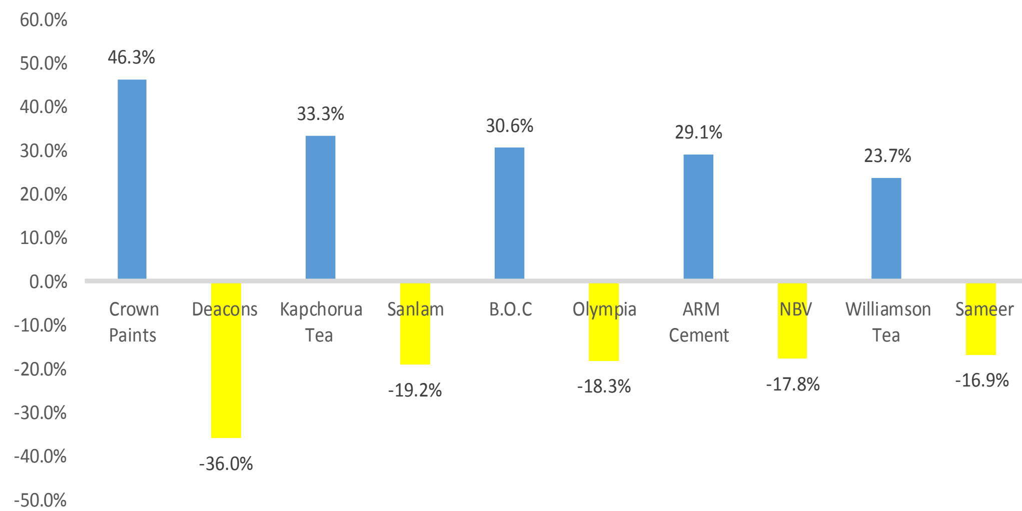
Equities

We had another slow month in August that was characterized by a dip in the main index (NSE-20: -3.1% m/m). While we expected major banks to underpin a general recovery in investor sentiment, we were surprised that they all posted price declines (KCB: -4.8%, Equity: -8.3% and Co-op: -2.7%) despite posting very good growths in earnings (KCB: +c.18% y/y, Equity: +c.18% y/y and Co-op +7.4% y/y). We believe that low foreign activity was to blame for the price pullbacks as some of them were away for most of them were away on their summer breaks. That said, we note that there were a number of stocks which rose albeit on thin volumes. Crown Paints, Kapchorua Tea and BOC topped the gainers list while Deacons, Sanlam and Olympia led from behind.

Top Gainers and Decliners



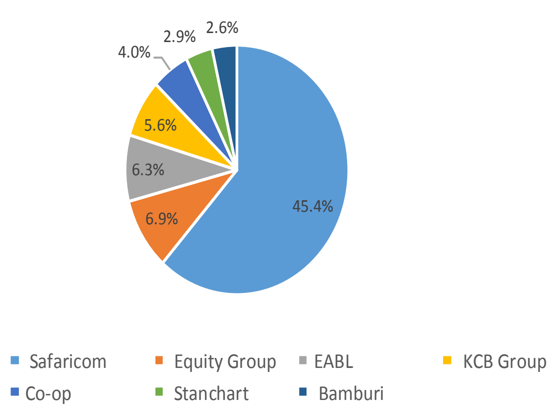
Source: NSE, NICS Research

Taking stock of the performance of the market from January-to-August, we highlight that the NSE-20 declined substantially (-13.5% to 3203.40 points). We began the year on an excellent note with stellar capital gains recorded in the first quarter due to what we attribute that to investors taking positions for the year. In the 2nd quarter, we note that there was net selling by foreigners owing to global trade tensions.

As we noted earlier on, the stocks that underpinned the broad-based gains were large capitalisation stocks with sizeable foreign investor following. So skewed is the composition of the index that 7 stocks account for three-quarters of the total market capitalisation of the index. It just so happens that Safaricom on its own accounts for nearly half of the total market value. As the year went on, these particular stocks were affected the most by the trade tensions as they have the highest following among foreigners.

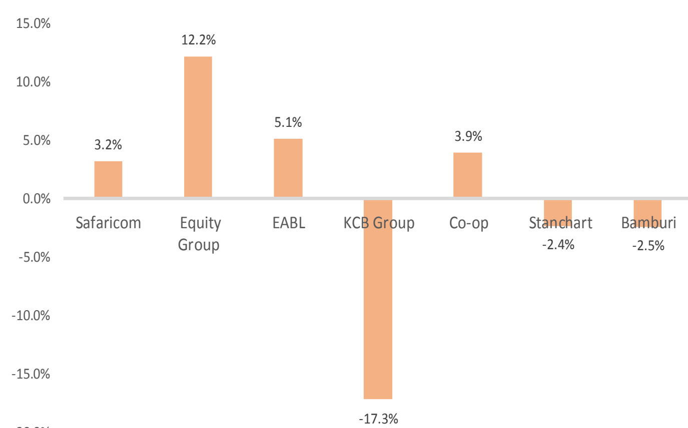
As a consequence, on a year-to-August basis, of the 7 stocks, we note that KCB (-17.3%), Stanchart (-2.4%) and Bamburi (-2.5%) declined. Only Safaricom (+3.2%), Equity Group (+12.2%), EABL (+5.5%) and Co-op Bank (+3.9%) posted gains.

7 companies account for 74% of the market capitalisation



Source: NSE and NICS Research

Steep declines diluted modest gains



Source: NSE and NICS Research

Catalysts

Historically, we note that September and October have been months where activity has been quite subdued. That said, we see November as a month where there are likely to be some share price triggers. We note that banks are expected to begin reporting their 3Q18 results. We also expect Safaricom and Centum to report their 1H19 results. We see Safaricom reporting strong growth in earnings on the back of strong growth in data and M-Pesa. Additionally, we expect to see Centum post better results than in the previous year owing to the sale of its stake in GenAfrica. We therefore expect better activity in November than in prior years.

Macro Indicators

- **Foreign Exchange:** We note that the shilling has been generally strong in FY2018 in comparison to FY2017. This has been bolstered by an increasing in diaspora remittances which resulted to an overall surplus of KES 129.3bn in the first quarter of this year. The international trade services registered a surplus of KES 49.3bn from KES 38.5bn while receipts from international services improved by 10.8% to KES 129bn. The current account deficit has also substantially improved to KES 107.9bn from KES 129.7bn in 2017. On grounds of increased exports this year, accompanied by lower food and SGR related imports, we foresee the shilling gaining more against the green back. We believe that the currency will be contained within USD/KES 101-103 band.
- **Inflation:** In the month of August inflation slightly declined to 4.04% from 4.35% the previous month thanks to the food component of the CPI which weighed down on the cumulative inflation percentage. Fuel, Electricity and Gas contribute a spike of 16% being the highest for the past eight months. This plummet is attributable to electricity tariffs revised upwards as well as increased unleaded fuel price which netted out the slight decline in diesel.
- **GDP acceleration:** The real GDP in 1Q18 advanced by 5.7% y/y compared to 4.8% y/y in the first quarter of 2017. With the positive outlook from the agricultural sector owing to apposite rainfall, we expect resilient growth in the second quarter of 2018. The kick start of the big four economic development agenda is also expected to influence economic output further. However, the newly revised CBR rate of 9% thus a borrowing ceiling of 13% could perpetuate crowding out of credit access to Small Microfinance Enterprises since the risk inherent may not commensurate the return expected. This might consequentially weigh on output.

STOCK PICKS

Bamburi Cement: BUY at TP of KES 242, Current Price KES 180.00

- Bamburi Cement has reported a 50% decline in FY17A PBT to KES 4.1bn, a poor performance but in line with the 37% decline in 1H17 PBT. Revenue performance was as bad, posting a more benign decline of 6% to KES 35.9bn, weighed down by an election affected performance in BMBC's main market of Kenya. But costs were the biggest challenge with EBIT down 47% as commodity and electricity prices rose. DPS declined significantly by 66% to KES 4.00 from KES 21.00 in spite of the payout ratio increasing to 88% from 83% in FY16A.
- Provisional data from KNBS show that cement consumption in Kenya contracted by 8% in 2017 to 5.8mtpa. This pales in comparison to the 11% growth reported in 2016. As discussed in our sector update note last year, access to credit continued to be a major inhibitor to the construction sector as Kenya's private sector credit growth decelerated to low single digits in 2017. Management blamed higher energy costs with electricity and coal prices rising. The former was due to Kenya switching to the more expensive thermal energy as HEP production was impaired by drought. The latter follows global commodity prices spike. 1.8mtpa of new capacity is on course to be added in 2H18 at both Nairobi Grinding Plant (NGP) and Tororo. Rebound in private credit sector growth is crucial especially in driving individual home builder consumption, which accounts for 75%-85% of total cement consumed in the region. Resumption of infrastructure will have a direct effect on construction rebound in 2018.
- We anticipate easement of electricity prices in Kenya in 2018 following increased HEP generation due to long rains. With thermal generation costing as much as USc.22/KWh compared to HEP's USc.3/KWh, the savings y/y should be significant as the country switches back to HEP. While exciting, the introduction of off-peak electricity prices, meant to incentivize companies to increase production, will unfortunately not benefit BMBC and ARMC as they are already operating near full capacity utilization levels. We expect cement prices to edge upwards as production costs rise and industry capacity utilization increases. We expect BMBC's EBIT margin to recover (FY18F; 20%, FY17A; 21%) ALSO ON THE ASSUMPTION THAT SALES WILL GROW AT c.15% boosted by the new capacity in 2H and relatively better cement prices.

Safaricom. HOLD at TP: KES 31.31; Current Price: KES 27.75:

Safaricom reported a FY18 EPS growth of 14% to KES 1.38 (NICS estimate of KES 1.34), marking its slowest growth in earnings over the last 5 years. A lower depreciation charge of 14%, compared to an average charge of 16% in the preceding 3 years, embellished the performance, otherwise, growth would have been 8%. MPESA and mobile data decelerated further than anticipated, growing at 14% and 24% versus our estimates of 17% and 30% respectively. DPS increased by 13% to KES 1.10.

- **MPESA revenues (28% of service revenues) decelerated** from 33% y/y to 14%, the first deceleration in four years (FY14A). While management blamed the difficult macroeconomic environment for the slower growth, which can be corroborated by the slower growth particularly in 'new business' (C2B, B2C, B2B) at +24% (FY17A; +103%) competition was also a factor. As alluded to in our 1H18 note, management reduced 'bank to MPESA' transfer charges by c.33%, while person to person (P2P) transfers charges declined by 27% in response to increased competition from largely Equitel. Additional cuts were effected on Lipa Na MPESA (LNM) tariffs by 50% in the same period. Average transactions per user per month increased by 14.6% to 11, slower than the 35% growth recorded in the preceding period.

- **Mobile data (16% of service revenues) continued to decelerate**, growing by 24% versus the 38% growth reported in the corresponding period last year. This continues the deceleration recorded in the three preceding financial years (FY15A; +59%, FY16A; +43%, FY17A; +38%). Usage per user continues to rise (FY18A; +56% to 421MBs, FY15A; +38%, FY16A; +77%, FY17A; +52%) implying either a slower accretion in subscriber numbers and/or lower data charges. Absolute Data subscriber net-adds declined for the for the first time in 3 years with 1.03m added compared to the 2.56m added in FY17A. Data prices, which declined by 29% y/y as at 1H18 (1H17; 16%) have been under pressure from increased competition with Airtel and Telkom Kenya significantly cheaper (refer to 1H18 results note for price comparisons). For instance, KES 1,000 will buy 6GB on Airtel, 4GB on Telkom and 3GB on Safaricom. Voice revenues (43% of service revenues) grew at a flat rate of 2%, despite Safaricom's subscriber market share declining by 280bps q/q to 69.1% as at December 2017, according to the CA's quarterly sector statistics. Airtel Kenya was the biggest beneficiary gaining 230bps q/q to 17.2%. This coincides with the main political opposition party NASA's boycott call of Safaricom products in the aftermath of the October 26th General Elections. Net adds were only 1.4m, 50% lower y/y and despite this, monthly voice ARPU contracted by 7% to KES 272, suggesting reduced usage. This is confirmed by our MoU estimate of 92, 5% lower y/y.

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- **Maintain HOLD at TP of KES 31.31 (Previously HOLD at KES 25.85):** We adjust our EPS forecasts marginally (FY19F; +2% and FY20F; +0.6%) to KES 1.50 and KES 1.57 respectively. We maintain our view of a deceleration in the main revenue drivers MPESA and Mobile data in the near term under increased competition. While the boycott call has been lifted, we are unlikely to see the subscribers who exited troop back, on realization of how relatively affordable Airtel Kenya is and given that their offering is almost on par. In fact, we expect a slower accretion in subscribers for Safaricom going forward. Elsewhere, we see little impact of mobile money interoperability, which allows the seamless transfer of money across different networks. Already, telcos are insisting that withdrawals can only be done with their agents. We maintain that the only way to compete with MPESA is to become as ubiquitous. We assign a higher relative valuation weighting in deriving our blended TP (70% from 60% before) given the counter's increasingly lofty valuation. HOLD.

Co-op Bank Group: BUY at TP of KES 19.53 Current Price KES 16.85

- **Co-op Bank Kenya released its 1H18 results with the main highlight being the c.8% y/y rise in the PAT (to KES 7.14bn). We note that a sharp jump in interest income (+7.9% y/y to KES 20.78bn) and slight growth in interest expenses (+2.2% y/y to KES 5.97bn) underpinned an increase in earnings. We discuss our insights about the company in more detail below.**
- **Slack loan growth to drive flat growth in YIEA in FY18F:** The total interest income grew by c.8% (to KES 20.78bn) with increases in income from loans and advances (+5.6% y/y to KES 16.13bn) and government securities (+17.5% y/y to KES 4.55bn) being the key catalysts. On a year-on-year basis, we note that the total amount invested in government securities increased by KES 9.7bn (to KES 80.2bn) thus underpinning the double digit increase in income from gov't securities. Similarly, we believe that the contraction of the loan book on a year-on-year basis (0.59% to KES 251.1bn) held back interest income growth. For the remainder of the year, we expect loan growth to be subdued (so long as the rate capping law is still in place as is our base case). We therefore hold that the yield on interest earning assets (YIEA) will remain flat year-on-year (FY17A: 12.0% vs. FY18A: 12.1%).
- **Deceleration in cost of funds expected in spite of large CASA deposits:** We acknowledge that the bank made good strides in managing its cost of funds with the interest expenses rising (+2.2% y/y to KES 5.97bn) at a slower pace than deposits (+3.9% y/y to KES 296.96bn). This is especially commendable not only because the bank has the lowest level of CASA deposits among the three biggest banks (KCB, Equity and Co-op) but also because it has in the recent past registered high single-digit growth in interest expenses. We believe that the constrained growth in funding costs thus led to solid growth (+10.4%. y/y to KES 14.81bn) in net interest income. Going into 2H18, we expect similar disciplined deposit growth that is expected to marginally ease the interest expenses (Cost of funds: FY18F; 3.6% vs. FY17F; 3.5%).
- **Careful check on opex expected to lower cost-to-income ratio to 48%:** We note that total non-interest income mildly declined (-1.6% y/y to 7.0bn) thus mirroring the industry-wide NFI weakness in the quarter. Fees and commissions on loans and advances especially slumped (-41% y/y to KES 0.80bn) presumably due to the pro-rating of the income over the loan period as required by the IFRS 9 standard. We also highlight other fees and commissions income robustly rose (+11% y/y to KES 4.32bn) which we believe could be as a result of the bank customers' continued use of non-branch channels. We also highlight that forex income slightly pulled back (-1.7% y/y to KES 1.22bn) on the shilling's relative stability in the first half. Therefore, we believe that the dip in the contribution of total income is likely to remain lower in the near term owing to the staggered recognition of the fees and commissions income over the course of the loan term as is required by IFRS 9.
- **We upgrade COOP to BUY (with TP of KES 19.53) from HOLD (Previous TP: KES 18.00) on price action** and a significant drop in loan loss provisions (-57% y/y to KES 330.3m). We were positively surprised by the solid growth in net interest income (c.10%) that was primarily driven by prudent growth in interest expenses. While the growth in total opex (c.5% y/y) was in line with inflation, we note that weakness in non-funded income led to the cost-to-income ratio increasing to 49.9% in 1H18 (1H17: 48.1%). That said, we note that the bank's performance (1H18 RoAE: 21.6%) matches the full year guidance for the year (FY18F RoAE: 22.0%). However, we are watching out for further softening in non-funded income and an adverse asset quality experience could weigh on earnings in 2H18. Having said that, we believe that the counter is undervalued relative to its peers thus offering room for upside. BUY.

BRITAM (Not rated) Current Price KES 12.35

- Britam posted a 73% dip in full year profits (to KES 527.5m) driven by a steep increase in the provision for a change in actuarial value of policyholder benefits. We understand that there was a reversal of the gain in 2016 as a result of changes in the industry's way of changing the way insurance liabilities are to be valued.
- FY17 gross earned premiums grew at a higher pace (+14.8% to KES 23.3bn) than net earned premiums (+16.7% to KES 20.3bn). Fund management fees, however, declined (-18.1% to KES 760.6m).
- The group's asset base rose (+18% to KES 99.0bn) as of December 2017. Specifically, financial assets at fair value through profit or loss solidly rose (+66.4% to KES 30.6bn).
- Going forward, we expect maritime insurance to drive further growth for the industry following recent regulatory changes that requires commercial importers to take insurance exclusively with local underwriters. We believe that Britam, being a market leader with a reputable brand and significant financial capacity, will be a key beneficiary. The insurer launched a self-service online portal late last year in a bid to tap into the KES 23bn marine business.
- We also believe that the counter warrants investor confidence considering that two institutional investors (IFC and AfricInvest) have pumped in (or are planning to pump in) in KES 9.25bn in the company to acquire 10.37% and 14.3% stakes respectively.
- Currently Britam trades at a trailing P/E of c.44.1x which is significantly above the c.10x average over the course of last year. We believe that a resumption in profitability is likely to enable the company to trade at a more favourable valuation.

Kenya Re (Not rated) Current Price KES 16.30

- FY17 PAT increased by 8.8% to KES 3.5bn. In the period under review, the grew by 7% boosted by a 8% growth in net earned premium to KES 13.7bn.
- The firm's earnings from investments rose (+3% to hit KES 3.16 bn) this year compared to KES 3 bn in the previous period.
- Net claims incurred also grew (+14% to KES 7.59 bn) on the back of the earthquake related compensation pay-outs in Nepal and floods experienced in India, said the re-insurer .
- Total outgo was outpaced by total income, growing at 8% to KES 6.5bn. This was due to a marginal increase in net claims and policyholder benefits of 2% to KES 3.6bn.
- Kenya Re opened its Zambia regional office in November 2016, in line with its regional expansion strategy as it seeks to increase reinsurance capacity for insurance companies in Africa. The regional office is expected to serve Namibia, Zambia, Zimbabwe, Botswana, Mozambique, Lesotho, Swaziland Malawi and Angola. while boosting good risk management and innovative insurance practices in the region. The reinsurer expects to benefit from the new Zambian government trade strategy for local and international investment as the country tries to diversify away from copper mining.
- With mandatory cessations by insurers to Kenya-Re still in effect till 2020, we anticipate the reinsurer to reap from underwriting maritime insurers. Experts anticipate local insurers will increase their reinsurance cover in order to increase their capacity to underwrite large shipments.
- Currently KNRE trades at a P/E 3.7x which is attractive relative to Britam and CIC Insurance.

EABL BUY at TP of KES 273.63; Current Price KES 194.00

While much has been made of EABL's FY18 PBT decline (–11.8%y/y to KES 11.74bn), we believe that are two overlooked bright spots in the company's financial performance. Firstly, we found that volume-driven growth in revenues (+4.6% y/y) as well as solid EBITDA growth (+5.6% y/y) provided evidence that management's strategic initiatives are paying off despite the macroeconomic and policy headwinds. Secondly, we also liked that the company boosted the dividend payout ratio (FY17A: 67% vs FY18A: 77%) despite the profit dip. We discuss other highlights as well as our outlook for the company in the following text.

- **Senator Keg and mainstream spirits to drive 9.3% topline growth in FY19:** We highlight that total revenues marginally grew to KES 73.46bn (+4.6% y/y) driven by growth (+7.0% y/y) in volumes of bottled beer (mainstream mainly), mainstream spirits and Scotch whiskey in particular. Going forward, we believe that EABL's bread and butter businesses will continue catalyzing topline growth. Specifically, we see a rebound in Senator Keg sales primarily owing to the absence of political tension in Kenya as well as the production of Senator at the KES 15bn Kisumu plant from December of this year. We also see EABL benefiting from the more affordable mainstream spirits as a result of the establishment of a KES 0.6bn spirits line in Nairobi. We also see modest beer sales growth owing to the inflation-adjusted excise tax increases that are expected to curtail solid demand growth. We expect Tanzania and Uganda (27% of revenues) to deliver from a mainstream beer perspective. We therefore expect to see revenues growing by 9.3% to c.80bn as a result.

- **EBITDA momentum anchored on deepening operational efficiencies:** We note that the gross profit rose (+4.1% y/y to KES 32.4bn) at a slower pace than total revenues owing to a greater rise in the costs of goods sold (+5.1% y/y). Admin expenses grew at a slower pace (+3% y/y) than inflation (+5% y/y) over the same period while selling and distribution expenses (+19% y/y) rapidly rose as the business ramped marketing for its newer and premium brands. Going into FY19, we believe that efforts to further realize productivity savings and contain admin costs should underpin a slight expansion in the EBITDA margin (FY18: 29% vs FY19F: 30%).

- **Building debt puts pressure on company to sweat its assets:** While we understand that EABL invested more in CAPEX in FY18 (KES 13bn) than in the previous two financial years combined (KES 10.54bn), we believe that increased focus is now on the company's ability to service its KES 27.5bn debt. While our analysis suggests that the company's interest coverage ratio (EBIT divided by interest expenses) is improving (FY19F: 5.56x; FY18A: 5.14x; FY17A: 5.06x), we still note that it is below the 7x level that is considered sustainable. We are therefore watching how the company manages its leverage situation as it is a key source of operational risk going forward.

- **We upgrade our rating to BUY with a TP of KES 273.63 (Previous TP of KES 328):** Generally speaking, we believe that EABL is a top-tier consumer company in Sub-Saharan Africa with robust fundamentals: consistent sales growth, growing operating profits and solid dividend payouts. We upgrade the stock to a BUY as the share price is much lower (-14.2%) than it was 12 months ago thus providing more potential upside. That said, we lower our target price as the FY18 results were weaker than expected. Going forward, we think that the company's growth trajectory will be driven by decent operating profits (through cost containment and innovation) that we expect will a generate stream of earnings (FY19F-23F CAGR: +12.3%) over our forecast period. We therefore expect healthy dividend payouts (FY19F-23F dividend payout ratio: c.55%) as a result and could thus lead to more price gains.

KCB Group: HOLD at TP of KES 54.46, Current Price KES 43.50

- **KCB Group Plc recently released its 1H18 results and realized a PAT growth of 18% y/y to KES 18.1bn with the key highlight being the significant (-59% y/y) drop (to KES 0.8bn) in loan impairments. We give our views below on the company's growth prospects in 2H18**.
- **Robust loan growth to drive NIMs to 8.7% by FY18F**: While it's well known that total interest income grew (+6.0% y/y to KES 32.2bn) thereby reversing the decline in 1H17 (-5.6% y/y), we especially pleased by the organic growth in interest income that was driven more by an expansion in loans and advances (+4% y/y to KES 422bn) at the expense of gov't securities (-3% y/y to KES 524.9bn). On the interest expenses side, we point out that there was robust growth (+12% y/y to KES 8.1bn) owing to the strong growth in customer deposits (+9% y/y to KES 525bn). Going into 2H18, we believe that strengthening loan growth will lead to the NIM advancing to 8.7% in FY18F (vs. 8.5% in FY17A).
- **Cost-to-income ratio to moderate to 49.1% on stringent cost discipline:** While the non-interest revenue (NIR) was flat y/y (KES 11.5bn) owing to a strong decline (-6% y/y to KES 6.8bn) in net fees and commissions (c.60% of NIR), we believe that there is scope for the cost-to-income ratio to decline further in 2H18. We highlight that total opex decelerated for the first time (-1% y/y to KES 17.7) for the first time in at least three years gives life to the evidence that there is likely to be a deceleration in the CTI ratio by FY18F. Our base case is that it will decline to 49.1% (FY17A: 50.9%). We point out, though, that the non interest revenue to total income ratio (1H18: c.33%) could surprise on the upside owing to the strong growth in forex income (+7% y/y) witnessed in 1H18 and thus could make the CTI dip below 49%.
- **Faster loan recoveries underpins lighter asset quality outlook:** The asset quality improved within the second quarter to 8.4% from 9.4% recorded in the first quarter. The cost of risk subsequently declined by c.20bps to 0.4% within the same quarter against the management outlook of 1.3% in FY2018. SMEs contributed the highest chunk of NPL concentration at 15.2%. Secured lending had the lowest NPL concentration at 3.2%, while mortgage and corporate had 7.8% and 11.6% respectively as at the end of first half. Management, however, expects faster loan recoveries in 2H18 that will likely underpin a decrease in the level of NPLs as well as impairments. We expect the NPL ratio to decline to 6% by FY18 and the cost of risk to be 0.8% by the end of the year.
- **We upgrade KCB to HOLD recommendation (from SELL) at a TP of 54.46 (previous 33.97).** KCB is currently trading at a trailing P/B of 1.5x. Given the strong capital adequacy of 17.2% and core capital to RWA ratio of 16%, the stock has a latent potential to rally further. Both the RoAE and RoAA recorded positive year-on year growth of 23.5% from 21.1% and 3.7% from 3.2% respectively. Going forward, we see modest acceleration in loans growth (mid-single digit) on the back of conducive macros. We also see increased cost containment leading to bottom line expansion. We also foresee an improvement in asset quality that is likely to underpin a decrease in impairments in 2H18. Management agreed on an interim dividend of KES 1.00 and with a TP of KES. 54.46, we anticipate an upside of c.11% within the next 12 months from the current price of 43.50. HOLD.

Kenya Power (Unrated): Current Price: KES 5.45

- Kenya Power posted a significant drop in its 1H18 profit before tax (-19% y/y to KES 10.912bn) mainly attributable to an increase in transmission and distribution costs (+1.6% to KES 33.4bn). Total income strongly gained (+11.4% y/y to KES 120.7bn) on the back of an expansion in electricity sales (KES 87.1bn from KES 92.0bn). The increase in electricity sales was driven by domestic consumers (+13.1%) with the street lighting (+43.2%) revenue also contributing strongly to the topline growth. Total power purchase costs however declined marginally to KES 50.5bn (-KES 784m) on the back of reduced non-fuel costs.
- Total operating expenses similarly rose (+12.7% to KES 118.006bn) driven by an increase in network management (+KES 1.7bn to 11.2bn), commercial services (+KES 0.4bn to KES 4.7bn), administration costs (+KES 2.8bn to KES 17.5bn). We do believe that the operating expenses will keep on increasing steadily owing to the company's focus on achieving universal access by FY20F.
- Going forward, Kenya Power aims to implement the Last Mile Connectivity Project aimed at achieving universal electricity access by FY20E at the same time enhancing the efficiency of the power transmission and distribution networks. We do believe the move to enhance the connectivity rate (among retail and commercial clientele) is likely to boost top-line growth and thus should catalyze profit momentum going forward. We also are very constructive about the positive effects of measures aimed at reducing power losses on the grid.
- We note that over the past few years, Kenya Power has been heavily discounted as evidenced by its very low trailing P/E ratio (1.75x). We believe that the current entry level is attractive for the any investor owing to the fact that the valuation is unjustified.

KENOL KOBIL (Not rated): Current Price KES 16.25

KenolKobil managed to grow both EBITDA and PAT by 14% y/y and 16% y/y respectively, during the first half of 2018. This is quite a strong performance, considering the macro headwinds facing the group like fluctuation in global oil prices, inflationary pressures and shrinking market share. An interim dividend of KES 0.36 has been declared which translates to a stellar growth of 20% y/y from KES 0.30 which was paid out in FY2017.

- **Volume growth:** The gross profit slid by 12.2% y/y to KES 3.6bn from a five year high of KES 4.1bn. The EBITDA markedly grew by 14% y/y to a high of KES 3.0bn for the first time in five years. This has consistently been on an upward trend from a low of KES 1.3bn in 2013. The revenue grew by 24% from the same time last year on the back of the increasing international oil prices. Volume recorded a growth of c.8% y/y from all business segments regardless of stiff competition in the sector. The stiff competition is evidenced by Petroleum Institute of East Africa (PIEA) data which pointed out that KenolKobil's share of volume sales narrowed to 9.9% in 1Q18, from 13.2% y/y, thus this growth could be attributed to the trading window in the second quarter.

- **Increased financing costs:** The financing costs significantly climbed by 61% to KES 133m from KES 82m. This was buoyed partially by surging volume and increasing global oil prices. A rise in floating LIBOR rate hiked the borrowing cost of dollar denominated loans raising financing costs higher.

- **Eased operating costs:** Administrative and operating costs declined by 46% y/y to KES 894m from KES 1.7bn. This was attributed to stringent inventory and cash management strategies, efficiency in procurement and absence of huge provisions incurred in the first half of 2017. A two fold growth was incurred on currency translation which recorded a gain of KES 27m from a loss of KES 26m in 2017.

- **Ratio analysis:** The current ratio remained resilient at 1.44x y/y, while the gearing ratio firmed by 35% y/y to 0.9x from 0.7x. Shareholders funds improved by a growth of 9% from KES 11.2bn in 2017 to KES 12.2bn in 2018. Net cash incurred in operating activities was KES 1.2bn which is a slump from KES 2.5bn generated in 2017, this implies a 150% decline y/y. Nevertheless, the cash and cash equivalents spiked by two fold to KES 1.1bn from KES -1.2bn y/y.

- **Expectations:** The group acknowledges that the positive performance has been triggered by cost containment and efficient allocation of resources across all business segments. The macros in relation to the oil industry are anticipated to be favorable for business in key markets during the second half of 2018. Given the past ability to absorb shocks from adverse fluctuation in global oil prices, the management is braced to meet profitability and revenue targets in FY2018. We expect to have a positive growth in profits and dividends.