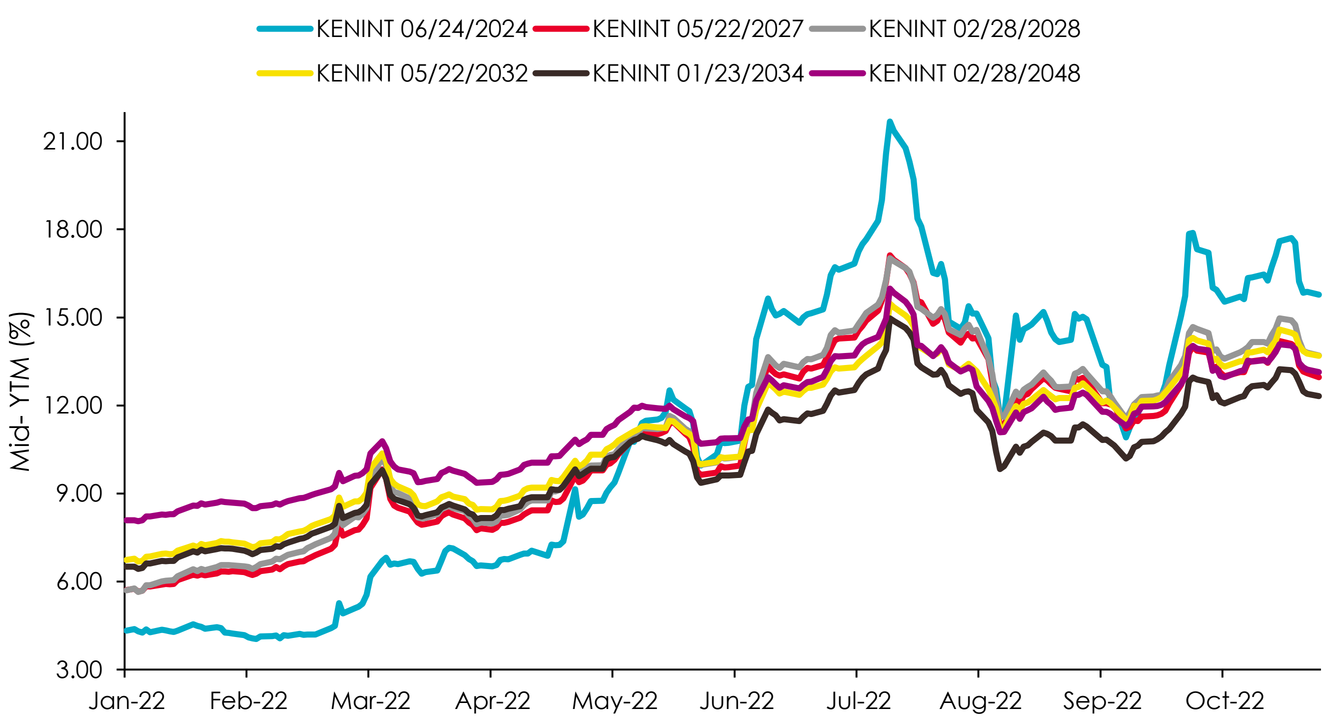
Issue Number	IFB1/2022/14
Type	**New**
Tenor	14.0 years
Redemption Date	27-Oct-2036
Coupon (%)	Market Determined
Bidding Guide	**13.75% - 13.99%**
Amount	KES 60.0 Bn
Period of Sale	26-Sep-22 to 8-Nov-22
Value Date	Monday 14-Nov-2022

Kenya International Debt Yield Curves

Kenyan Eurobonds yields remained relatively unvaried in October. However, Eurobond yields remain elevated above historical levels – a phenomenon we expect to persist for the rest of the year given the prevailing global economic and geo-political conditions.

Below are the six Kenyan Eurobonds and their yield trends in 2022:

No.	Eurobond	Tenor	Coupon Rate (%)	Current Yield (%)
1	KENINT 06/24/2024	1.7 Yrs	6.88	15.60%
2	KENINT 05/22/2027	4.6 Yrs	7.00	12.74%
3	KENINT 02/28/2028	5.3 Yrs	7.25	13.55%
4	KENINT 05/22/2032	9.6 Yrs	8.00	13.54%
5	KENINT 01/23/2034	11.3 Yrs	6.30	12.21%
6	KENINT 02/28/2048	25.4 Yrs	8.25	13.04%



Source: Bloomberg, NCBA IB Research

About NCBA Investment Bank

NCBA Investment Bank is a subsidiary of NCBA Group. The services offered by the brokerage department include equities trading for listed securities, fixed income trading for both corporate and government bonds, Over the Counter (OTC) equity transactions as well as execution of equities transactions across the East African countries. Additionally, NCBA Investment Bank backs these activities with solid advice from the research team to enable investors meet their return objectives. NCBA Investment Bank deploys simple and convenient client driven technologies, robust risk management, highly competent and experienced staff and has the backing of robust research capabilities to differentiate itself from other players in the market.

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Certification

The following analyst(s) who prepared this research report: Victoria Mututu and Justin N Mwangi hereby certify that: (i) all of the views and opinions expressed in this research report accurately reflect the research analyst's(s') personal views about the subject investment(s) and companies (y) and (ii) no part of the analyst's(s') compensation was, is or will be directly or indirectly related to the specific recommendations or views expressed by the analyst(s) in this research report.

Rating Definitions

BUY – Total expected 12-month return (incl. dividends) greater than 20%
ACCUMULATE-Total expected 12-month return (incl. dividends) between 10%- 20%
HOLD – Total expected 12-month return (incl. dividends) between 0%-10%
SELL – Total expected 12-month return (incl. dividends) less than 0%

Disclaimer

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