INTO AFRICA

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X-RAY ON AFRICA'S FUNDAMENTALS

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During these difficult times, we wish you and your loved ones health, happiness and brighter days ahead. Welcome to the March/April 2020 edition of *INTO AFRICA*, a publication written by the professionals, for professionals, investors, policymakers … We Advance and provide fresh insights into Africa's emerging markets through renowned thought leadership and peer-to-peer knowledge-sharing. This edition is titled: ***"X-Ray on Africa's Fundamentals".***

Looking at the economic and market outlook for 2020 just a few months ago, there is no doubt times have changed. The spread of the coronavirus (COVID-19) dealt a severe, unexpected shock that impacted people and markets around the globe.

As efforts to stem the spread of COVID-19 continue, uncertainty remains high across global financial markets. The pandemic-driven selloff, heightened by turmoil in global oil markets, is unprecedented in its speed and severity. Volatility and correlations across asset classes are reminiscent of the global financial crisis, as investors seek to reduce risk exposure as new information is released daily. The purposeful halting of the global economy is jarring in the short term and raises questions about the pace and timing of the eventual recovery. The debate has now moved on from whether there will be a recession in 2020, to how deep and long it will be. As markets have moved to reflect this new reality, the unprecedented global coordinated response by scientists, technologists and engineers, working in parallel on a vaccine and therapeutic treatment will lead us past this crisis.

The coronavirus pandemic continues to take its toll on the African continent. While the continent as a whole still accounts for relatively few deaths from the disease, the numbers are rising. As countries scramble to contain the virus and are affected by the efforts of other countries to do the same—the economic impacts grow. Growth in Sub-Saharan Africa has been significantly impacted and is forecast to fall sharply from 2.4% in 2019 to -2.1 to -5.1% in 2020, the first recession in the region over the past 25 years, according to the latest Africa's Pulse, the World Bank's twice-yearly economic update for the region.

Many African countries are opting for a combination of emergency fiscal and monetary policy actions with many central banks in the continent taking important actions like cutting interest rates and providing extraordinary liquidity assistance. However, it is important to ensure that fiscal policy builds in space for social protection interventions, especially targeting workers in the informal sector, and sows the seed for future resilience of the economies. The immediate measures are important but there is no doubt there will be need for some sort of debt relief from bilateral creditors to secure the resources urgently needed to fight COVID-19 and to help manage or maintain macroeconomic stability in the region.

The World Bank Group is taking broad, fast action to help developing countries strengthen their pandemic response, increase disease surveillance, improve public health interventions, and help the private sector continue to operate and sustain jobs. It is deploying up to $160 billion in financial support over the next 15 months to help countries protect the poor and vulnerable, support businesses, and bolster economic recovery.

While clearly the scope and reach of the coronavirus crisis are unprecedented, we should keep in mind, though, that the world has weathered many crises in the past: world wars, widespread famines and deadly viruses. Humanity has emerged from these turbulent periods, not without cost, but often stronger for it. Thus, in the world of finance, rather than allow panic to dictate our path, we should dispassionately ask, what do we do now?

Africa's investment fundamentals are unshaken. Although the current COVID-19 impacts might paint a dull picture of investment prospects on the continent overall. However, over the long-term, the potential for good returns still looks bright, suggesting an opportunity for counter-cyclical investors.

Tunde Akodu

Editor

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ARE AFRICA'S INVESTMENT FUNDAMENTALS
THREATENED OR UNSHAKEN?

By **Gilbert Anyetei,** Associate in RisCura's Alternative Investment Services team

The findings in the latest **Bright Africa** report from RisCura might paint a dull picture of investment prospects on the continent overall. However, over the long-term, the potential for good returns still looks bright, suggesting an opportunity for countercyclical investors.

Such investors do best when they look through markets to identify specific, regional opportunities. In Africa's case, it's important to start by discarding the idea that the continent is a single investment destination with a homogenous potential for reward.

Bright Africa segments Africa into 'meaningful markets' by analysing cultural and linguistic connections, interconnectivity through trade blocs, sharing of expertise, good business relations, and relative ease of transportation, among others.

We identified **nine meaningful markets**, each with its own attractions, flaws, cultural differences and business practices. Given their sizes and unique circumstances, some of these are single countries, such as Nigeria and South Africa while others are groupings of countries united by common histories and language, established trade relations and geographic proximity.

Limited Exports

A healthy balance of trade is crucial to the success of any country, or region. More exports mean increased economic activities that lead to higher employment rates. Proceeds from exports represent a flow of funds into the country, which stimulates consumer spending and contributes to economic growth.

In Africa, however, exports are significantly concentrated in extractives. As such the continent continues to feel the adverse impact of the commodity cycle with total exports (mostly extractive commodities) decreasing from 2014 to 2018 by 21% in USD terms.

Fortunately, across all African countries, GDP output is far more diversified than exports. This has served as a mitigating factor against the impact of the commodity cycle in recent years.

Currently, trade within Africa remains poor, as two-thirds of African imports come from Europe and Asia, whereas intra-continental trade is a mere 13% of all African imports. The poor inter -connectivity amongst African nations is one of the obstacles that the continent faces. Building up trade within the continent is an important strategy, one that the African Continental Free Trade Agreement (AfCFTA) seeks to bolster. The agreement was signed by 44 countries in March 2018 and has the potential to boost the continent's global connectedness, especially as additional countries continue to join the agreement.

Infrastructure Issues

Weak transport infrastructure has long been an issue for African trade, contributing to the continent's low level of competitiveness. The World Bank Forum estimates that road networks carry USD 200bn of trade in Africa – approximately less than 10% of total GDP on the continent.

The road network density is much lower in Africa than in other regions. The African highway network has many missing links and sections remain unpaved or require substantial repair, and some areas are considered to have serious safety concerns. These conditions are partially caused and further exacerbated by the sheer size of the continent and the resulting large distances between cities.

The continent's railway conditions are equally poor. Colonial powers each built different railway networks in different countries that do not necessarily link up, which makes it difficult for countries to move goods between them.

Intra-national trade costs are high in many countries in Africa. Costs are incurred both when transporting goods over long distances, and when clearing goods at harbours or border controls. Doing Business measures the time and cost (excluding tariffs) associated with three sets of procedures documentary compliance, border compliance and domestic transport within the overall process of exporting or importing a shipment of goods. The most recent round of data collection for the project was completed in May 2018. Sub-Saharan Africa ranked last out of all global regions, with a border compliance time of 97.3 hours, compared to the much more favourable 58 hours of North Africa. The total cost to import 15 metric tons of containerised auto parts was a staggering USD 605.8 USD; where North Africa's cost to import was USD 442.4.

The cost of moving goods domestically can also be up to five times higher in Africa than in the US. According to RMB's "Where to invest in Africa" 2019 publication, the estimated cost of transportation in Africa is around 50% - 175% higher than other parts of the world. Data from the UN Economic Commission for Africa (UNECA) has estimated that removing the high border tariffs between African nations could increase intra-African trade by 52% in less than five years.

AfCFTA seeks to tackle these infrastructure and other challenges facing trade within Africa. The launch of its 'operational phase' in July 2019 should begin to enable investment opportunities in transport infrastructure and cross border trade. The start of trading under the agreement is scheduled for 1 July 2020.

Imports

East Asia and Western Europe remain the continent's most significant import regions, at 26% and 30%, respectively. Overall, African imports have remained relatively consistent with the prior year. However, North African imports from Western Europe decreased from 41% in 2017 to 37% in 2018. This was driven by the shift in imports from Western Europe to the Middle East and East Asia.

East Africa continues to place a far larger reliance on East Asia for its imported goods, making up 37% of the region's total imports. The region also has a much larger exposure to the Middle East and significantly lower exposure to Western Europe than the rest of the continent. This variation is partially the result of geography and cultural ties.

Trade in West Africa remains relatively consistent with 2017 as Western Europe (32%) and East Asia (30%) remain the largest import partners. Southern Africa maintains the largest intra - continental trade, as 23% of imports were from within the sub-Saharan African region. This is mainly due to South Africa exporting to its neighbours in Southern Africa, highlighting the potential for intra-African trade as well as the importance of good transport links. However, South Africa's exports experienced constraints in the latter part of 2018 due to loadshedding, implemented as a result of the country's power supply shortages. The disruption to manufacturing and mining output, coupled with weaker external demand, has hindered further growth.

North Africa's trade with sub-Saharan Africa remains negligible – which can be attributed to, amongst other factors, the poorly developed infrastructure linking sub-Sahara Africa with North Africa.

The difference between regions is due to the large impact of transport costs on import decisions, as well as cultural preferences and relationships established over time. Because most products imported into Africa are sourced from geographically distant locations, the proximity to the import destination makes a big difference in the selection of trade partners. By far the most economical way to get goods to Africa is by sea, meaning that the shortest oceanic voyage becomes the preferred partner, by default.

China remains the continent's top import partner, constituting 16% of all imports; and is the primary import source in 14 African countries for machinery, electronics, vehicles, mineral fuels and cereal. France, Germany and the US made up 15% of all African imports in 2018.

MAURITIUS

INVESTMENT OPPORTUNITIES AND CHALLENGES IN 2020

By **Robin Smither,** Senior Executive/ Head Corporate Banking, AfrAsia Bank

Introduction

Since its independence in 1968, Mauritius has successfully transitioned from a sugar based economy to an innovation-driven and knowledge based economy. Expanding sectors have been agriculture, high-end tourism, smart manufacturing, financial services, ICTs and business process outsourcing, hospitality and property development.

Today, Mauritius is one of Africa's most sought-after destinations for institutional and private investors seeking a politically stable jurisdiction, in addition to being an effective regional financial hub for Africa and Asia. Two key factors have contributed to the attractiveness of the island and drawn investors globally. Mauritius has an investment grade rating of 'Baa1' on the Moody's rating scale, and out of all African countries, it ranks highest on the World Bank's Ease of Doing Business index and Ibrahim Index of African Governance, consolidating its premier position as the investment hub of Africa.

Investment opportunities

Managing the ongoing economic development of Mauritius remains a priority for the country to sustain growth. Mauritius offers businesses the opportunity to invest in a dynamic and potentially rewarding economy and regional centre that provides direct access to the Africa – Asia corridor and beyond. Its first-class infrastructure, and myriad of investment schemes to promote and foster foreign investment makes it a choice destination in which international companies may operate their representative office for the region or to which they may expand business operations. Besides that, it provides highly-trained and skilled personnel, state-of-the-art infrastructure, and telecommunication systems. Mauritius has also established its Investment Promotion Agency, the Economic Development Board (EDB) to provide a secure platform to the global investor community for local and offshore investment. It has also built a viable financial sector with local and international banks which are well placed to support activities of this nature.

Financial Services

Mauritius, as a leading International Financial Centre (IFC), is now an important recipient of investment funds and private wealth. The IFC activities contributed almost 12% to the GDP in 2019, with a growth rate of 5.2%. The island continues to see meaningful investment from a variety of financial institutions abroad and even recorded a 33% increase in direct investment flows during the first three quarters of 2019 as compared to the same period last year. Mauritius plays a pivotal role in facilitating investments with social and environmental impact in Africa. Over 600 funds with an African focus have chosen Mauritius as their structuring platform. However, there is still room to deepen its offering as a sophisticated offshore financial hub catering to a wide range of investor needs.

Real Estate

Mauritius's stature as a migrating destination has never been in doubt. The country has attracted a number of ultra-high net worth individuals (UHNWIs), mainly from France and South Africa, through investments in dedicated up-market real estate associated with residence permits. Mauritius is further looking to positon itself as an attractive location to conduct business alongside high quality of living. The rise in smart cities, business industrial parks, marinas and property development schemes are done with the intention to attract international investors and business. In fact, there are five smart city projects that have obtained certificates for development and six projects which have letters of intent. These initiatives could serve the island well in the medium to long term given the business risks and challenges that plague African countries.

Fintech Hub

A series of regulatory developments is positioning Mauritius as a fintech hub embracing blockchain and other disruptive technology. The Government has recognised that the digital revolution is seen as a means to increase private investment and subsequently employment in the country. The establishment of the Mauritius Africa Fintech Hub aims to position Mauritius as the gateway for investment into and out of other African countries. Likewise, the Financial Services Commission has provided for Securities Token Offerings (STOs) to be issued, as a method of raising funds from investors. A Regulatory Sandbox Licence is also offered as a means of conducting business activities for innovative projects for which there is no (or an inadequate) legal or regulatory framework in the country. Mauritius is ready to attract investments flows for the fintech space and should play a bigger role going forward in the untapped African fintech market.

The Ocean Economy

With 2.3 million km² of exclusive economic zone (EEZ), Mauritius is the 20th country in the world with such a large EEZ. The Government aims to double the contribution to GDP of the ocean economy to 20% in the medium term by increasing the activities of its blue economy. MUR 6 billion are being invested to expand and upgrade the port while a further USD 700 million has been forecasted to capitalize on other sectors such as tourism, seaport and seafood-related activities. Mauritius intends to explore other sectors like aquaculture, maritime services and commerce and renewable energies amongst others. Most of these activities will necessitate the expansion of existing port infrastructure to solidify the island's role as a hub for global trade flows. The number of vessel calls is estimated to double in 2020 and further increase by 41.7% by 2040. Whilst most investments are being funded by the Government until now, following the lead of the European Commission by launching an equity investment for the blue economy, will be a sure way of strategically targeting institutional and private investors.

Challenges

The Government of Mauritius has embarked on multiple infrastructure projects, be it in transport or public services. Albeit a necessity, construction, modernization and maintenance of public infrastructure are very costly. Public sector debt stood at 65.3% of GDP in June 2019 while the international norm is 60%. Development of infrastructure should not lead to excessive public debt, as this could eventually lead to negative economic growth. The International Monetary Fund has already advised the Ministry of Finance to undertake fiscal consolidation.

Mauritius has arguably matured into a respected IFC having adopted best international practices; with sound regulatory and legal frameworks and a conducive business environment. This eventually earned Mauritius a reputation of a reliable jurisdiction as evidenced by growing network of double taxation treaties based on the OECD model. To sustain its development as an IFC of substance, the offshore financial sector needs to move on from plain vanilla services to providing more sophisticated financial offers. This creates a twofold challenge.

Firstly, that such a transition will require a new take on skills development and secondly, Regulatory Bodies of the financial services sector should continuously ensure the integrity of the Mauritius IFC by strengthening the system. Cases involving the proliferation of financial crime or exposing weak controls by the financial services players can instantly deter offshore investors and tarnish the island's reputation. The repercussions will undeniably affect other sectors of the economy. For this reason, the government has been active in implementing several guidelines and laws such as its National Strategy 2019-2022.

Conclusion

Mauritius owes its remarkable economic performance to sound economic governance, steady reforms to sustain long-term growth, a favorable business environment, effective state-business relations, and proactivity of the state in supporting transformation, including attracting foreign investors and gaining access to foreign markets. However, a significant impediment to faster growth and expansion of the new pillars of the economy, could be the unavailability of highly skilled, experienced and specialised personnel at the right time to sustain momentum.

Nevertheless, Mauritius' vision, is placing the island not only as the ideal hub for investment but also a leading example in Africa. Mauritius should be a serious consideration to the global investor community.

Contributor's Profile:

Robin Smither has over 16 years' experience in Corporate and Investment banking with an extensive knowledge in global markets, investment banking and lending products. Robin was with Standard Bank for more than 11 years, spent 3 years in Mauritius as Head of Corporate Banking, followed by some time in South Africa as a senior banker to Standard Bank's large global multinational clients where he developed an extensive knowledge of Africa related banking and business. Robin currently heads up the domestic and international corporate banking activities for the Bank. Robin also acts as a non-executive director on some of the AfrAsia Capital Management investment funds.

KENYA: EQUITY MARKET REVIEW AND PROSPECTS IN 2020

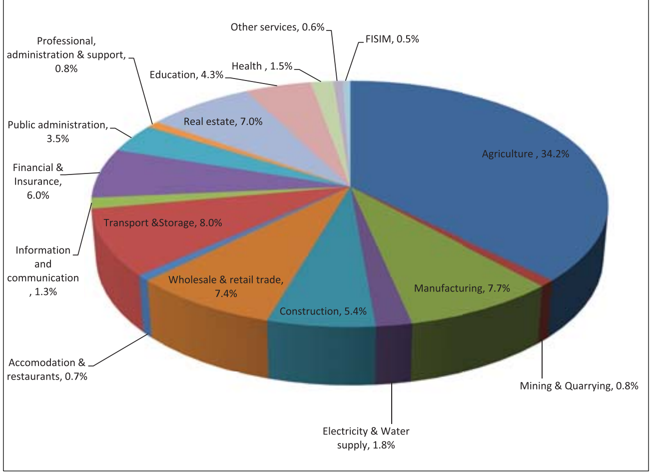
By **Sarah Wanga,** Head of Research, AIB Capital Limited

Earlier this year, Kenya's economy was expected to grow at 5.9% from an estimated growth of 5.5% in 2019. This growth was likely to be supported by:

- Increased private sector credit growth following the removal of interest rate caps.
- Government payments to contractors: It was estimated that delayed government payments to contractors accounted for 30% of the NPLs in the Banking sector.
- Accommodative monetary policy stance.

However, following the outbreak of the corona virus, economic growth, private sector credit growth and consumer demand are expected to decline. Economic growth could decline to as low as 3% in 2020.

Kenya's GDP Composition



The sectors of the economy that are likely to be greatly affected are:

- **Agriculture**: Earnings from tea, coffee and horticultural exports are expected to decline. In the current environment, demand for cut flowers is likely to be subdued and this is expected to continue even after the virus is contained and countries re-open their borders.
- **Manufacturing sector**: Manufacturing activity is likely to reduce as companies reduce production. The sector is also heavily reliant on intermediate goods from China. The disrupted supply chains may reduce the manufacture of some products.
- **Finance and Insurance**: The financial sector is highly integrated with the global economy. It is therefore likely to be negatively affected by global developments as foreign investor outflows increase.

The industry should, however, benefit from technology. Over the past few years, companies in Kenya's financial sector have invested heavily in technology. This will enable them to provide services in the current environment. The government is also encouraging Kenyans to use cashless payment systems. This should benefit banks and Safaricom (M-Pesa).

- Construction and Real Estate: Over the past few years, growth in the sector has declined. The current developments are likely to lead to a further slowdown in the sector.

Key economic indicators:

- **CBK to maintain accommodative monetary policy stance**: In March, Kenya's Central Bank reduced both its CBR (Central Bank Rate) and CRR (cash reserve ratio) by 100bps to 7.25% and 4.25% respectively. Despite these measures, private sector credit growth is expected to remain subdued as banks' appetite for risk is likely to reduce. The government may however, put in place measures that will seek to support businesses that are likely to suffer as a result of the shutdown.
- **Short-term inflationary pressures**: Kenya relies on imports (both intermediate and final goods). In the short-term, there may be a decrease in supply due to the shortage. Demand shocks on consumer staples are also likely to push up prices. As the impact of the initial shock reduces, prices are likely to decrease as lower economic activity in the country is likely to lead to a decrease in demand.
- **The Kenyan shilling is expected to depreciate against the USD**: The shilling is expected to continue to lose ground against the USD as dollar demand outweighs supply. The country's import bill is likely to decrease mainly supported by the lower oil prices
- **Equity Market**: The market has witnessed an increased outflow of funds. Investors are likely to exit the companies that are likely to be affected in the current environment.

Safaricom is likely to attract investor interest as the company is likely to benefit from an increase in the use of it voice, data, fiber, and M-Pesa services. Meanwhile, the banking sector could record an increase in NPL (Non-performing loans) and private sector credit growth is likely to be subdued. The sector, however, remains attractive as the government has put in place measure to support the sector. Revenue growth in the manufacturing sector is likely to be subdued due to reduced consumer demand.

MOROCCO | MARKET EXPECTED TO CONTINUE UPWARD SLOPE IN 2020

By **CFG Bank Research Team, Morocco**

The markets rise in 2019

After having registered a significant drop in 2018 (-8.0%), the CFG 25 index recorded strong growth in 2019 (6.6%). Indeed, after a consolidation phase that spanned from November 2018 to June 2019 over which the market fluctuated depending on the news, good or bad (profit warning amongst other things), and reached a 2019 low on June 12th at 22,810 points, market started a bullish rally that continued until early 2020. This recovery was mainly driven by (i) the positive impact of IAM's secondary public offering, (ii) a further decline in interest rates, (iii) an acceleration in the outsourcing rate of pensions funds' AUM, and (iv) a further normalization of the adjusted corporate earnings growth with expectations standing at +3.2% in 2019E and +4.7% in 2020E (adjusting for the financial penalty imposed by the telecom market regulator on Maroc Telecom of MAD 3.3bn and a MAD 350m provision for impairment made by Managem). Thus, driven by these elements, the CFG 25 index reached a 2019 high on December 12th at 25,634 pts before concluding the year on a 6.6% rise. From a sectorial perspective, 15 of the 25 sectors listed on the Casablanca Stock Exchange stood out recording positive performances. It is worth noting that the telecom and banking sectors' positive performance accounted for almost 70% of overall market gains in 2019.

In addition to share price gains, market liquidity rose sharply with overall trading volume up 23.5% to MAD 57.9bn. Whereas trading volume on the Central Market decreased by 16.1% to MAD 31.2bn, trading volume on the Block Market recorded an impressive 173.8% rise to MAD 26.7bn allowing overall market liquidity to increase over 2019. This rise in trading volume contrasts with a 26.1% volume decrease in 2018 to MAD 46.9bn. As a result, average daily trading volume has risen sharply from MAD 190m over 2018 (with an average daily trading volume of MAD 151m on the Central Market) to MAD 235m (with an average daily trading volume of MAD 127m on the Central Market).

GROWTH EXPECTED TO CONTINUE OVER 2020

In 2020, we expect the upward trend in the equity market to continue with an estimated gain expected between 5% and 10% (vs. +6.6% for the CFG index in 2019). In our opinion, share price gains are likely to be driven by the following two factors.

Interest rates remaining at their currently low levels

In a context of markedly slower economic growth since 2013, with inflation curbed and a substantial reduction in our twin deficits, interest rates have moved sharply lower since 2014 to historically low levels currently. After this major downward move, we believe that rates have reached a point of equilibrium that is likely to persist over the short to medium term. Indeed, a scenario of another cut in the key interest rate seems unlikely over the coming months since (i) the growth rate of loans to the non-financial sector should slightly decrease over 2020E, and (ii) inflation is expected to remain moderate over the medium term in line with Bank-Al-Maghrib's price stability target.

Further normalization of the corporate earnings' growth

After contracting 5 years in a row, listed companies' earnings portrayed strong recovery in 2016 and 2017, rising by 12% each year. This bullish trend was however abruptly stopped in 2018 (-8.3%) due to a number of exogenous factors, such as (i) the boycott campaign that had a direct impact on the net income of Centrale Danone (MAD -538m over FY-2018 vs. MAD +115m over FY-2017) and Oulmès (MAD -+16m over FY-2018 vs. MAD +190m over FY-2017) amongst other companies, as well as, an indirect impact on Total Maroc that was unable to pass on the sharp increase in oil prices to the final customer by fear of retaliation, (ii) a rise in claims in non-life segment that led to a drop in the insurance segment's aggregated earnings, and (iii) the settling of a number of fiscal audits that impacted negatively numerous companies (LafargeHolcim Maroc, Lesieur, Boissons du Maroc, Addoha, Ciments du

Maroc, etc.). This has been coupled with (i) a substantial decrease in the mining sector's earnings due to a fall of commodity prices, as well as, in Imiter mine's ore grade, and (ii) the difficulties that the real estate sector is having (aggregated earnings fell by MAD 266m in FY-2018 as compared to FY-2017) and therefore penalizing the capital goods sector (aggregated earnings fell by MAD 238m in FY-2018 as compared to FY-2017).

We expect this negative trend to continue over FY-2019 mainly due to the financial penalty imposed by the telecom market regulator on Maroc Telecom of MAD 3.3bn. Adjusting for this exceptional item and for a MAD 350m provision for impairment made by Managem following the revaluation of a number of mining assets, corporate earnings would have grown by 3.2% according to our estimates. Consequently, after a 4.0% decrease in H1-2019, we believe that corporate earnings should close the year on a 9.2% counter performance according to our estimates, i.e. down MAD 2,708m as compared to 2018.

In 2020, adjusted corporate earnings are expected to continue growing. Indeed, even if corporate earnings are expected to fall by 9.2% over 2019, adjusted corporate earnings (adjusted for the financial penalty imposed by the telecom market regulator on Maroc Telecom of MAD 3.3bn and a MAD 350m provision for impairment made by Managem) are expected to increase by 3.2% in 2019 and 4.7% in 2020. Therefore, benefitting from the amplifier effect of exceptional costs that will impact 2019E, corporate earnings should experience an 18.9% rise over 2020E. Therefore, in 2020, the corporate earnings growth rate should record a further normalization (+3.2% in 2019 and +4.7% in 2020).

On the negative side, the port industry is expected to register a decline of 20.8% or MAD -128m, due to (i) the return of dry bulk volumes handled by Marsa Maroc to a more normative level, following a good performance in 2019 with exceptional coal and cereals imports, and (ii) the commissioning of trans-shipment activity in Tangier Med II starting H2-2020 that should negatively impact operating margins (low utilization rate over the first months). As for the tourism sector, it is expected to experience a slight MAD -22m drop in earnings over 2020E following the non-renewal of the Sofitel Royal Bay's leasing contract (in Agadir).

However, we believe that the repetition of the 2007 scenario where market's P/E was significantly higher than where it currently stands seems improbable in the short term (more moderate growth, lack of new IPOs). It is worth stressing that adjusted for the financial penalty imposed by the telecom market regulator on Maroc Telecom and the provision for impairment made by Managem, the market's P/E would currently stand at 20.5x 2019E earnings. Given current interest rates, corporate earnings' growth outlook, and the long-term sustainable growth, we believe that the theoretical P/E ratio should stand around 20x. These valuation levels also reflect the low Moroccan institutional investors' exposure to international markets. Indeed, even though insurance companies and pension funds can invest up to 5% of their AUM overseas according to Moroccan law (as part of the foreign exchange regulatory framework), their international exposure do not in fact exceed 2.5%. Therefore, almost all of Moroccan savings are invested either on the local equity market or the local fixed income market, thus driving upwards valuation levels. Consequently, the market should in our opinion continue trading at an adjusted forward- looking P/E of around 20x, hence our belief that the index will continue to appreciate by around 5% to 10%.

Last, we also think it is important to refute the idea that the market is expensive due to the cost of capital being low. Yields currently stand at historically low levels (2.65% for 10-year Treasury bonds), while the market risk premium has come down sharply since Q4-2016 to its current level of 4.9%. It is worth recalling that we calculate this using an ex-ante approach based on a DDM for the entire equity market. We exclude the historical data (ex-post) approach due to the Moroccan market's lack of historical breadth. The latter method is generally considered appropriate for some developed Western markets which have significant historical breadth.

2019 has been an excellent year for all of our preferred stocks. Indeed, between February 2019 and February 2020 our top picks portfolio registered 36.0% Total Shareholder Return versus a 9.5% Total Shareholder Return for the market. Our 2019 top picks portfolio's performance has been driven by the excellent share price performance of HPS (+64.0%), LBV (+47.4%), and to a lesser extent by SBM (+24.2%) and MSA (+23.7%). We approach 2020 with a still condensed list of top picks, comprised of LBV, HPS, SBM, and RIS.

TANZANIA: CAPITAL MARKET REVIEW AND PROSPECTS IN 2020

By **Ombeni N. Uhuru,** Senior Investment Analyst at Tanzania securities Ltd

Economic overview

Tanzania's economy maintained a strong performance in the first three quarters of 2019 with GDP growth averaging at 6.9%. The growth was attributed to public sector investments and strong private sector performance. The main contributors to this growth were construction, agriculture and transport activities.

Annual headline inflation stagnated at 3.8% in December 2019 from the same rate in November after rising 0.2% from 3.6% in October 2019. Headline inflation is expected to remain low and below the medium-term target of 5.0% in the remaining part of fiscal year 2019/20 owing to subdued non-food inflation rate.

Twelve-month inflation rate for food and non-alcoholic beverages remained on an upward trend to 6.3% in December 2019 from 6.1% in November and 5.1% in October 2019. The increase was mainly due to rises in prices of maize grain, maize flour, rice, and beans following increased demand in domestic and regional markets and food shortages in some parts of the country. Likewise, on monthly basis food and non-alcoholic beverages inflation increased to 1.3% in December 2019 from 0.8% in November 2019 compared to 1.1% in December 2018.

Money supply remained robust whereby M3 (extended broad money supply) grew by 9.6% in the year ended December 2019 compared to 4.5% in December 2018. This increase was driven by expansion in foreign assets of the banking system (which grew by 13.2% in December 2019 compared to contraction of 8.3% in December 2018) and growth of credit to the private sector (with 11.1% in December 2019 compared to 4.9% growth in December 2018). M2 (broad money supply) also registered annual growth of 11.8% in December 2019 compared to 3.8% in the year ended December 2018.

Tanzania Equity Market Overview

In Q4 of 2019, the equity market experienced an upward trend spearheaded by increased foreign investors' participation at the bourse. The DSEI, TSI, and IAI closed the quarter up by 6.47%, 2.98%, and 5.19%, respectively. The market activities in terms of volume and turnover were higher in Q3 with the total turnover of TZS 526.91 billion compared to TZS 33.32 billion in Q4 2019 and a total of TZS 560.24 billion in the entire 1H of 2019. This year the market hit key support levels thus implying the market is reverting to upward trends.

Equity market performance in 2019 was highly driven by the appetite of foreign investors for Local stocks and positive expectation on the overall performance of the economy, which drives the market upwards. With the polices and Government efforts to attract foreign investors it’s expected that year 2020 will be glamorous. In January 2020, the market turnover recorded an increase to TZS 45.36 billion which is 2.44 folds of the TZS 18.52 billion recorded in December 2019.

Banking Sector

The banking sector is expected to perform well in the year 2020. Banks both locally listed and cross-listed reported increases in profits.   The two largest banks, CRDB and NMB, posted profits of TZS 120 billion and 148 billion respectively for the year 2019. Before 2019 the sector endured rough pathways that saw heightening NPLs which affected the banks’ balance sheets and interest income hence the overall performance. This doom and gloom period saw a decline in lending activities, pushing banks' excess liquidity into Treasury assets. The expected growth in credit to the private sector following the burgeoning performance will boost bank interest income and will expand their balance sheets. Therefore, this expansion in credit to private sector will have a positive effect on spreads that banks will be making as opposed to current/recent reliance on the Treasury securities whose returns are lower by considerable margins compared to lending. The expected performance supported by the growth in interest income will boost the banks’ profits and hence their attractiveness to investors. CRDB has been the most active counter at the bourse while the NMB counter continues to be one of the least active. If the banking sector maintains the 2019 performance including the decreasing trend in NPLs, we foresee brighter prospects for the industry in 2020.

Industrial and Manufacturing Sector

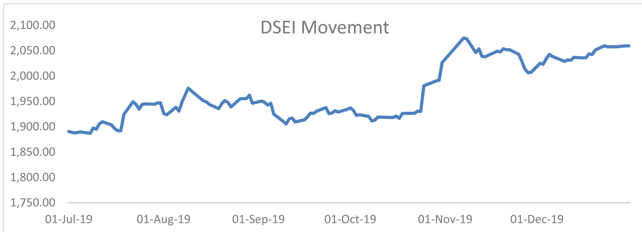
At DSE the following companies are listed under this sector: TCC, TBL and TPCC posting good financial results in the 1Half of 2019. The sector's performance on the stock exchange during the year 2019 remained stable and attractive to both local and foreign investors. With the expected strong economic growth, it's envisaged that in the year 2020 the sector will maintain its good performance. In the market, the TBL counter has remained the top mover in this sector during the year. The largest brewer in Tanzania, TBL recorded a 7% increase in gross profit to TZS 183 billion in 1H 2019 from TZS 170 billion in the similar period of 2018, while operating profit increased by 28% to TZS 114 billion from TZS 89 billion. EPS grew by 14% to TZS 241 per share from TZS 211 per share. TCC's 1H results of 2019 show that revenue grew by 7.8% to TZS 227 billion from TZS 211 billion in the similar period of 2018. Profit after tax increased by 16.8% to TZS 26.6 billion from TZS 22.8 billion in 1Half of 2018, while EPS increased to TZS 267 per share from TZS 229 per share in the 1Half 2018. TPCC has almost 40% market share of the cement industry in the country and is expected to maintain its strong performance at the bourse due to high demand for cement following the government's ongoing infrastructure development activities. Earnings and Dividends are expected to increase which makes TPCC as the stock of choice to many investors with appetite for moderate risk but stable cash flow needs.

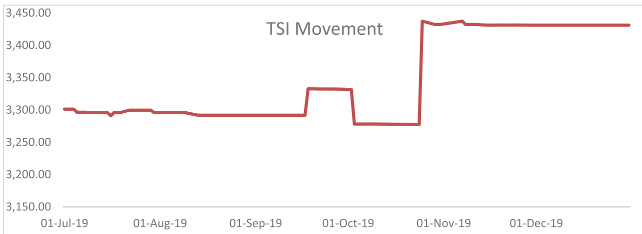
Telecommunication Sector

The telecommunication sector is represented by Vodacom Tanzania Plc at the Dar es salaam stock exchange, for the year ended March 2019 saw a decline in profit to TZS 90 billion from TZS 170 billion in the year ended 2018. Following this faltering in earnings performance, EPS nose-dived to TZS 40.28 per share from TZS 83.81 per share in the same period of 2018. The telecom's main growth driver of service revenue will continue to be M-Pesa based on this line's consistent incremental revenue contribution for the past 4 years. M-Pesa revenue contributed TZS 333.5 billion or about 32.73% of the total service revenue in the financial year ended March 2019. For the coming financial year, we expect the sector's performance to improve given the anticipated listing of other telecommunications companies at the bourse.

Commercial Services Sector

Commercial sector stocks continue to perform moderately represented by Uchumi, Swissport, Precision Air, Kenya Airways and Nation Media Group. Swissport's performance in the 1Half of 2019 was poor, revenue decreased by 34.41% to TZS 17.4 billion and profit dropped by 55% to TZS 2.2 billion. Precision Air decreased its loss to TZS 24 billion in 2019 from TZS 40 billion in 2018. Cross-listed counters such as Kenya Airways, Nation Media Group, and Uchumi Supermarket saw their performance improve in 2019. This indicates that the future of the commercial sector is green from the standpoint of cross-listed stocks. For the locally listed stocks in the commercial sector the future remains uncertain.





Contributor's Profile

Ombeni Uhuru is currently a Senior Investment Analyst at Tanzania Securities Ltd. He previously worked in the Trading and Advisory Departments at TIB Rasilimali Ltd. He has over 3 years' experience in equity, fixed income, Private Equity, and macroeconomic research. He has a bachelor's degree in finance from the University of Dar es Salaam Business School, is an Associate Member of the Chartered Institute for Securities and Investment (CISI), Certified Professional Banker from Tanzania Institute of Bankers and a CFA Candidate of the CFA Institute.

TUNISIA'S EQUITY MARKETS

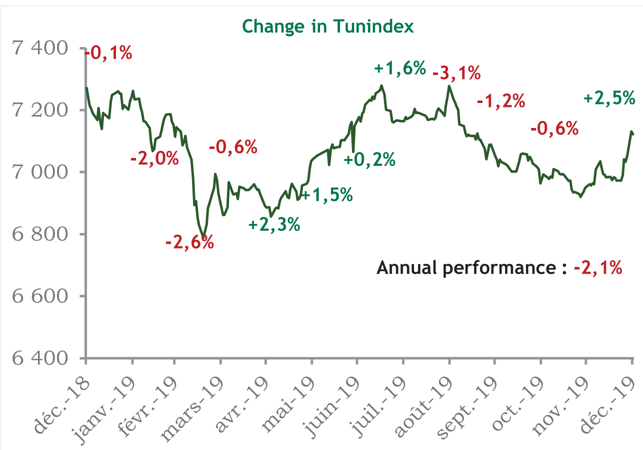
WHERE DO OPPORTUNITIES LIE IN 2020?

By **TUNISIE VALEURS TUNISIA**

Liquidity crunch, slowdown in GDP growth, tightening monetary policy, general elections (Parliament and President), highly fragmented parliament results, endless negotiations between the political parties to form a new government, all these events do not create the ideal environment for investments in equities, which is why the Tunisian Stock Exchange was under pressure at the end of the year.

We know it, financial markets hate uncertainties, but this does not mean that investment opportunities are hard to find, provided we do the right stock picking. We look at stories with solid fundamentals and low risk profile, it will be our mantra in the current shaky environment.

The persistent resilience that we see in the private sector since the start of the 2011 revolution coupled with the low valuation levels that we see in the market make us « reasonably optimistic » about investments in listed stocks. Some names in the market will remain strong despite the turmoil. We nonetheless recommend to take a longer-term view when buying stocks and not to follow the sell-off trend that has recently shaken the market, we see the sell-off as « unjustified » on certain names.



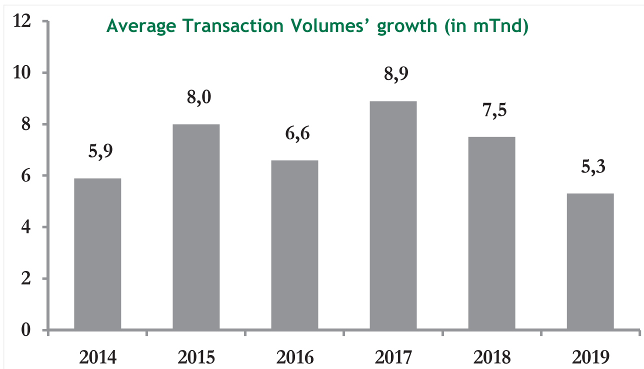
2019 Roundup, where we stand?

The year 2019 was more difficult than expected. The Tunisian stocks have been shaken in 2019 across the board after the big jump they made in 2018. We look at the two main indexes in the Tunisian Stock Exchange: Tunindex and Tunindex 20 both have been under pressure to close the year down respectively 2.1% and 3.7%.

Many factors have contributed to create a bad climate in the exchange: the rising interest rates in the first place creating strong competition from interest bearing securities, then there is the bad political climate characterized by the disappointing results in the general elections or at least that was how investors perceived it.

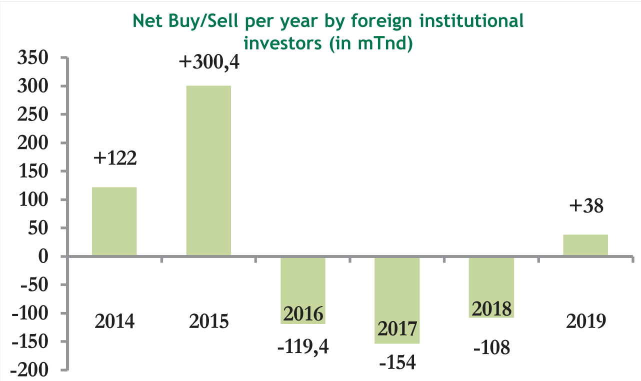
The fast-growing blue chips which have pushed the market's performance in the last few years have all lost steam in 2019. The big caps like SFBT, Poulina, SAH Lilas and Délice Holding have stalled in 2019 although some of them continued to post a strong earnings' growth trend. The banking sector or the market's heavyweight, is still suffering from investors' revulsion despite the much better than expected results that came in a bad business environment.

The Tunisian market's capitalization dropped 3% to stand at 23.7 Billion Tnd, under pressure of stumbling banking stocks.



The year 2019 has also been disappointing by transaction volumes if we compare it with 2018 (completely the opposite) under pressure of shrinking volumes on the big banking caps. The average trading volume per day stood at 5.3mTnd, which means a 30% drop in transaction volumes compared with 2018.

The primary market has reported a lower volume year on year (by volumes of funds raised). Only the rights issues continued to dominate the primary market with five rights issues (although all of them have found difficulties to successfully close their issues). Total funds raised reached 281mTnd, to finance the investment programs of (Land'Or), which reduced debt on the balance sheet, then (SAH Lilas) to create more treasury on the balance sheet then (BNA) to fix the bank's solvency ratio, then two leasing companies (Tunisie Leasing & Factoring and ATL).



Foreign investors have also reduced their volumes although they have been net buyers in 2019 for the first time in four years (Net positive at 38mTnd). Foreign investors are concerned about the Tunisian economy and the capacity of the Tunisian Dinar to resist. Competition from other frontier markets like Egypt didn't help as well.

Which strategy for the coming months?

After long months of technical correction, Tunindex should jitter as investors will not be able to make a decision whether to look at the attractive valuation levels or shy away from stocks because of the uncertainties on the economy. If we look at fundamentals, there is clearly a strong argument to buy stocks (P/E 2020e at 9.4x and an average dividend yield at 3.9% estimated for 2020). Compared with other markets like Morocco for example (P/E 2019e at 19.4x) the Tunisian marketplace is still one of our favorite.

f we look at the listed companies' performance in the first 9 months of 2019, there is clearly a strong signal that the private sector in Tunisia has a tremendous resilience capacity. In average, the listed companies have managed to boost their top line growth +8.5% (first 9 months of 2019). They have also managed to defend their margins despite the rising inflation rate through export channels or in other cases through strong competition to imported goods. They kept their strong fundamentals despite the "painful" liquidity crunch and the sharp rise in the cost of money.

Key figures in the equity market	2016	2017	2018	2019
Market capitalisation (in Billions of Tnd)	19,3	21,9	24,4	23,7
As % of GDP	21%	23%	23%	21%
Number of Listed companies	79	81	82	81
Foreign shareholding	24,5%	23,4%	24,9%	24,7%

The market's heavyweights are trading at extremely attractive multiples which do not reflect their strong growth potential (banks trade at 7.0x their expected earnings for 2019 and 1.1x their book value in 2019).

Valuation ratios	2016	2017	2018	2019
P/E	11,6x	13,1x	10,1x	10,4x
Dividend Yield	3.7%	3.5%	3.8%	3.6%
P/B	1,9x	2,1x	1,9x	1,5x

The year end is still uncertain and could take the stocks on a roller-coaster as long as the political parties are unable to form a new government. More than the power struggle, the negotiations around the 2020 fiscal law will have a direct impact on the market. In the intermediate term we remain optimistic. Our gaze will be fixed on the year 2020 and the possibility for a number of stocks to rebound strongly after they suffered a big sell-off in 2019. It was too much of a correction and a blind selling that did not take into account the strong fundamentals of these companies and the quality of their management. We also look positively at the news that Tunisia has finally managed to make its way out of the blacklist (FATF**) in October 2019 and the good performance of the Tunisian Dinar in the FX market. It is an argument for foreign investors to buy stocks in Tunisia bearing in mind their attractive valuation.

We recommend to cherry pick stocks with robust fundamentals and low risk profile. We also recommend to take a long-term view given the current turmoil that could trigger more sell off in the short term. Two years is a minimum investment horizon in our opinion.

ASSESSING THE OUTLOOK FOR SUB-SAHARAN AFRICAN LOCAL MARKETS

By **Samir Gadio,** Head, Africa Strategy, Standard Chartered Bank

EM local markets started 2020 on a stronger note as global investors' risk-taking improved after a more cautious stance last year. But the spread of the coronavirus resulted in a bout of risk aversion in late January, pausing this positive momentum. Risk conditions could still stabilise if investors expect further policy stimulus from China, accommodative global central bank policies for longer, and possible OPEC+ production cuts. That said, new episodes of market bearishness cannot be ruled out if growth data from China disappoints, global demand (or perceptions thereof) weakens further, commodity prices remain subdued or, more worryingly, the coronavirus outbreak spreads widely to other countries.

A weaker USD may be key to anchoring positioning in EM bonds and carry trades this year. Yet the USD has remained sticky as modest depreciation in late Q4-2019 – driven by expectations of the US-China 'phase one' trade deal signed on 15 January – has receded. A potential US growth slowdown and further Fed rate cuts could anchor a weaker bias for the USD, but recent economic data has been stronger. Sluggish growth dynamics in other G10 countries – especially core emerging markets such as China – and negative headlines on the coronavirus may still position the USD as a safe-haven currency.

Flows into EM local-currency debt funds remained positive until late January, despite redemptions in the first week of February, as risk conditions turned less supportive. In Sub-Saharan Africa, the initial rebound in portfolio flows into core markets (Nigeria, Ghana, Kenya and Uganda) has also faded since late January.

South Africa is the main exception, as portfolio inflows were still rising moderately as of early February. Investors appeared to be positioning for the budget reading on 26 February and taking advantage of a steep curve after recent SARB easing, despite increasing pressure on the South African rand (ZAR). With long-dated South African Government Bonds (SAGBs) still trading above 10%, the market will be on the lookout for tactical duration opportunities. A potentially better budget reading for FY21 (ends March 2021), and recent headlines suggesting that the authorities may consider a special-purpose vehicle (SPV) to take a large portion of Eskom's debt off-balance-sheet, may prevent a Moody's downgrade on 27 March and exclusion from the World Government Bond Index.

In this scenario, the long end of the curve could flatten temporarily. Portfolio flows may also be supported by cheaper USD-ZAR entry points in recent weeks, along with SAGB underperformance versus EM bonds since 2019 and robust CPI -adjusted yields onshore. That said, long-dated SAGB gains may prove tactical, as concerns about weak growth, supply, medium-term fiscal and public debt dynamics, and ratings could re-emerge.

In Nigeria, open-market operation (OMO) bills offer decent carry, but better levels are needed to attract portfolio inflows amid lower oil prices, weaker EM risk sentiment, and FX pressure since late January. Foreign buying of OMO bills restarted in early January, but has reversed recently amid large maturities in February. The Central Bank of Nigeria's (CBN)'s interest rate reaction function to lower oil prices and Nigerian naira (NGN) weakness appears to have changed, as OMO bill yields have trended marginally lower in recent sales while the CBN only partly rolled over maturities. The central bank's focus seems to have shifted to lowering interest costs and reducing the OMO bill stock. At the same time, the gradual decline in OMO bill yields and the 500bps hike in the cash reserve requirement to 27.5% at the 24 January MPC suggest that the CBN wants to avoid a disorderly move lower in OMO rates in response to excess liquidity.

The CBN will likely seek to minimise NGN volatility, despite lower oil prices, but it could allow spot fluctuations within a tolerable range. The recent bout of FX pressure is unlikely to result in major NGN devaluation unless oil prices drop sharply and stay depressed for a prolonged period, as occurred after the 2008 and 2014 oil price shocks. While FX reserves have resumed their downtrend, the CBN still has enough ammunition to step up FX supply and contain offshore and domestic USD demand. Although the CBN has not shown signs of reversing its OMO yield stance so far, it allowed the NGN futures curve to re-price lower by NGN c.2 on 29 January. Further NGN futures curve discounting could prove to be a cheaper and less controversial way to boost returns on local debt for offshore investors, relative to an outright increase in OMO bill rates.

Meanwhile, the ban of local non-bank investors from the OMO market has resulted in demand-supply mismatches and an excessive rally in Federal Government of Nigeria (FGN) debt securities. Unattractive short-dated FGN and money-market rates have supported institutional investor demand for less liquid assets such as promissory notes, commercial paper and selected state bonds, but their availability is limited; equities could be an alternative, but stock-market traded volumes remain modest. More importantly, the local bid for longer-dated FGN bonds has increased materially, as evidenced by the substantial oversubscription of the 30Y (and 10Y) tenors at the 22 January bond auction. Bond yields would have fallen further in the absence of auction overallotment by the Debt Management Office. The low yield environment for non-OMO securities should make it easier for the authorities to raise domestic financing, possibly even for infrastructure projects, but could increase medium-term FX risks by eroding the incentive to hold NGN assets.

In Ghana, bond yields above 20% on the bid still look nominally attractive, despite a c.100-140bps retracement lower in recent weeks. Some foreign investors may see an opportunity to get involved in local bonds, accrue high-yielding carry, and possibly lighten positions before the December elections. They may also expect that fiscal slippage to be more moderate in 2020 than in previous election cycles, while the authorities are likely to support the Ghanaian cedi (GHS) given the political cost of a weaker currency in an election year. This market positioning appeared to gather pace in early 2020, before EM risk conditions turned less supportive amid the spread of the coronavirus. In addition, real rates are robust given contained inflation; this could still support a Bank of Ghana (BoG) cut from 16% after an on-hold decision on 31 January. Tactical bond positions could be constrained by from richer spot (c.5.45) entry levels following the GHS recovery since late 2019, which was driven by increased BoG FX sales and improved FX market expectations before the recent external issuance. This followed a c.13% GHS depreciation against the USD in 2019; if replicated in 2020, this would result in single-digit bond returns in USD terms and provide a limited buffer in case of market pressure.

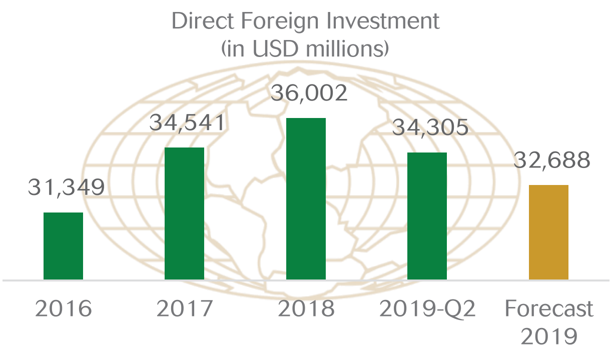
In Kenya, we are constructive on infrastructure bonds given their low-volatility carry, but yields may be bottoming out after a rally. The October 2035 bond traded at c.11.0% as of early February, versus c.11.8% in late November. Global risk-on conditions before the coronavirus outbreak had supported portfolio flows into infra bonds and, subsequently, some yield compression within a multi-month narrow range. Portfolio inflows could pick up again as virus fears eventually ease. Moreover, if the government makes progress on fiscal consolidation and the Central Bank of Kenya remains accommodative, infra bond yields could trend lower again. However, a new infra bond issuance later his quarter may cause rates to rise temporarily, providing better re-entry levels in the primary market. The investment case for Kenya's infra bonds should be supported by contained inflation, manageable supply risk for the rest of FY20 (ends June 2020), and especially Kenyan shilling (KES) resilience. February is likely to be a strong month for the KES given seasonal horticulture flows, while corporate FX demand is still moderate and the current account position has improved noticeably. That said, dividend payments in Q2 could put pressure on the KES.

Finally, fixed income rates in Uganda may resume their earlier uptrend, as portfolio flows could fade in a more bearish external risk environment. Prior to this, large foreign demand at the 22 January bond auction – especially in the 10Y tenor – had reversed yield upside. Concerns about an upward revision to the domestic issuance target for FY20 (ends June 2020) ahead of a supplementary budget could now push bond yields higher, along with broader fiscal risks ahead of the February 2021 elections. The flat bond curve may steepen, as the authorities seem to be allocating more supply to longer tenors. The Bank of Uganda's dovish monetary stance could moderate these risks amid low inflation, but it may be tempted to tighten policy in H2 if economic conditions turn more uncertain before the elections, weighing on the Ugandan shilling (UGX). In the meantime, UGX stability could be temporarily tested in June, which is generally a weak month for the currency amid dividend payments and public spending before the end of the fiscal year.

ZAMBIA'S EQUITY GOLD MINE

By **Jeremy Alexander Mwafulilwa,** Senior Analyst, Pangaea Securities Limited

Zambia presents an ideal location for strategic investors looking for a destination that has links to multiple countries through regional and physical connections. It is strategically located allowing the country to be integrated into regional markets. Although it's geographical advantages, there has



Source: Bank of Zambia & Pangaea Forecasts

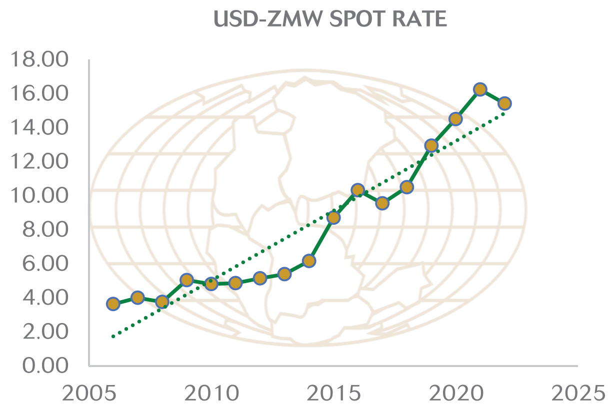
been a decline in direct foreign investment, as indicated in the graph above. This is directly attributed to the negative market signals emitted into the Zambian investment ecosystem, which have impacted Zambia's asset ratings. Standard & Poor's credit rating for Zambia currently stands at CCC with a negative outlook which can be attributed to Zambia being vulnerable to nonpayment of upcoming commercial debt obligations.

Zambia's debt burden partnered with its depleting foreign exchange reserves has created a sense of dread in the market, causing foreign investors to retreat, draining the country of much needed foreign currency.

The Silver lining

The Capital Market in Zambia has been in existence for 25 years with high value listed companies that are selling below real market value due to a lack of confidence in the viability of actualizing a return in the current environment. This year, the sellers' market is higher than the buyers' market – the disequilibrium creates an opportunity for buyers to dictate share prices, buying below real value. The imbalance has been caused by a depreciating and fluctuating currency, with historical trends suggesting stability immediately after the election year, we expect a considerable outflow and inflow of investors – at such a time, share prices tend to move towards real value, creating a premium for the early movers.

The Zambian Kwacha depreciated by 15.15% for



Source: Bank of Zambia & Pangaea Forecasts

the 2019 calendar year. The depreciation of the currency was largely on account of increased demand for debt service payments which are dollar-denominated, energy imports and the strengthening of the US$. This presents a silver lining as some high-performance equities are currently undervalued and cost under $1. Despite the erosion of value from the kwacha, these equities present a unique opportunity for exponential returns.

Copperbelt Energy Corporation

LuSE Ticker	CECZ
LuSE Price, In ZMW	1.22
PE	2.5
LuSE Price in USD	0.083
Fully Diluted Shares	1,625,000,597
LuSE Market Cap, in K [Fully Diluted]	1,982,500,728
Market Cap in USD [Fully Diluted]	134,863,995

Copperbelt Energy Corporation ("CEC") is a power utility company operating in Zambia and Democratic Republic of Congo ('DRC") which provides investors on the Lusaka Securities Exchange ("LuSE"), with exposure to foreign currency (US$) yields. CEC principally operates in power generation, transmission, distribution and supply business, primarily servicing the mining companies in Zambia and the DRC.

Glaring competitive advantage and efficient signal of a businesses ability to thrive in a challenging operating environment in Zambia is its ability to generate revenues in foreign currency, US$ to be specific. This allows the business to hedge against the constant depreciation of the Zambian Kwacha. despite CEC being the most actively traded share on the LuSE, its market cap is currently trading at a significant discount to its net asset value. This is due to the uncertainty that arose from the company's bulk supply agreement with ZESCO. ZESCO is the most significant player in the Zambian power generation, distribution, and transmission sectors. CEC supplies electricity to the majority of Zambian mining operations by purchasing power from ZESCO under a 20-year bulk supply agreement (BSA). The power purchased from ZESCO and sold to the mines is the most significant contributor to CEC's revenue. The BSA is currently being negotiated between ZESCO and CEC as it is due for renewal in 2020. There is currently some degree of uncertainty on its renewal and what form the new agreement will take. It's also worth noting, however, that ZESCO benefits from this as CEC is a source of US Dollar revenues and ZESCO lacks the infrastructure it depends on CEC for.

An equity perspective CEC, valued at 8.3¢ per share is severely underpriced at PE of 2.5. An incentive for prospective investors is the cashflows benefits of owning a stake in CEC. CEC pays a consistent dividend annually with dividend yields going up to 17.8% as of the 2019 financial year.

zanaco Zambia National Commercial Bank

LuSE Ticker	ZNCO
LuSE Price, In K	0.49
P/E	3.06
LuSE Price, In USD	0.030
Fully diluted shares	1,443,750,531
LuSE Market Cap, in K [Fully Diluted]	707,437,760
Market Cap in USD [Fully Diluted]	48,454,641

Zambia National Commercial Bank ("Zanaco") is one of the biggest commercial banks in the country with the second largest branch network in Zambia with 66 branches around the country. Zanaco has a strong deposit base with approximately $ 662 million in deposits as of 2019 and boasts the second highest market share on deposits. Zanaco also has a loan book of $335 million with the 3rd largest loan book in the market.

Zanaco cements itself as a resilient player in the equities market as it has maintained its position as a people's bank by being able to generate significant interest income in an ecosystem that is plagued by a lack of liquidity.

From an equity perspective, Zanaco has strong fundamentals that prove its viability as a high performing asset. With an ROAE in 2019 at 23%, it has the potential to provide immense value to share holder. The security is priced at 3¢ with a PE OF 3.06. For measure, Zanaco's loan book alone is significantly larger than its market cap. This is a clear indication of the disproportionality in the equities market.

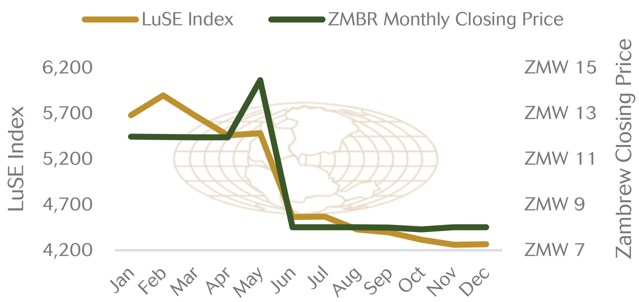
One of the best performing shares on the LuSE,

Zambian Breweries Plc

LuSE Ticker	ZABR
LuSE Price, In K	8.00
P/E	3.06
LuSE Price, In USD	0.544
Fully diluted shares	546,000,000
LuSE Market Cap,	4,368,000,000
Market Cap in USD [Fully Diluted]	297,142,857

Zambian Breweries Plc ("Zambrew") is an index mover. As for the past year, Activity around the security has been significant enough to map the trends of the index.

The Euromonitor Report of 2018 ranked Zambia as



country with the highest per capita consumption of alcohol in the sub-Saharan region. Zambrew are strategically placed capturing significant market share within the region. In 2018 alone Zambrew generated ZMW1.8 billion ($180.2 million) on alcoholic drinks alone.

As one of the only manufacturing businesses in Zambia, Zambrew is not affected by the depreciation of the Kwacha as principle products are manufactured in Zambia. Although, Despite Zambrew facing anticipated inflationary cost increments, we expect Zambrew shares to continue in their path of dominance based on their current strategy of targeting a growing middle class.

Zambrew shares are priced at 54¢ with a PE ratio of 3.06. As a market leader in the beverage industry in Zambia, Zambrew stands to capitalize on the growing population and leverage its market share to create value for shareholders.

Puma Energy Zambia Plc

LuSE Ticker	PUMA
LuSE Price, In ZMW	0.98
PE	4.30
LuSE Price in USD	0.066
Fully Diluted Shares	500,000,000
LuSE Market Cap, in K [Fully Diluted]	490,000,000
Market Cap in USD [Fully Diluted]	33,108,108

Puma Energy Zambia Plc ("Puma") markets and distributes petroleum products and lubricants. Puma energy is a subsidiary of Puma Energy International BV; a global energy business with integrated midstream and downstream operations in 50 countries across five continents.
Similar with CEC, the 6.6¢ indicates that PUMA stocks are extremely underpriced. The company's PE is at 4.30. Puma generates revenue in US$, with majority of the sales generated from long-term contracts with the mines, construction companies, Non-Governmental Organizations ("NGO") and the aviation companies.

Conclusion

Risk aversion has never been the African investors forte and what may seem to be a hazard for the masses is an opportunity for the bold. The equities market in Zambia is ripe with opportunity and the first movers will be rewarded in the medium to long term horizon.

Contributor's Profile

Jeremy Mwafulilwa is experienced in Investment, Finance and Business Development with work experience doing analytical work in both Malaysia and Zambia. Jeremy has been exposed to a wide range of industries and cultures enabling him analyze complex financial processes inherent to Investment Analysis. He holds a First-Class Honours Degree in Actuarial Sciences and Finance.

FINANCE ACT, 2020: IMPACT ON DOING BUSINESS IN NIGERIA

By **Chinedu Ezomike,** Partner & Head, Commercial Practice, Andersen Tax, Nigeria

Introduction

On 13 January 2020, President Muhammadu Buhari signed the Finance Act, 2020 (the Act) into law. The Act is aimed at promoting fiscal equity and aligning local laws with global best practices. It also introduced tax incentives for investments in infrastructure and the capital market and for small businesses. More importantly, the Act is targeted at raising additional revenue for the Government through the introduction of new fiscal measures, including the increase in Value Added Tax (VAT) rate from 5% to 7.5%.

The introduction of the Act is the first major overhaul of the Nigerian tax system in more than a decade and there has been a lot of discourse on its impact on the Nigerian business environment. In 2019, the World Bank ranked Nigeria 131st out of 190 Countries on its ease of doing business index and 159th on the specific area of ease of paying taxes. There is clearly a need for improvement in these rankings as they are important indices that influence growth and development of national economies.

We have set out below a brief analysis of some provisions of the Finance Act and their potential impact on doing business in Nigeria.

Tax Exemption for Small Businesses

Based on the Act, small companies which are defined as those with gross turnover of less than ₦25 million in a year, are now exempt from income taxes. Also, medium-sized companies which are defined as those with turnover of between ₦25million and ₦100million, now have their income tax rate reduced from 30% to 20%. The Act also introduces a VAT compliance threshold of ₦25 million in annual taxable supplies. This means that small companies are exempted from the VAT compliance burden. This is a significant relief for many small businesses which will no longer have to deploy resources in paying income taxes and filing monthly VAT returns. Such companies will be able to invest the additional resources in their businesses.

Incentives for Agricultural Sector

Companies engaged in agricultural production are now eligible to an initial tax-free period of five years which may be renewed for an additional three years, subject to satisfactory performance of the business. This is a significant incentive for companies investing in the agricultural sector and this should see investments pour into small, medium and large companies in the sector, if properly harnessed.

Removal of the Commencement Rule Provision

There was a requirement for new companies to prepare the tax returns of their first three tax years under a commencement rule provision. Under this provision, there was a risk that the basis period of some of the tax years would overlap or even coincide, thereby exposing the profits to tax, more than once. This provision has now been removed under the Act and new businesses are required to be taxed on their profits for the actual accounting periods during commencement. This will potentially reduce the tax exposure of the companies during commencement periods.

Basis for Minimum Tax Computation

A new basis for minimum tax computation was introduced as 0.5% of gross turnover. This replaces the previous basis of computation that sought to tax companies' capital and exempted companies with at least 25% imported equity. The new provision for minimum tax computation will ensure that only companies that generate income from operating activities will be subject to the minimum tax provisions.

Companies with less than ₦25million in turnover are exempt from the minimum tax and the percentage of imported equity is no longer a consideration. Companies involved in agricultural businesses and companies in their first four years of operation are also exempt from the minimum tax provisions.

Excess Dividend Tax

Section 19 of the Income Tax Act is an anti- avoidance provision to the effect that where a company distributes dividend in a year where it has no taxable profit or the dividend distributed is more than the taxable profit, the dividend amount can be substituted as the taxable profit for the year. This was referred to as the Excess Dividend Tax. This provision was interpreted broadly and applied even where the dividend was distributed from retained earnings, which had already suffered tax. This was a major sticking point for local and foreign investors and was subject to multiple litigations.

The Act has amended the Section 19 provisions to exclude dividends distributed from retained earnings, franked investment income, tax exempt profits and Real Estate Investment Companies. This is a major relief to shareholders as it eliminates the double taxation occasioned by the old provisions and now incentivizes distribution of dividends from retained earnings.

Taxation of the Digital Economy

Digital services, which are completely rendered from offshore to a Nigerian resident may now be taxed in Nigeria, if it is determined that the service provider (foreign company) has a significant economic presence in Nigeria. This was not the case previously as non-resident companies were required to have a fixed base in Nigeria to establish a taxable presence. This new provision in the Act is in line with current global approach for taxing e-commerce businesses. This is an evidence that the Nigerian tax landscape is being aligned to reflect global best practices in emerging sectors of the economy.

Restriction on Interest Deductible from Related Party Foreign Loans

Although Nigeria does not have a thin capitalization rule, the Act has introduced, for the first time, a restriction on related party interest deduction. This limits deductible interest paid by Nigerian companies on loans from related party foreign lenders to a maximum of 30% of Earnings before Interest, Tax, Depreciation and Amortization. Any excess interest is allowed to be carried forward for five years. This is aimed at moderating the debt to equity ratio of companies and ensuring that investors have the right mix of investment portfolio. The risk here is that leveraged companies will ultimately have to absorb such interest expense, where they have been unable to offset within five years.

Taxation of Insurance Companies

Insurance companies in Nigeria have hitherto been taxed unfairly. There were provisions in the income tax law restricting their claim of expenses including unexpired risks, imposing a special minimum tax regime on them and restricting their ability to carry forward their tax losses to four years. This had stifled growth in the industry and made it unattractive from a tax perspective. The Act has now resolved these issues by removing those provisions from the law such that insurance companies are now taxed like other companies. This is a welcome development and a reprieve for the sector, especially in the light of the increased capitalization requirements for insurance companies. It is hoped that these amendments will encourage investments into the sector.

Conclusion

The Nigerian Government has made conscious efforts to improve the business environment by ensuring a holistic amendment of tax laws in the Finance Act, 2020. It is hoped that the implementation of the Act will be done in a manner that allows companies enjoy the maximum benefits of the changes and demonstrate the Government's commitment to improving the ease of doing business in Nigeria.

The Federal Ministry of Finance is expected to issue the required guidelines as may be necessary to provide clarity and certainty on any grey areas. This will aid implementation of the Act as a pro-business and investment legislation.

Contributor's Profile:

Chinedu Ezomike is the Partner & Head of the Commercial Practice Group at Andersen Tax in Nigeria. He has 11 years' experience in the provision of Professional Tax & Regulatory Services to clients in various industries.

He started his Professional Services career with KPMG, where he rose to the post of Senior Manager before joining Andersen Tax. He works with clients to define and develop tax strategies and solutions, helping them optimize tax processes.

His tax and regulatory experience covers corporate tax planning, tax due diligence, tax advisory and compliance for local and multinational companies in various industries. He has advised several companies on income tax issues, indirect tax management, corporate tax structuring and regulatory compliance.

Chinedu has led several advocacy efforts aimed at improving the tax environment in Nigeria and has also worked with several companies in resolving tax disputes with various tax authorities.
He has been involved in capacity building for both client personnel and revenue officials and has written and published several tax related articles both locally and internationally. He also serves as a resource person at the Enterprise Development Centre of the Lagos Business School (LBS).

ROLE OF REGIONAL FINANCIAL INTEGRATION IN PROMOTING GROWTH, DEVELOPMENT AND POVERTY REDUCTION IN AFRICA

By **Ibrahim Abdullahi Zeidy,** Chief Executive Officer of the COMESA Monetary Institute

Introduction

Regional financial integration refers to a process, market driven and/or institutionalized, that broaden and deepen financial links within the region. At the very least, this process involves eliminating barriers to cross border investments and differentiated treatment of foreign investors. Further deepening of financial links can take the form of harmonizing national policies, laws, and institutions. Over time, cohesion of regulatory frameworks, operational structures and information systems, and convergence of prices and risk assessment mean that national financial markets within the region effectively function as one. Taking this concept further, a group of countries may set up a regional bond or stock market, distinct from and potentially coexisting with national markets, with the specific intent of pooling resources, risks, and returns. Whatever form they take, Regional Financial Integrations (RFIs) have a certain minimum set of prerequisites: currency convertibility and payment system integration to reduce settlement delays, information and communication infrastructures and removal of legal and regulatory barriers[1].

Most African countries are still at a relatively early stage of development and financial integration is low and global banks have a bigger foot print than regional banks. However, there is a great drive by all major regional integration initiatives in Africa, towards liberalization of inter and intra-regional flow of goods, services and capital which are beneficial for growth. In view of this, many regional organisations in Africa are in the process of being converted to a Common Market with "free movement of goods, services, investment, skilled labour, and freer flow of capital." With the advent of CAFTA there is also scope for further regional trade liberalization, with potentially important benefits for growth, employment and poverty reduction. Typically, enhancing trade integration requires a high degree of financial integration, in order to boost growth, employment, financial inclusion and poverty reduction.

The objective of this paper is to provide requirements for promoting safe RFI in Africa. The paper is organized as follows: Section 1 review benefits of RFI. Section 2, review impediments to and risks from closer financial integration. Section 3 discusses some experiences of financial integration in Africa. Section 4 presents some lessons that could be drawn from successful European experiences in establishing RFI. Section 5 provides generic roadmap for achieving RFI in Africa. Section 6 provides brief conclusion.

1. Benefits of Regional Financial Integration (RFI)

In theory, financial integration can bring important benefits to a country and a region. African countries financial systems remain for the most part bank centered. Quantifying and valuing the benefits specific to RFI can be extremely difficult. However, several existing regional financial integration initiatives around the world provide direct evidence that such integration can help unleash certain "external" macroeconomic benefits, and at the same time also lead to several "internal" or direct micro benefits. The World Bank publication on "The Guidelines for the Successful Regional Integration of Financial Infrastructure" lists the following potential direct and indirect benefits of RFI:[2]

a) Direct benefits include among others the following:

- Lower user-costs for individuals, businesses and public administrations as end users of the RFI arrangement.
- Lower end to end transaction costs for the financial firms participating in RFI arrangement.
- Improved cross border access and reach to all market participants to financial services, with faster, more reliable and simpler transaction services;
- Improved risk management, greater risk reduction and stronger financial stability resulting from wide spread utilization of

1. John Wakeman-Linn and Smita Wah, "Regional Financial Integration: It's Potential Contribution to Financial Sector Growth and Development in Sub-Saharan Africa" Presentation at the Finance for the 21st Century. High level Seminar organized by the IMF Institute in Collaboration with the Joint Africa Institute, Tunis, Tunisia,
2. Guidelines for the Successful Regional Integration of Financial Infrastructure (Draft), World Bank, September

consistent and up-to-date international policy, legal and technical standards, as well as best practice risk management designs and procedures.

- Help the less financially developed economies to catch up with the more developed ones.
- Spur the development of the financial sector and product innovation.

b) The indirect benefits include among others the following:

- Expansion of trade and investment flows among market participants in the region to enable deeper regional economic and financial integration.
- Attraction of external investment capital to the region, which deepens and broadens regional financial and capital markets.
- Deepening and broadening of regional financial and capital markets.
- Impose greater discipline on governments, banks, and non-bank institutions and make the economy more resilient to shocks.

2. Barriers, Risks and Other Challenges that can prevent Successful RFI

Barriers relate to differences or incompatibilities across the various countries that want to participate in the common regional arrangements. These may cause severe delays or otherwise impair or even impede successful RFI in terms of the efficiency, safety and overall effectiveness of regional solutions. The barriers will need to be addressed as prerequisites of the regional financial integration programme. The key barriers include:[3]

(i) Differences in national legal, regulatory and oversight regimes among member countries. This results in competitive distortions and encourage regulatory arbitrage. The differences also go against efficient group approach towards risk management and make the resolution of cross border financial institutions very difficult.

(ii) Inadequate harmonization of national financial integration operating schemes, rules, and technical standards etc.

(iii) The need to have a clear grasp of the potential contagion and spill over risks brought on by integrated financial markets for example which result from macro-financial linkages. The flipside of financial integration is the risk of negative spillovers and spillbacks, which if left unaddressed, could result systemic risks.

3. Some experiences of Financial Integration in Africa

Pan-African Banks (PABs) are undoubtedly the most defining features of regional financial integration over the past decade in Africa. There has been a rapid expansion of PABs in recent years, with seven major PABs having a presence in at least ten African countries. Three of these are headquartered in Morocco, two in Togo, and each in Nigeria and South Africa. Additional banks primarily from Kenya, Nigeria and South Africa have a regional presence with operations in at least five countries. PABs have a systemic presence in around 36 countries. These banks have been particularly active in syndicated loans, especially in the financing of infrastructure and supporting local markets. Some of the PABs have gone beyond traditional banking activities to embrace operations in capital markets, insurance, pensions, money transfers, and microfinancing.[4]

The growth of PABS, offers a number of opportunities and benefits. The expansion of these banks reflects the increase in economic integration within Africa more generally and is contributing to improve competition, support financial inclusion, and give rise to greater economies of scale. In addition, they have been filling the recent gap left by European banks and are becoming the lead arrangers of syndicated loans.[5]

Apart from the success of PABs, there are several interesting success stories. Kenya has been a world pioneer in mobile banking. Many African countries have also started to use technology to leapfrog traditional paths to financial deepening. The Agence UMOA-Titres (AUT) has played an interesting role in developing the regional sovereign bond market in the WAEMU region. Its role is to assist the member states in their financing operations on the financial market by coordinating securities issuance. It is also responsible for the conduct of auctions, oversight of market conduct, publication of market data, and investor relations. As a result, it has provided governments in the region with a wider market for their securities, and undoubtedly led to the extension of maturities as well as lowering of yields, compared to national issuance.[6]

3. Ibid p.13
4. Charles Enoch, Paul Mathieu and Mauro Mecagni "Pan-African Banking: Opportunities and Challenges for Cross-Border oversight, IMF, 2015 p.1.
5. IMF, "The Financing of Infrastructure in Sub-Saharan Africa: A changing Landscape", in Regional Economic Outlook; Sub-Saharan Africa, Washington DC. October 2014

In WAEMU, since 1998, the Bourse Regionale des Valeurs Mobilieres (BVRM) has served as a regional exchange for trade on stocks and bonds. In WAEMU progress are also made on other fronts of market integration largely through supra-national regulatory laws and bodies. Another important development is the rapid growth of the regional market in local currency debt, especially public debt.[7]

4. Some Lessons from the Experience European Union

EU provides most advanced example of RFI. However, given the stark difference between European and African economies, great care must be taken in trying to apply lessons from EU to Africa. The EU model of RFI has evolved and adopted over decades, and functions in an institutional and economic environment that is in many aspects quite different from that found in most African countries.

The following are some of the lessons that could be drawn for successful experience of European Union in achieving RFI[8]

i) Achieving RFI requires strong political commitment.
ii) It is important to have a clear grasp of the potential contagion and spillover risks brought on by integrated financial markets, as well as transition and operational risks. Once these risks are identified, strong policy frameworks at national and regional levels would need to be put in place to properly manage these risks
iii) RFI would need to be supported by sound institutional legislative frameworks, which include among others the following:
    - The minimum regulatory requirement for entry.
    - Permissible banking activities which are consistent with current stage of member countries development and growth objectives.
    - Regional arrangements for effective cross border banking supervision and regulation.
    - Regional institutions to set standards and rules and to enforce national compliance of regional rules.
iv) To have a regional approach to ensure financial stability;
v) The need for regional macro-financial surveillance mechanisms.

5. Generic Roadmap for Achieving Regional Financial Integration

According to AfDB publication on Financial Sector Integration in three regions of Africa, Roadmap for RFI have the following five stages:[9]

(a) Stage I-Preparatory stage: In this stage countries need to fulfil certain preconditions relating to establishing macroeconomic stability and financial system soundness. In this stage, the main responsibility falls on domestic policy makers to modernize domestic financial system, especially the payment system. At the same time Free Trade Area agreement between member countries should be implemented. Substantial exchange of information and other forms of interaction between the countries would be needed to make them aware of the reforms being undertaken in partner countries.
(b) Stage II- Harmonisation Stage: At this stage, modernization of the financial sector in individual countries would be further extended by the introduction of and compliance with various international standards and practices in the financial sector to ensure regional harmonization. Intraregional exchange controls would need to be abolished. Member countries which already have stock exchanges need to strengthen them Those which does not have need to introduce them. Free Trade arrangements should be effective to enable private financial sector to expand their activities cross border.
(c) Stage III- Cooperation stage. The achievement of harmonization in areas of financial institutions; rules and regulations would lay the foundation for this stage of integration. At this point, countries would cooperate in implementing agreed convergence criteria, to be monitored and evaluated by a regional ministerial council. They would also complete the full harmonization process relating to regulatory, supervisory, and accounting procedures began under stage II, and would cooperate in cross border regulation and supervision activities. Arrangements would also be made to link domestic securities

6. Monfort Mlachila " Regional Financial Integration in Sub-Saharan Africa: Key Note Presentation at the XXVII, Lisbon Meeting of the Central Banks of Portugues Speaking Countries, 9 October 2017, p.8.
7. John Wakeman-Linn and Smita Wah, "Regional Financial Integration: It's Potential Contribution to Financial Sector Growth and Development in Sub-Saharan Africa" Presentation at the Finance for the 21st Century. High level Seminar organized by the IMF Institute in Collaboration with the Joint Africa Institute, Tunis, Tunisia, p11.
8. GeertAlmekinders, Salashi Fukunda, Alex Mourmourus, Jiaping Zho &Yong Sarah Zhou" ASEAN Financial Integration" IMF Working Paper WP/15/34, pp17-18
9. AfDB, Financial Sector Integration in Three Regions of Africa: How Regional Financial Integration Can Support Growth, Development, and Poverty Reduction. 2010, pp14-14-17

markets. Building on the effectiveness of FTA, countries would enter into an agreement to establish a customs union. Legal systems would be reformed to enable cross-border enforceability of contracts. This stage would also see enhanced cooperation in the areas of monetary and exchange rates policies.

(d) Stage IV-Integration Stage: This shifts the focus of action to the regional level. This stage would be characterized by an operational customs union, the effective integration of various financial institutions, and the exercise of regulatory and supervisory functions, including single bank licensing, a single regulatory agency, and increased cross border presence of financial institutions originating in member countries. The core measure in this stage would be a partial pooling of external reserves to meet balance of payment difficulties of member countries, the establishment of regional bond markets, and possibly a unified regional stock exchange. Following the strengthening and linking of national capital markets, new regional financial products, such as regional bonds, would also emerge to tap local savings.

(e) Stage V- Unification/ Monetary Union Stage: this final stage would see the introduction of a common currency and a common central bank on the financial side, and possibly the launching of an economic community on the real side. The operationalization of this stage, especially if accompanied by the creation of an economic community, entails the establishment of concrete institutional arrangements to facilitate the transition from national currencies, exchange rates, and central banks to the unified monetary system. It would involve detailed attention to the supporting institutional set up. Achievement of this stage is not easy-it demands strong political will at the highest levels, a dedicated civil service that believes in regionalism.

The roadmap sketched above involves a number of detailed measures to be implemented at various stages of the integration process. However, each stage also implies one or two core measures that must be undertaken. Thus in stage I, the emphasis is on developing national payment systems. In stage two it is the modernization of the financial system by adopting international banking and other standards, abolition of intraregional exchange controls, liberalizing foreign investment flows, combined with strengthening stock exchanges. Core measures in stage III would include effective implementation (monitoring and evaluation) of convergence criteria, cross-border regulatory and supervisory mechanisms, and linking of national stock exchanges. In stage IV the emphasis would be on unifying stock exchanges, and development of regional financial products such as regional bonds.

6. Conclusions

This paper highlights that increased RFI could boost trade, FDI flows, portfolio investment and cross border banking, and become an important source of growth, employment and more inclusive development, poverty reduction, as well as resilience to shocks for African economies. In fact, financial integration is an important component of ongoing initiatives to create a single market for goods and services in most regional integration arrangements. These indeed calls for regulatory harmonization and strengthening of policy coordination among member states. While this is appropriate, the recent experience in EU underscores that it is equally important to take a regional approach to financial stability. European experience also suggests the need for regional macro-financial surveillance mechanisms.

Contributor's Profile:

Mr. Ibrahim Abdullahi Zeidy is the current Director of the COMESA Monetary Institute. He coordinated the setting up of the COMESA Monetary Institute. Previously, he worked as a Senior Monetary Economist at the COMESA Secretariat, in Lusaka, Zambia for 11 years and as a Director of Research in National Bank of Ethiopia which is the country's Central Bank for 6 years. In both institutions, he worked as a researcher and coordinated research activities. As a Director of COMESA Monetary Institute he also organised many knowledge sharing workshops on monetary and financial integration issues.

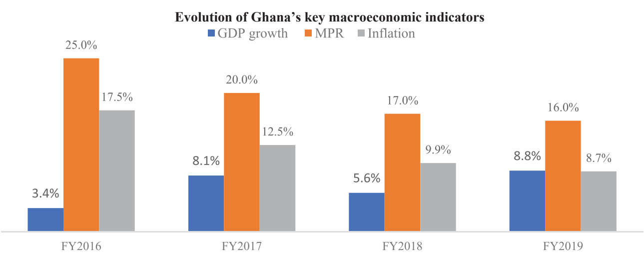
In his current role, Mr. Zeidy is responsible for the implementation of the COMESA Monetary Cooperation programme which is aimed at ultimately achieving the COMESA Monetary Union.Mr. Zeidy has M. Phil Degree in Monetary Economics from Glasgow University, with about 30 years of experience on macroeconomic policy and financial sector issues. He participated in many international and regional conference and workshops.

WHERE DO OPPORTUNITIES LIE IN GHANAIAN EQUITY MARKET

By **Derrick Mensa,** Portfolio Manager, IC Asset Manager Ghana

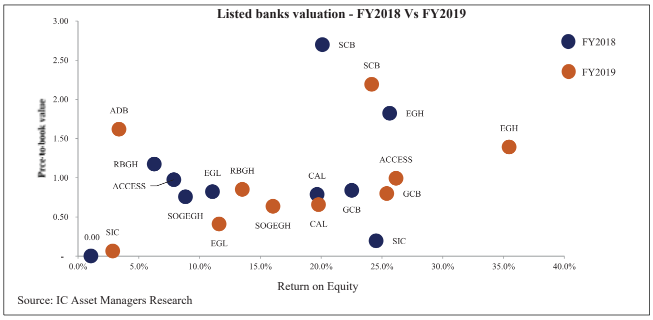
More than GHS 9.9bn (USD 2.1bn) has been wiped off the market capitalisation of the Ghana Stock Exchange (GSE) since the market turned bearish 17 months ago. While the onset of the decline can be attributed to market correction, the sell-off which has persisted post 2H2019 have been more speculative in my opinion.

A pick-up in earnings momentum amid a backdrop of strong macroeconomic fundamentals have not been rewarded. Instead, investors have chosen to focus on the impact of financial sector reforms which have seen nine banks collapse and the license of 53 investment management firms revoked.



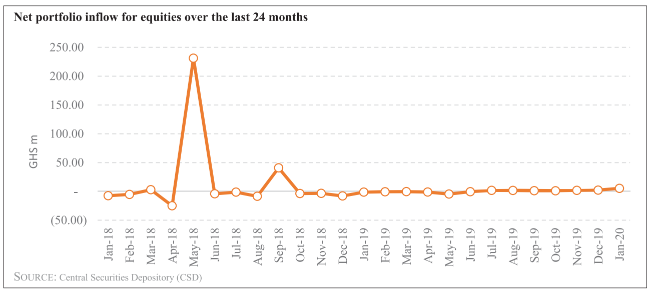
Source: Bank of Ghana

While the uncertainty brought on by the financial sector clean-up is warranted, I believe this has been overdone. The GSE-CI has lost 16.6% since the peak of the banking sector crisis. Meanwhile, earnings growth of listed banks is up 90.6% within the same period, leading to cheaper valuations. In effect, I see significant buying opportunities. However, is the timing, right?



Source: IC Asset Managers Research

Major headwinds such as late 2020 elections and the impact of COVID-19 could see the gradual demand build-up from increased net portfolio inflow fizzle out and leave the GSE slightly more flaccid.



SOURCE: Central Securities Depository (CSD)

Supply chain disruptions could impact the bottom line of manufacturers like Fan Milk (FML), Unilever (UNIL), Guinness Ghana Breweries (GGBL) and Aluworks (ALW). Commodity trading companies like Benso Oil Palm (BOPP) could also see lower revenue due to the 21.8% drop in crude palm oil prices since the outbreak of COVID-19.

The above notwithstanding, I believe financial stocks and telcos present the best buying opportunities not only for their relatively cheaper valuations but also due to the potential for these counters to offer the best insulation to the major headwinds in 2020.

For starters, any apprehension owing to political risk from the upcoming 2020 elections seems to be priced in given the hefty discounts on trading multiples.

Secondly, for the banks, loan book split indicates relatively lower exposure to trading and manufacturing firms which are more susceptible to supply chain disruptions due to COVID-19 making them less vulnerable to the economic impact of the virus. I also estimate that non-funded revenue is likely to remain robust on account of a pick-up in treasury activity on investment securities as well as FX trading income; neutralising any negative impact from lower commissions on off-balance sheet activities.

However, it is important to note that due to the recent capital raising, there is very little economic value (i.e. return on equity in excess of cost of equity) in listed Ghanaian banks. Ecobank Ghana is the only listed bank with economic value and therefore remains my top pick within the sector.

Ghanaian insurers are unlikely to see a significant impact from COVID-19 due to the industry's premium mix. Motor and Fire policies form a bulk of non-life premiums with health policies accounting for under 5% of non-life premiums. Furthermore, given the relatively low mortality rate from COVID-19, I do not anticipate a significant impact on Life insurers except for those who provide health insurance policies. Interestingly, Enterprise Group (EGL), my top pick within the sector does not currently offer health insurance and as a result, the impact of headwinds such as COVID-19 will be minimal in my opinion.

While supply chain disruptions could impact the operations of telcos, I believe the current discount on MTNGH's share price is more than enough compensation. The mobile network operator is currently trading at an EV/EBITDA of 3.3x, which compares favourably to 8.6x for Kenya's Safaricom, 3.9x for MTN Nigeria and 6.8x for South Africa's Vodacom.

In addition, to deal with any potential disruptions, the company has front-loaded its Capital expenditure and PPE (property, plant & equipment) needs, giving its suppliers ample time to meet their delivery schedule.

In summary, I believe Ghanaian financial and telecom companies offer significant upside from current valuations. However, it is important to recognise that near-term risks are unlikely to lead to any significant capital gains in the immediate term. This is the time to cherry-pick and wait for a multi-year bull-run once the current headwinds subside.

Contributor's Profile:
Derrick Mensahis a Portfolio Manager & Head of Business Development at IC Asset Managers (ICAM). He has over eight years of experience in investment analysis, valuation and corporate finance. Prior to joining ICAM, Derrick worked with African Alliance Securities as a Senior Equities Analyst with coverage across West African banks. Derrick has also been involved in raising over USD 300m in both debt and equity capital through IPOs and Private Placements. He was rated by South Africa's Financial Times in 2014 and was awarded the prestigious honour of the Most Promising Investment Professional in 2011 by the Ghana Investment Awards. Derrick holds a BSc Biological Sciences from the Kwame Nkrumah University of Science and Technology in Ghana.

PLUMMETING ZIMDOLLAR, ZIMBABWE AT CROSSROADS

By **Enock Rukarwa,** Research & Investment Analyst, FBC Securities Zimbabwe

2020 resuming from where 2019 ended

The economic crises deepened in 2019 characterized by debilitating power outages of up to 18hrs a day, acute foreign currency shortages, fuel shortages, reduced production and runaway inflation. Coming into 2020 fundamentals have not changed hence the same plagues will continue torment the Zimbabwean economic plight. Given the numerous headwinds which the country is faced with; survival becomes strategic for most organizations.

At the center of the challenges is the availability and cost of foreign currency, which has seen businesses fail to acquire the much needed raw materials and meet foreign obligations. Production for some businesses has been crippled by erratic supply of electricity, fuel and water. A general assessment on company performance in 2019 can reveal that margins went down drastically in real terms.

Stagflation is an accurate characterization of Zimbabwe's current economic situation as inflation is at its highest post-dollarization although the economy is in a recessionary period. The foremost substance to Zimbabwe's stagflation trap is increasing broad money supply, which registered growth of 135% from ZW$10bn in December 2018 to ZW$23bn in September 2019.

Despite current market circumstances being a replica of the 2008/9 predicament, the government is still embarking on snowballing money supply even further through the issuance of Zimbabwe dollar notes and coins to account for 10% of broad money (M3) supply from 5% in 2019.

It is imperative for government to improve the efficiency of the new FX interbank market to deepen the interbank FX market's function as the basis for market-determined exchange rate and to close the parallel market spread. Consistent with the government's monetary targeting framework, the exchange rate needs to shift to a floated regime, with limited interventions by the RBZ to avoid excessive exchange rate fluctuations.

Existing exchange controls, which limit FX purchases in the official interbank market for current account transactions, will continue to control demand for FX, but the permitting and enforcement framework should be applied transparently and uniformly. Consistent with the desire to move towards a unified exchange rate any subsidies for specific goods or sectors (e.g., fuel or medicine) should be channelled through the budget, not through administered exchange rates.

ZSE Performance 2019

The benchmark Index, the ZSE All Share gained 57% in 2019. However mathematically this was a negative real return as inflation closed the year around 440% YOY. The stock market scratched gains amidst rough patches largely characterized by a myriad of headwinds in the energy sector, monetary sector and drought effects.

While inflationary pressures saw investors hedge in May and parts of June, the move to introduce a 90-day disposal window of dual listed securities to restrict arbitrage opportunities and the introduction of a mono-currency saw sentiment wane further as foreigners lost appetite. November had a record low in terms of foreign buys at ZW$18.24 million while local liquidity was limited. This saw market capitalization fall below psychological benchmarks of between US3.5billion-USZW$4 billion to USZW$1.77 billion.

Penny stock MedTech once again led the annual risers returning 7 500% to 1.52c on market cap of ZW$46 million. Year old Cassava and Seed Co were the only counters to close with a negative return. Cassava was down 1.33% and Seed Co was the worst performer losing 8.44%.

ZSE total market capitalization continued the upward momentum in 2019 as it rallied a further 51.8% during the year to close the year at ZW$29.64bn. The rally was sustained from a 95.59% rally in 2018 and a 140.94% gain during 2017. The ZSE began its rally in March following the reintroduction of the Zimbabwe dollar in the preceding month prior to the abolishment of the multi-currency regime and the 90-day vesting period for fungible stocks.

The rally was however, predominantly spurred by foreign investors who were using fungible stocks, including Old Mutual to exit the market and a few local institutions hedging into the ZSE as a safe haven.

In terms of potential investment pockets, albeit weakening economic fundamentals we recommend cautionary investments into exporting companies, dually listed stocks, highly diversified counters, property companies, consumer facing stocks and high liquid counters. The main thrust remains value preservation and survival withstanding economic decay.

Business strategies withstanding headwinds

However harsh, the environment might be, there are still opportunity pockets for exploitation. Intensifying investments in sales and marketing initiatives, promoting foreign demand is fundamental as domestic market remains subdued. Companies have to continue defending market shares and exploiting exports markets where possible.

Operational efficiencies have to be enhanced to ensure cost containment and quality product and service delivery. Controlling value chains through vertical and horizontal integration can be a key enabler in managing capex and opex. Three pillars of cost containment remains right sizing, fixing business fundamentals and value chain leveraging.

Management teams have to be highly focused on adapting business models to take account of wearying economic rudiments. In this regard, attainment of volume targets and controlling the overhead base which is under pressure from extreme cost-push have to be given due attention.

2020 Outlook

We expect forex challenges to persist and consumption to be dampened in 2020, as the effects of austerity measures and monetary reforms will be apparent in the medium-term. Nonetheless, 2019 saw a significant contraction in corporate earnings in real terms, attributable to a change in function currency and limited working capital funds as borrowers' lacked capacity to provide loans. Furthermore, we are concerned that persisting drought conditions, burgeoning money supply, relatively lower forecast economic output and a depreciating currency will affect consumption in 2020 resulting in further economic contraction.

It is imperative to consider a company's level of independence on the domestic market, foreign currency obligations, dependency on imports, and exposure to the bottom-of-the-pyramid and the company's level of control in pricing when valuing Zimbabwean stocks. As such, we have a natural proclivity toward 'hedged counters' which predominantly derive their earnings outside the country's borders.

Exchange rate issues have an impact on COGS, and we expect this to remain a challenge as long as disparities between the interbank and parallel market remains. Naturally, this also affects companies with off-shore obligations and companies with regional operations but domiciled here meaning that they cannot capitalize their off-shore subsidiaries easily.

COVID-19 RISKS WILL PRESSURE SOUTH AFRICAN BANKS EARNINGS & ASSET QUALITY IN 2020

By **GCR Research Team,** South Africa

The South African Banking Sector has shone in the Economic Gloom

The South African economy has been struggling for much of the past decade. Over the past five years, GDP per capita growth has been negative, meaning the South African population (as a whole) have been getting poorer. In combination, official unemployment increased to 29.1% in the last quarter of 2019, the highest since 2008. Many reasons have been touted for the decade of poor economic performance. In our opinion, the high inequality is undoubtedly a persistent root cause, alongside infrastructure shortfalls and labour competitiveness/rigidity. Failing State-Owned Enterprises, long standing policy uncertainty, weak political implementation and now unsustainable government fiscal deficits are also a restraint to growth and investment. Furthermore, all too frequent public and private governance failures, have also taken their toll. Little wonder, therefore, that South Africa business confidence reached a 21 year low in the first quarter of 2020 (before the National Disaster was announced).

Despite this long-standing economic malaise, the country's banking sector has generally fared well over the past decade. Over the past 10 years, the South African banks have rarely underperformed the average through the cycle returns for emerging market banks, of 15%-20% return on equity (ROE) and 1%-2% return of assets. Furthermore, they have regularly outperformed the credit loss experience of most emerging market peers with credit losses trending below 1% for the top tier banks. Therefore, one could assume that South African banks can, with some consistency, make the returns without taking the same associated risks of their emerging market peers. However, the recent 2019 results demonstrated that the South African banking sector is not immune to the domestic economic malaise. The average return on equity dipped to 14.37% at December 2019 from 16.01%

one year earlier and credit losses also increased materially, although from a low base and generally still below the 1% level, for the top tier banks.

2020 will be very challenging for the economy and the banks.

2020 is shaping up to be an even more challenging year than 2019 and, of course, the exact local and global impact of the COVID-19 pandemic is currently unknown. However, to date, GCR has assumed a severe stress environment will extend through the period laid down by the timelines of the National Disaster, i.e. up to 15th June 2020. The type of stress is based on the reduction of economic activity reflecting a fall in consumer spending and negative business sentiment caused by travel restrictions, large scale self-isolations, quarantines and social distancing measures in effect in South Africa and globally. Specifically, GCR assumes that South African corporates and individuals exposed to hospitality, tourism and discretionary retail will be hit hardest (economically) and it will exacerbate already significant weaknesses in the economy. GCR believes that the significant 100bps interest rate cut will provide little impetus for growth in Q2'20 but it should further help debt serviceability of the private sector and could provide more stimulus in the 2nd half of 2020.

We note that this scenario could change, almost from day to day. However, at the time of this article, GCR is anticipating an extreme stress scenario in Q2'20 with modest negative economic growth across 2020, alongside continued deterioration in the employment rate and increased corporate insolvencies. We also believe the significant international market sell-off hasn't ended and the year will be characterised by periods of extreme volatility for local and international markets, further dampening confidence and lowering financial flexibility/ market access. These risks are expected to exacerbate South Africa's homemade woes, especially on the strength of the currency, weaker foreign direct investment and curtailing export demand.

As a result, GCR believes that the South African Banks potentially face a very challenging 2020. The major downside risks for performance are the unknown challenges for the banking sector amidst the COVID-19 pandemic. GCR considers the lack of consumer spending and business activity to be inevitable but currently the impact on the economy and credit losses remain relatively unquantifiable. This unknown is further exacerbated by the new IFRS9 accounting rules, which force the earlier recognition of loans losses. Even if customers do not miss payments, which would be classified as stage 3, the material change in circumstances caused by COVID-19 is likely to trigger an increase in stage 2 loans and the short-term horizon of the stress could materially raise stage 1 provisions. Although unlikely, a relaxation of the accounting rules, particularly on stage one and stage two, could guard against a short-term earnings shock for global banks.

Despite the uncertainties, we believe a 10% increase in year on year portfolio impairments could be likely under the above scenario. Presuming very low or flat loan growth, this could reduce short-term profitability by around ZAR5bn. At the same time, GCR believes (on average) impaired loans could increase by around 5% to 10%, to around 4%-4.5% of gross loans by year end 2020. Presuming that the banks maintain their current average coverage levels of specific impairments, this could lead to an additional credit impairment increase of around zar6bln to 8bln across the banking sector. If we combine the additional credit impairments with expectations regarding generally lower credit extension, lower interest income and weaker transactional income for the banks, we could see profitability dip by around 15% in 2020. As a result, we are currently expecting an average ROE of between 12.5% to 13% for the South African banking sector at FY20. Despite this, over the long-term we expect South African banks to remain relatively strong components of the South African economic system, with sound levels of capitalisation and good longer-term earnings.

The relative robustness of South African households is good, but the changing nature of debt raises risks in 2020.

Positively, since 2008, household debt as a percentage of nominal disposable income has decreased to 72.6% (3Q, 2019) from 85.7% (year end 2008). At the same time, household's cost of servicing debt has reduced to 9.4% from 13.4%. As a result, South African households appear to be in a relatively good space to service debt, despite low wage growth and higher unemployment. This is especially true when factoring in the significant 100bps negative movement in rates on 19 March 2020.

However, GCR also notes that there has been a change in the nature of household liabilities, which could demonstrate some underlying vulnerability to the current downturn. In 2011, relatively lower interest and secured mortgage credit accounted for 55% of total household liabilities. By year end 2018, mortgage loans had reduced to 47%, which means households are now more exposed to comparatively higher interest and relatively shorter-term unsecured debt. This reflects the relatively higher growth of credit cards, overdrafts and instalment credit versus mortgages on aggregate, over the past few years, for the major banks. Furthermore, given the relatively slow growth of the mortgage book and dynamics of the domestic housing market, it seems likely that South African banks (apart from Investec Bank Ltd.) are increasingly exposed to middle income earners. Unfortunately, this slice of the bankable population could be hit hardest in terms of disposable income and employment in 2020, due to the impact of COVID-19 and the economic downturn.

Corporate leverage is low, but so are profits

Corporate South Africa has long been the strongest component of the economy. Overall, we have seen a modest increase in leverage over the past decade, with debt to capital (according to the Annual Financial Statistics Survey, published by Statistics South Africa) increasing to 57% from 47%p to 2018. However, there has also been a fairly significant reduction in profitability, with net debt to income increasing to 44% from 29% over the same period. This appears to be a clear indication of the economic headwinds on the corporate sector. Furthermore, the lack of economic activity has had a toll, especially on the local construction industry and more recently on commercial real estate, which is suffering from high vacancy and some valuation pressures. Going forward, GCR views the hospitality, tourism and discretionary retail sectors to be most at risk, due to the travel and gathering restrictions caused by the COVID-19 pandemic. We estimate that these vulnerable sectors represent around 10% of the total loan books for the banking sector. Lastly, and probably most importantly, we also expect small and medium sized entities ("SME") to suffer from the additional economic strain and reduction in consumer spending.

Positively, corporate credit losses have been low for the banking sector. On average, noting significant bank by bank differences, corporate loans represented around 15% of stage 3 loans but over 30% of the total loan books, at year-end 2019, for the major banks. Furthermore, SME are a smaller part (around 15% of total corporate lending) of the banking sector credit advances and the banks seem generally well collateralised for commercial real estate lending at the moment. While SME exposure may be fairly limited for most of our rated financial institutions, GCR continues to monitor how SME focused banks and securitisation are affected by the situation.

Profitability is expected to come down, but capital will remain sound

The South African top tier banks generate returns equally (roughly) from interest income and stable non-interest income. GCR believe the significant reduction in interest rates will be passed on to borrowers, reducing net interest margins for the sector and ultimately reducing profitability due to the endowment effect, although it may also stave off some credit impairments. This is likely to be exacerbated by low growth in interest yielding assets. Positively, bond yields seem to be picking up and therefore the change in earning asset mix towards more liquid assets may not dampen margins too much. Low business activity is also expected to pressurise growth of non-interest revenues, which are dominated by fees and commission of transaction and lending products. The major unknown in this regard are the economic and operational challenges for the banking sector amidst the COVID-19 pandemic. GCR considers the lack of consumer spending and business activity to be inevitable but currently unquantifiable. Furthermore, the impact of mass illness, branch closures and other potential operational disruptions could raise costs and risks. Trading revenues, the vast majority of which is non- proprietary, could improve due to the volatile environment but these remain a small amount of total revenues. Positively, the coverage of operating costs by relatively risk-free non-interest income underlines some stability for banks. However, given our expectations for increased credit impairments we do believe returns against equity and assets will shrink again in 2020 (see above). About capitalisation, GCR expects the tier one ratio, perhaps supported by additional tier one issuance, to range between the 13% and 13.5% range by year end 2020. This would broadly be in line with the mid-range of the intermediate assessment for the sector.

FUTURE GROWTH ASSET MANAGEMENT

INVESTMENT VIEW AND STRATEGY IN 2020

At a global level, the shift from quantitative easing to tightening has not only stalled but has been forced into a 180 degree turnabout. Central banks, fiscal authorities and multi-national organisations across the globe have announced a number of measures in a desperate effort to at least partly offset the negative economic impact of the COVID-19 pandemic on economic activity. Since the outcome of the pandemic is still very uncertain, we have no way of knowing if this will be sufficient to stem the tide.

Locally, our main concern regarding the bond market remains the strong link between lacklustre economic growth and a weakening fiscal position. The impact of the recent COVID-19 related events raised this concern considerably. More specifically, this points to the rising debt burden of the state, even considering the most recently tabled expenditure-restrained budget, which carries significant implementation risk. This continues to threaten the country's sovereign risk profile and places pressure on domestic funding costs.

Under current conditions and in response to the unfolding crisis, our pre-COVID-19 view of a stable monetary policy path is now inappropriate. The central bank may very well continue with repo rate reductions following the latest cut of 100 basis points. The collapse in economic activity, a relatively benign inflation path and the global backdrop opened the door for more monetary easing, both via rates and also using other measures.

While our investment theme most certainly remains negative in light of unfolding events, market valuation has kept abreast of these developments. Our fair value and other relative value estimates clearly point to significant value in both nominal and inflation-linked bond markets. While a move further away from these fair value estimates is very likely, this is hard to predict with any degree of accuracy. One obvious risk from a flow perspective is the expected enforced selling by passive foreign fund managers following the exclusion of the country from the WGBI following the Moody's downgrade to sub-investment grade. However, we would argue that the extent of the dramatic sell-off in March, together with significant rand depreciation, would offer relatively good value to the more unconstrained foreign investor.

We've opted to focus on our estimate of fair value, and, in our collective mind, the market at current levels has discounted enough bad news to allow us to cautiously and incrementally add risk to our funds.

INVESTOR TAKEOUT: In light of the recent market sell-off, we have switched from our previous defensive investment strategy of striking a balance between avoiding capital loss and not losing out on the accrual offered by a steeply sloped yield curve. The market has moved far enough away from our fair value estimates to enable us to focus on accumulating risk in the form of longer-dated bonds and thus higher modified duration. This applies to both nominal and inflation-linked bond markets and mandates.

COVID-19 (CORONAVIRUS) | DRIVES SUB-SAHARAN AFRICA TOWARD FIRST RECESSION IN 25 YEARS

Growth in Sub-Saharan Africa has been significantly impacted by the ongoing coronavirus outbreak and is forecast to fall sharply from 2.4% in 2019 to -2.1 to -5.1% in 2020, the first recession in the region over the past 25 years, according to the latest Africa's Pulse, the World Bank's twice-yearly economic update for the region.

"The COVID-19 pandemic is testing the limits of societies and economies across the world, and African countries are likely to be hit particularly hard," said Hafez Ghanem, World Bank Vice President for Africa. "We are rallying all possible resources to help countries meet people's immediate health and survival needs while also safeguarding livelihoods and jobs in the longer term – including calling for a standstill on official bilateral debt service payments which would free up funds for strengthening health systems to deal with COVID 19 and save lives, social safety nets to save livelihoods and help workers who lose jobs, support to small and medium enterprises, and food security."

The Pulse authors recommend that African policymakers focus on saving lives and protecting livelihoods by focusing on strengthening health systems and taking quick actions to minimize disruptions in food supply chains. They also recommend implementing social protection programs, including cash transfers, food distribution and fee waivers, to support citizens, especially those working in the informal sector.

The analysis shows that COVID-19 will cost the region between $37 billion and $79 billion in output losses for 2020 due to a combination of effects. They include trade and value chain disruption, which impacts commodity exporters and countries with strong value chain participation; reduced foreign financing flows from remittances, tourism, foreign direct investment, foreign aid, combined with capital flight; and through direct impacts on health systems, and disruptions caused by containment measures and the public response.

While most countries in the region have been affected to different degrees by the pandemic, real gross domestic product growth is projected to fall sharply particularly in the region's three largest economies – Nigeria, Angola, and South Africa— as a result of persistently weak growth and investment. In general, oil exporting-countries will also be hard-hit; while growth is also expected to weaken substantially in the two fastest growing areas—the West African Economic and Monetary Union and the East African Community—due to weak external demand, disruptions to supply chains and domestic production. The region's tourism sector is expected to contract sharply due to severe disruption to travel.

The COVID-19 crisis also has the potential to spark a food security crisis in Africa, with agricultural production potentially contracting between 2.6% in an optimistic scenario and up to 7% if there are trade blockages. Food imports would decline substantially (as much as 25% or as little as 13%) due to a combination of higher transaction costs and reduced domestic demand.

Several African countries have reacted quickly and decisively to curb the potential influx and spread of the coronavirus, very much in line with international guidelines. However, the report points out several factors that pose challenges to the containment and mitigation measures, in particular the large and densely populated urban informal settlements, poor access to safe water and sanitation facilities, and fragile health systems. Ultimately, the magnitude of the impact will depend on the public's reaction within respective countries, the spread of the disease, and the policy response. And these factors together could lead to reduced labour market participation, capital underutilization, lower human capital accumulation, and long-term productivity effects.

The authors emphasize the need for a customized policy response to reflect the structure of African economies (especially the large informal sector) and the peculiar constraints policymakers currently face, particularly the deteriorating fiscal positions and heightened public debt vulnerabilities, and the overall low operational capacity to respond.

Due to the COVID-19 pandemic, economic circumstances within countries and regions are fluid and change on a day-by-day basis. The macroeconomic analysis in the report is based on data available by the first quarter of March 2020.

The World Bank Group is taking broad, fast action to help developing countries strengthen their pandemic response, increase disease surveillance, improve public health interventions, and help the private sector continue to operate and sustain jobs. It is deploying up to $160 billion in financial support over the next 15 months to help countries protect the poor and vulnerable, support businesses, and bolster economic recovery.

Q1 -2020 | SUB-SAHARAN AFRICA: ECONOMIC PROSPECTS AND MARKET PERFORMANCE REVIEW

Economic Prospects

During Q1'2020, the United Nations Economic Commission for Africa (UNECA) released the World Economic Situation and Prospects for 2020, revising the Sub-Saharan Africa (SSA) GDP growth to 1.8% from the earlier projected 3.2% in January 2020. The lower growth rate was majorly attributed to the economic impact of the COVID-19 pandemic set to disrupt supply chains, plummeting commodity prices and key sectors such as tourism, agriculture, oil and mining set to be greatly affected. The projections for 2020 are lower by 140 bps compared to the previous projection of October 2019, which stood at 3.4%. The largest economy in SSA, Nigeria, is expected to experience a less robust GDP growth in 2020 with the International Monetary Fund (IMF) revising this downwards by 30 bps to 2.0%, from 2.3% previously, attributable to the decline in the oil price growth and disruption of global supply chains due to the COVID-19 pandemic.

Currency Performance

All select currencies depreciated against the US Dollar except for the Ghanaian Cedi, which remains unchanged supported by market reforms which included the rate at which the commercial banks were willing to commit to exchange the currency for the USD at a future rate. The depreciation recorded by the currencies is partly attributable to the ongoing COVID-19 pandemic, which has seen a fast-falling demand for export commodities particularly from China, the most vital trading partner and the epicenter of COVID-19 outbreak. The Zambian Kwacha was the worst performer, depreciating by 22.3% against the dollar YTD owing to the low economic productivity with the fall of copper prices and drought, compounded with heavy imports which continue to put pressure on the local currency. The Kenya Shilling depreciated by 3.6% to close the quarter at Kshs. 105.1 against the US Dollar attributable to demand from merchandise importers who had entered contracts before the coronavirus-related disruptions, buying hard currency to offset them in the current thin market with very little dollar inflows, prompting the Central Bank of Kenya (CBK) to sell dollars, despite their earlier plan to purchase dollars from the market to improve forex reserves.

African Eurobonds

Yields on African Eurobonds increased in Q1'2020 after a decline in 2019. This was partly attributed to the COVID-19 health crisis, with investors attaching a higher risk premium on the affected regions due to the anticipation of slower economic growth. During the quarter, the Government of Ghana, on 4 February 2020 issued the longest dated Eurobond as part of debt issuance to raise USD.3.0 bn. The government launched the sale of a USD 750m tranche, which will amortize and have an average life of 40-years at a yield of 8.9%. The bond was oversubscribed 5x to USD downgrade 14.0 bn indicating a huge interest for Ghana's debt. In addition, yields on the Zambia Eurobond increased in Q1'2020 by 19.1% points as a result of a mass exodus of foreign investors amid fears of the country's debt sustainability and the ongoing COVID-19 pandemic, with most investors believing it to be close to default. Yields on its USD 750m of notes due in September 2022 soared 14.7% points to 66.3% attributable to the weakening copper prices and drought, which has led to power cuts caused by low water levels at its hydroelectric dams. Yields on Kenyan and Senegalese Eurobonds have been increasing since the beginning of the year, signalling that the demand for the instruments has declined during the period. The trend was replicated in all the Eurobonds attributable to the expected economic decline due to the COVID-19 pandemic.

Equities Market Performance

Most of the Sub-Saharan African (SSA) stock markets recorded negative returns in Q1'2020. The region experienced capital outflows, a from last year's recorded inflows. This is attributable to the ongoing Coronavirus pandemic, with investors selling out of the equities market in favour of safe havens and the expected economic fallout. Rwanda is the best performing index showing resilience amid the COVID-19 pandemic following gains made by cross-listed stocks such as Equity Bank, which has recorded YTD gains of 25.7%. South Africa recorded the worst performing index with losses of 38.9% attributable to the continued selloffs brought by concerns about the economic fallout caused by the Coronavirus, despite assurances that the cabinet is putting together an economic stimulus package to deal with the detrimental impact from the actions taken to combat the virus. The performance of the Nairobi All Share Index (NASI) was driven by losses of 21.3%, YTD attributable to the ongoing Coronavirus pandemic, with investors selling out of the equities market.