

Market snapshot

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

| Sep Performance (%) | LCY | USD |
|---------------------|------|------|
| Nigeria | 6.0 | 6.9 |
| Kenya | 0.2 | -0.6 |
| Botswana | -0.8 | -1.6 |
| Tunisia | -0.3 | -1.7 |
| MSCI EM | -1.8 | -1.8 |
| Egypt | -3.3 | -2.6 |
| Morocco | -1.5 | -2.6 |
| Zambia | -0.5 | -3.0 |
| MSCI World | -3.6 | -3.6 |
| Mauritius | -4.4 | -4.7 |
| BRVM | -3.3 | -5.0 |

September had mixed performances, with Nigeria up (+6.9%). Negative performances from Kenya (-0.6%), Egypt (-2.6%), Morocco (-2.6%) and Mauritius (-4.7%). COVID-19 has returned to the forefront of the world stage once again as a second wave of infections emerge in parts of the EU and the UK. In contrast, Africa and most of our key markets see a decline in infections and a possible end of the first wave. The UN World Tourism Organisation released a report on the pandemic impact on international tourism which has taken a knock. African and the Middle East suffered a 57% contraction in the sector in 1H20.

Economic and political overview

Nigeria – The Central Bank of Nigeria’s (CBN) Monetary Policy Committee (MPC) cut the policy rate by 100bps to 11.5%. This is the bank’s attempt to cushion the blow of the supply side shocks. The CBN has disbursed NGN 369bn (USD 967m) so far to various sectors most impacted by the pandemic. Cinemas and gyms were reopened this month at 33% capacity limits.

Discussions on states’ ability to pay minimum wage resumed. They were suspended as the pandemic took precedence. Some federal workers are being paid in larger States such as Lagos and Abuja. However, 13 of 36 States are technically insolvent and have pointed to their inability to pay the adjusted minimum wage of NGN 30,000 per month. Overall, state governments owe the Federal government USD 15.1bn which is 10.5% of GDP as of June.

The CBN announced the issuance of more licences for payment service banks subject to a minimum capital base of USD 13m. The high hurdle could serve as a deterrent for many new entrants and fintech companies. Telcos, banking agents, retail chains and postal services can apply for licenses should they meet the requirement.

The CBN started to supply more liquidity to the I&E window in September. Stanbic IBTC noted that the CBN started to supply more liquidity after discussions with banks on how to address the backlog. FMDQ clearing statistics show they sold

USD1.8bn to the window in September versus USD 857m in August and a low of USD 747m in May. Stanbic say the backlog is declining gradually. We remain skeptical as the liquidity does not compare well to the previous range of USD 6-8bn per month in 1q20 before the market effectively shut in April. It is a step in the right direction and we monitor the daily clearance data to see if the new trend persists.

Macro releases (August stats):

- Inflation rose 13.2% y/y (Jul: 12.8%) due to continued disruptions in supply of goods and services.
- FX reserves crept down to USD 35.7bn (Jul: USD 35.9bn).
- PMI was 54.6 (Jul: 50.4).
- M3 growth grew 5.6% y/y (Jul: 3.2%).
- Credit to the private sector slowed to 21.4% y/y (Jul: 24.3%).

Egypt – GDP was 3.5% as at FY19/20 (June), in line with the government's expectations. Stimulative policies supported growth, especially in 2q20 as tourism and manufacturing sectors suffered. Moody's maintained Egypt's credit rating at B2 with a stable outlook. This reflects the diversification of the economy, funding base, FX reserves and credible monetary policy.

The Central Bank of Egypt's (CBE) Monetary Policy Committee (MPC) cut rates by 50bps to 9.75% this month. Additionally the CBE has extended the fee waiver on EGP transfers and ATM withdrawals until year-end. However the 6 month moratorium on loans expired on 15 September and has not been renewed.

The National Bank of Egypt and Bank Misr have stopped issuing 15% one-year special certificates of deposit (CDs). Collectively, they gathered EGP 383bn (USD 24.4bn) in under a year; 12% of total local currency deposits. Demand deposits typically constitute 10-15% of total deposits, due to high funding costs in Egypt. In contrast, Nigerian Demand deposits make up 60% of total, with much lower cost of funds. Nigerian banks like GTB have funding costs c.2.6% vs Egypt's CIB of 6.8%. We should see margins improve with the abolishment of CD issuance and earnings uplift as competition eases.

Museums and archaeological sites reopened this month. Tourism support services also resumed under strict protocols. Egypt's tourism sector rebound is already outperforming its regional peers having seen over 250 000 visitors since July. Like most other countries, travellers are required to present a negative lab test result for COVID-19 on arrival, with some airports testing on site. This has come on the back of declining COVID-19 cases and quarantine facilities at c.16% utilisation. Open-air gatherings are now also permitted.

Macro releases included (August stats):

- Inflation was 3.4% y/y (Jul: 4.2%).
- FX reserves were flat at USD 38.4bn (Jul: USD 38.3bn).
- PMI was flat at 49.4 (Jul: 49.6).
- Credit loan growth rose to 18.2% y/y in July (Jun: 16.8%).

- Remittances grew 9.5% y/y in July, to USD 2.9bn. From January to July, total remittances were up +7.8% y/y to USD 17bn.

Kenya – 1H20 saw job losses total 2.2m according to the Kenya National Bureau of Statistics. 2q20 showed the largest impact of COVID-19 with unemployment at 10.4% (1q20: 5.2%). The combination of unemployment and under-employment is the labour under-utilisation rate which jumped to 17.2% in 2q20 (1q20: 8.3%).

The Central Bank of Kenya (CBK) has directed banks to seek approval prior to declaring dividends. The focus is to ensure banks have sufficient capital to withstand the impact of COVID-19. There has been a spate of high provisions posted across the sector, covering high-risk sector loans.

Horticultural exports increased as economies opened up, growing 9% y/y cumulatively to end-July. Kenya's primary market for fresh produce is Europe, which had higher demand m/m during the year. Fruit earnings posted significant growth of 55% y/y. However vegetables declined -11% y/y. Flowers, constituting the highest percentage of income, showed growth of +1.6% y/y.

Laptops, smartphones and other gadget imports grew 56.3% y/y. This was due to working from home, coupled with e-learning for students, which necessitated the extended use of tech products to ride the wave of movement restrictions and curfews. Kenya is seeing fewer daily COVID-19 cases, and sectors of the economy are set to reopen soon. Bars and pubs have been permitted to reopen end-September.

Other macro releases included (August stats):

- Inflation was flat at 4.4% (Jul: 4.4%).
- FX reserves slid down to USD 8.96bn (Jul: USD 9.34bn).
- PMI was 53.0 (Jul: 54.2)
- Kenya received 14, 049 tourists during August, as international flights resumed.
- Remittances rebounded 23.7% y/y (Jun: -2.3%) to USD 277m, driven by North American inflows.
- Current account deficit narrowed to -4.7% of GDP in July (Jun: -5% of GDP) as exports continued to grow.

Morocco – The government extended the state of emergency to 10 October as COVID-19 cases began to spike. Casablanca and Marrakech had restrictions reinstated in September, including closures of beaches and shorter trading hours. Travel has been banned, with exceptions requiring special authorization.

Loans grew 5.8% y/y end-July, with debt and overdrafts growing +12.7% y/y, equipment loans up +4.3% y/y and real estate loans up +1.8% y/y. Non-performing loans grew by 14.2%.

Macro releases (August stats):

- Inflation 0.9% y/y (Jul: -0.1%).
- FX reserves grew to USD 29.7bn (Jul: USD 28.3bn).
- M2 growth was 12.1% y/y in July (Jun: 8.8%).

Company updates

IDH (Egypt, Healthcare) 2q20 results and management call update: As had been flagged, revenues in April and May were down, as people were not only locked down, but consciously avoided medical facilities. Increased home visits and de-confinement saw June revenues recovery strongly, delivering 38% y/y growth. Overall for the quarter, revenue was -12.6%, with EBITDA -19.6% and EPS -20.2%. Having initially delayed the dividend, very healthy cash flows allowed for a dividend of USD 0.187 per share or 5% yield. In terms of outlook, as of 1 July all branches are fully open and Q3 activity is showing strong growth on 2019, while increased PCR testing and resumption of radiology should augment this. Home visit infrastructure is now in place, should a second wave require new lockdowns. For 2020, management are guiding to revenues of EGP 2-2.1bn with an EBITDA margin of 40%, in line with our forecasts. Even on FY20 numbers, the company trades on an unchallenging PE multiple of 17.5x, which should contract sharply in 2021 to 12x, well below its historical average of 21x.

HPS (Morocco, IT) 1H20 results update: Revenues came in +3.4%, EBIT +9.4% and EPS plus 22.9%. The growth in profitability was driven by improved performance of associates, as well as cost containment efforts. The slow top-line was mostly as a result of the non-core Services division contracting by 6%. The Solutions division was flat, as winning new projects ground to a halt. There were some encouraging developments during the period that will contribute to future growth:

- The ABSA Africa (ex-Barclays) countries were successfully migrated onto the POWERCARD platform.
- Deployed QR code functionality at the Ghana Interbank Payments and Settlements System.
- Strong growth in Upselling on existing contracts, mostly in tap to pay and mobile payments solutions for clients.

The Processing division grew revenues by 17% as the SocGen Africa project was deployed as well as a number of new clients (banks and telcos) signed up to use the Moroccan mobile switch, which HPS developed and owns alongside the main interbank switch.

Label Vie (Morocco, Consumer staples) 1H20 results update: The company put in a strong performance with revenues coming in +14.9%, EBIT 19.9% and PAT growing only 14.2%, dampened by the COVID Fund contribution. The company had originally guided to flat earnings growth for the year due to the COVID Fund contribution, however they opted to amortize it over 5 years, which local accounting and financial regulators are allowing them to do. In terms of format performance, Carrefour Market grew revenues by 21%, Hypermarket by 16% and Atacadao by 17%. For store expansion, of the 18 new stores guided to pre-Covid, they will only be able to complete 9 by year end. The Aradei Capital (59% owned real estate business) listing as a REIT, tabled for end 2020, has been postponed to 2021.

EABL (Kenya, Consumer Staples) call with management: Alcohol sales have just resumed in Kenya and management reported that Kisumu was at full production prior to the reopening. No distribution lag is anticipated, so this quarter should see volumes rebound. It may be a slower growth as shifts in behaviour due to strict capacity regulations in place are inevitable. The 'Raising the Bar' campaign launched in June, was EABL's way of proactively assisting bars and restaurants to prepare for resuming business. It is a 2-year programme which allows outlets to access digital training and targeted support to help comply with regulations and pay for equipment deemed necessary. We do not expect to see a full return to normal levels immediately, but demand proved to rebound quickly in the initial stages before the alcohol ban in Kenya.

Tanzania continues to grow unencumbered by restrictions. Access to alcohol is simple in Uganda through the informal distribution network. The pandemic has forced management to take a closer look at their off-trade business in Kenya, which allows access to alcohol online and in retail stores. Consumer take-up has been good with bulk buying, convenience packs and alternative formats available at the outlets. Management continue to invest into new areas of expansion e.g. pink gin, with the focus on recovery in 2021.

MCB (Mauritius, Financials) FY20 Results: PBT -18% y/y, 4q20 down 42% y/y driven largely by 3x increase in provisions to MUR 5bn which is CoR of 2%. The results exceeded our expectations by c.10% as operationally pre-provisions banking income was +8.2% y/y. The main positive was an improved NIM from the cheapening cost of funds. NIM was +11% y/y for 4q20 and FY20. While fee income was down as activity declined, trading profits in FX and bonds +70% was hugely supportive on the non-funded side. Overall a satisfying set of results with substantial challenges looming on the horizon. We rate the management, their strategy and dominant position in trade finance and local fintech but the macro will prove a headwind for the next 12-18 months until tourism normalizes.

Market outlook

The impact of COVID-19 is still being assessed but at this stage it is the main driver of short-term negative macro performance in all our markets. In addition, a lower average oil price in the past 4 months has negatively impacted Nigeria's ability to clear USD FX demand in particular. Overall, we have focused on business models that are either essential or innovative (e.g. Fawry in Egypt) and that can meet our minimum quality criteria. **Nigeria** – Nigeria's outlook remains particularly murky with the twin negatives of COVID-19 and oil. We have revised our previously constructive view on recovery, albeit slow, to negative. The allocation to Nigeria is lower for the time being. Three catalysts will change our view to a more positive stance: 1) full devaluation of the NGN 2) normalisation of the local bond market and 3) Dangote's mega-project fuel refinery coming online. The underlying portfolio companies are very robust in a tough environment. **Egypt/Morocco** – Egypt and Morocco will see some pressure from lower tourism on consumer demand but we expect the overall impact on macro to be relatively muted. In addition, the businesses we have selected are hedged against lower consumer demand. We are therefore comfortable holding larger positions here. **Kenya** – Our view on Kenya is more negative for 2020 but we have not altered our relatively positive medium term outlook. We expect investments here to remain robust and rebound strongly as the economy recovers. **Mauritius** – Mauritius is very dependent on the timing of large scale tourism recovery. Unless tourism comes back strongly in 2021, the macro and MCB will be under pressure.