Insurance Sector: Initiation of Coverage

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Diamonds in the rough….

Analysts

Samuel Mugacha

E-mail: samuel.mugacha@fib.co.ke

William Githui

E-mail: william.githui@fib.co.ke

Pauline Muiruri

E- mail: Pauline.muiruri@fib.co.ke

Bernard Kiarie

E-mail: bernard.kiarie@fib.co.ke

Head Office:

Crawford Business Park, Ground floor

State House Road Tel: +254- 020-7606026-37

www.fib.co.ke

P.O Box 45236, 00100
Nairobi.

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INVESTMENT SUMMARY

We initiate coverage on the insurance sector with a POSITIVE OUTLOOK.

The insurance sector is a key enabler in the growth and development of the economy through providing risk mitigation measures to individual or firms making huge investments.

In 2012, the global insurance premiums increased by 2.3% to USD 2,621 billion after contracting by 3.3% the previous year. This growth was largely supported by emerging markets whose premiums expanded by 4.9% while advanced markets recorded a 1.8% growth.

In Africa, we note that the contribution by the continent to the global insurance premiums remains low at 1.6%, which is boosted by countries with relatively high penetration levels such as South Africa, Namibia, Mauritius and Kenya.

However, growth in insurance premiums continues to be high driven by the expanding middle class. According to the African Development Bank (AfDB) the middle class accounted for more than a third (34.3%) of the total population compared to 26.2% of the population in the 1980's and 27.0% in the 1990's.

Although the insurance penetration in Kenya is considered one of the highest in Africa at 3.2% (2012), it still remains low when compared to South Africa which is at 14.2%.

Going forward, we believe the game changer in the Kenyan insurance sector is the development of micro insurance. According to the Centre for Financial Regulation and Inclusion, over 12 million Kenyans earn between USD 2.00 and USD 10.00 per day, forming a significant market segment for micro insurance.

In addition, World Bank statistics show that out of the 2 million adults that are formally employed, only 30.0% (600,000) of the individuals currently use any form of insurance, including the mandatory National Hospital Insurance Fund (NHIF) and National Social Security Fund (NSSF).

Metric (2013)	Britam	CIC Insurance	Jubilee	Kenya Re	Liberty	Pan Africa
Gross earned Premiums	8,847,166	10,067,665	18,087,946	9,645,151	7,397,981	5,324,099
EPS	1.22	0.65	41.79	4.29	2.15	13.05
BVPS	7.77	3.09	193.67	25.61	10.61	34.78
Investment Income /Total Income	18.2	7.0	20.5	20.0	35.6	18.0
P/B	2.4	2.9	1.6	0.8	2.1	3.9
ROE	15.7	20.9	21.6	16.7	20.2	37.5
ROA	5.7	8.2	4.1	10.6	3.5	5.9
Target Price	23.97	11.56	516.85	26.10	24.33	144.43
Recommendation	BUY	NEUTRAL	BUY	BUY	NEUTRAL	NEUTRAL
Upside potential	35.4%	4.7%	66.7%	31.7%	8.1%	6.2%

GLOBAL INDUSTRY OVERVIEW

The insurance sector is a key enabler in the growth and development of any economy. The sector encourages huge investments to be taken by an individual or a firm, by providing risk mitigation measures through absorption of risk and minimizing the impact of large losses on firms and individuals.

The sector also improves the efficiency of other segments of the financial sector, such as banking and bond markets by enhancing the value of collateral through property insurance and reducing losses at default through credit guarantees and enhancements.

Global life insurance grew along with the overall economy during the sixties, but in the seventies high inflation and interest rates reduced the attractiveness of life savings policies, lowering the penetration rate in Europe and North America even as it took off in Japan.

Insurers reacted by introducing new policies linked to the performance of underlying investments to provide at least a partial hedge against inflation. As interest rates and inflation began to fall in the eighties, life insurance boomed, increasingly supported by emerging markets and worldwide penetration peaked at 4.75 percent in 2000.

Non-life insurance penetration in advanced markets increased steadily from 1962 to mid-eighties. Growht was first fuelled by the increase in vehicles and growing economic wealth and later by the rapid expansion in liability lines. In emerging markets, penetration is still increasing due to a rising middle class and increasing risk awareness.

Industry Performance

Global life insurance premiums increases by 2.3% in 2012.

In 2012, the global life insurance premiums increased by 2.3% to USD 2,621 billion after contracting by 3.3% in the previous year. Growth is still lagging behind the average pre-crisis (2006) level of 7.7% for life and 1.5% for non-life.

Emerging markets life premiums grew 4.9% while advanced markets grew 1.8% during the same period.

During the same period, Emerging Markets growth improved with life premiums expanding by 4.9%. Advanced markets growth stood at 1.8 %, (2011: -3%), largely supported by the robust performance in advanced Asia and the US while Western Europe continued to shrink.

Global Non-life premiums increased by 2.6% in 2012**.**

Non-life (general insurance) premiums increased by 2.6% in 2012 to USD 1,992 billion (2011:1.9%). In emerging markets, non-life premiums had a growth of 8.6% in 2012 (2011:8.1%) while advanced markets growth picked up to 1.5% (2011:0.9%).

World Insurance Premiums (USD Billion)

	2008	2009	2010	2011	2012
Life premiums	2,490.00	2,332.00	2,516.00	2,627.00	2,621.00
Life growth rate	*-3.50%*	*-2.00%*	*3.20%*	*-2.70%*	*2.30%*
Non-life premiums	1,780.00	1,735.00	1,819.00	1,970.00	1,992.00
Non-life growth rate	*-0.80%*	*-0.10%*	*2.10%*	*1.90%*	*2.60%*

Source: Swiss Re

According to Price Waterhouse Coopers [PWC] (Life Insurance 2020: Competing For a Future), demand for life cover has been slowing down. This was attributed to the disillusionment created by the financial crisis that dented public trust and changed customers' risk appetite and perception. This presents a challenge to life insurance companies on how to regain public trust.

However, we note that the rapid growth of towns and cities in emerging markets presents insurers with tremendous growth opportunities.These opportunities will be in the form of wealth protection (as purchasing power for luxuries increases) and health.

Regulatory Changes

Some of the key focus areas include the implementation of the Insurance Core principles (ICPs) by the International Association of Insurance Supervisors(IAIS) and Solvency II Directive by the European Union.

As more jurisdictions begin to implement the ICPs, assessing how to accommodate multi-jurisdictional compliance and reporting requirements has increasingly become a challenge.

The Solvency II Directive is meant to ensure insurers have enough capital set aside to provide reserve funds to cover all insurance claims that they are likely to receive.

The directive has set standards which cover three main areas:

a) **Valuation of assets/liabilities and capital requirements:** - Covers how assets such as government bonds, equities and property that they own are valued. They also cover the amount of funds insurers need to hold in reserve to make sure they can pay policyholders' claims.
b) **Governance and risk management:** - Entails how the structure and management of insurance business is governed, enabling insurers to identify, measure, monitor, manage and report risks to which they are exposed.
c) **Reporting and disclosure:** - Ensures what information insurers report on their business and how it is reported.

The solvency II Directive was expected in January 2014

Full implementation of solvency II was expected in January 2014. Insurers were required to provide their solvency II capital positions to regulators.

The transition to a more risk-sensitive regulatory regime will lead to higher capital requirements and increased capital costs for certain risk exposures.

SUB-SAHARAN AFRICA

Africa continues to be the lowest contributor to the global insurance premium at 1.6%.

Africa continues to register the lowest contribution to the global insurance premium at 1.6%. This average is boosted by relatively high penetration levels in South Africa, Namibia, Mauritius and Kenya.

Life insurance premiums increased approximately by 14.0% in 2012.

Life insurance premiums in Africa are estimated to have increased by 14.0% to USD 50 billion in 2012, compared to 2.9% in 2011. South Africa, the region's dominant market, accounts for around 90.0% of regional life premium volume. In South Africa premiums were up by 14% in 2012 compared to 2.9% in 2011 driven by increases in new policies as well as retirement annuities. Life insurance penetration in SSA, though very low, is increasing gradually along with rising awareness of the benefits of insurance.

According to AfDB, Africa's middle class has been steadily rising since the 1980s.

According to the African Development bank (AfDB), Africa's middle class has been steadily rising since the 1980s. During this period, the middle class accounted for 26.2% of the population, standing at 111 million. A decade later it had risen to 27.0% or 196 million and by 2010 more than a third (34.3%) of the population was middle class.

According to AfDB, the middle class includes individuals with annual income exceeding USD 3,900 in purchasing power parity (PPP) terms or with daily per capita expenditure between USD 2.00 to USD 4.00 and those with daily per capita expenditures between USD 6.00 and USD 10.00. Recent estimates by AfDB put the size of the middle class in the region in the range of about 300 to 500 million people.

We expect demand for insurance to increase as people seek better health care for themselves and their families. Lifestyles will also improve in the form of wealth acquisition thus creating a need to protect that wealth as risk aversion increases.

GDP growth in Sub-Saharan economies expanded marginally by 5.3% in 2012 compared to 5.2% in 2011.We are likely to see this growth pick up in 2013 mainly due to strong domestic demand coupled with resource-based investments in resource rich countries. The continent's current GDP in real terms is estimated to be USD 1.6 trillion and expected to grow to USD 2.6 trillion by 2020.

GDP growth in Sub-saharan economies expanded marginally by 5.3% in 2012 compared to 5.2% in 2011.

As a result of this current and expected growth, insurance and reinsurance companies have been on hand to tap into the opportunities and challenges provided by this economic expansion. In addition, insurance companies can also be seen as financial intermediary investment companies with long investment horizons thereby enabling them to tap into the growth of the economies through direct investments.

In the long-term, SSA is expected to maintain a solid average real GDP growth of 5.5% per year between 2014 and 2017. Natural resource development projects and oil production will be key drivers of growth and the insurance industry will benefit from solid economic environment particularly in the business lines related to the booming natural resource sector. As the discovery and exploration of natural resources in SSA continues, the opportunity for insurance in the region continues to widen.

In Eastern Africa, oil and gas discoveries in Kenya and Uganda will require huge investment in capital in form of equipment that will need to be insured.

According to the Swiss Re, oversight has largely improved in Sub-Saharan Africa (SSA) with strengthened regulation and improved supervision. This will lead to consolidation, a better-capitalized industry and increased consumer confidence in insurance services.

KENYAN INSURANCE SECTOR

Brief Introduction

The insurance sector in Kenya is regulated by the Insurance Regulatory Authority (IRA). The IRA is a statutory agency established under the Insurance Act 2006 CAP 487 of the laws of Kenya to regulate, supervise and develop the insurance industry. The authority is a precursor to the then office of the Commissioner of Insurance that came into existence with the enactment of the Insurance Act in 1986. Prior to this, insurance regulation was based on the UK legislation under the Companies Act 1960.

The authority works with industry players in achieving the following fundamental objectives: Ensuring compliance by insurance/reinsurance companies and intermediaries with legal requirements and sound business practices; Promoting voluntary compliance; seting clear objectives and standards of intervention for insurance/reinsurance companies; Protecting consumers and promoting high degree of security for policyholders, promoting efficient, fair, safe and stable market; Maintaining the confidence of consumers in the market; Ensuring insurance/reinsurance companies remain operationally viable and solvent ; Establishing a transparent basis for timely, appropriate and consistent supervisory intervention including enforcement

Kenyan insurance sector has 46 insurance companies,170 brokers and 4,862 agencies

Industry Players

The Kenyan insurance sector is comprised of 46 insurance companies, 170 insurance brokers and 4,862 insurance agencies.

Year	Insurance companies	Agents	Brokers	Investigators	MIPS	Insurance surveyors	Risk managers	Loss adjusters	Motor assessors
2007	43	2665	201	213	21	30	8	23	-
2008	42	3356	141	152	19	19	6	17	-
2009	44	3320	154	112	25	29	6	20	60
2010	46	3847	159	121	26	26	10	22	74
2011	45	4578	168	128	28	28	8	21	89
2012	46	4862	170	140	24	27	10	21	92

Source: AKI report 2012

Insurance penetration in Kenya is among the highest compared to other countries in Sub Saharan Africa. Most African countries have penetration levels well below 1.0%. Insurance penetration levels for some African countries and other regions are shown in the table below.

	2010 (Life)	2010 (Non-Life)	**2010 Total**	2011 (Life)	2011 (Non-Life)	**2011 Total**	2012 (Life)	2012 (Non-Life)	**2012 Total**
Kenya	1.05	2.05	**3.1**	1.02	2	**3.02**	1.08	2.08	**3.16**
South Africa	12	2.8	**14.8**	9	2.6	**11.6**	11.56	2.6	**14.16**
Nigeria	0.1	0.4	**0.4**	0.2	0.7	**0.9**	0.18	0.51	**0.68**
Mauritius	3.99	1.86	**5.85**	2.7	1.8	**4.5**	4	1.94	**5.94**
Germany	3.45	3.75	**7.2**	3.16	3.64	**6.8**	3.09	3.65	**6.74**
India	4.39	0.71	**5.1**	3.4	0.7	**4.1**	3.18	0.78	**3.96**

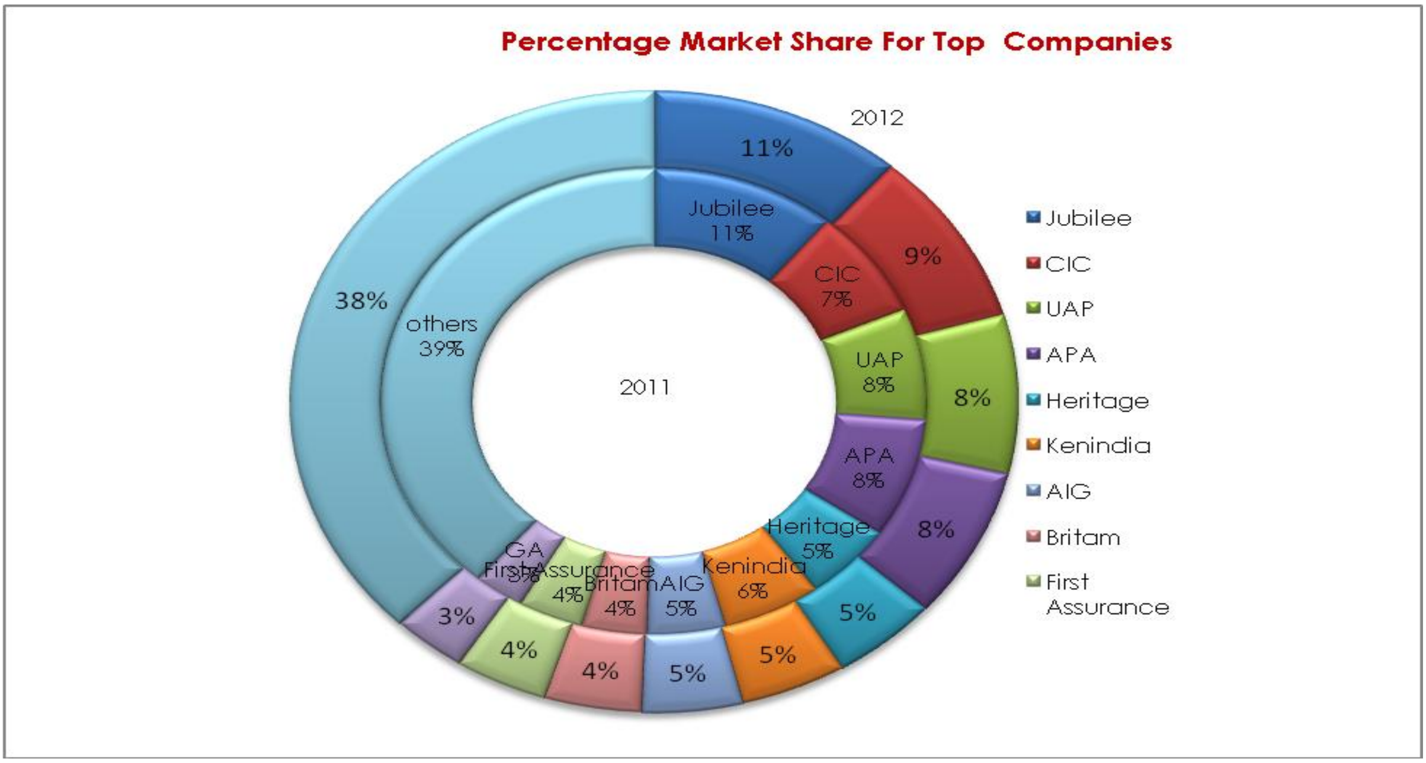
Source: World Bank insurance report and AKI reports

Apart from South Africa, Namibia, and Mauritius, most African countries lag the rest of the world in terms of insurance penetration. With an insurance penetration of 3.2%, Kenya is still considered to have a low penetration level when compared to other developed markets such as Germany (6.7%) and South Africa (14.2%).

Top 10 Insurance Companies and Market Share

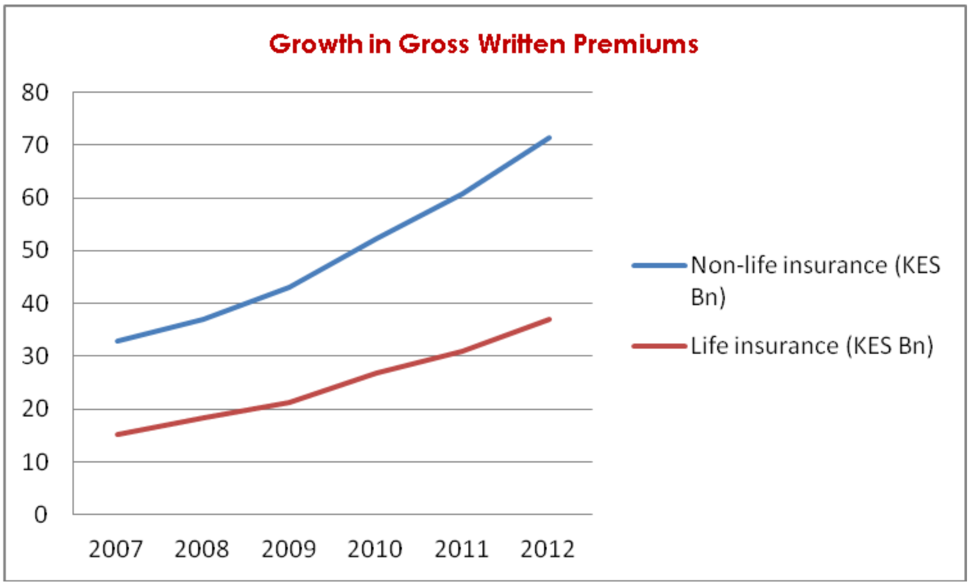
	Trend in Gross Premiums KES '000			Trend in Market Share		
	2010	**2011**	**2012**	**2010**	**2011**	**2012**
Jubilee	4,711,566	6,660,922	8,085,352	9.00%	10.98%	11.31%
CIC	2,961,208	4,580,309	6,557,122	5.66%	7.55%	9.18%
UAP	3,866,576	4,715,514	5,925,796	7.38%	7.77%	8.29%
APA	4,611,408	5,019,780	5,590,038	8.81%	8.27%	7.82%
Heritage	2,477,112	3,248,925	3,405,694	4.73%	5.36%	4.77%
Kenindia	3,341,735	3,565,694	3,376,542	6.38%	5.88%	4.72%
AIG	2,612,757	2,803,897	3,203,367	4.99%	4.62%	4.48%
Britam	1,785,090	2,349,216	3,112,745	3.41%	3.87%	4.36%
First Assurance	2,089,694	2,370,141	2,942,554	3.99%	3.91%	4.12%
GA	1,411,585	1,817,674	2,351,860	2.70%	3.00%	3.29%

Source: AKI (Figures in KES '000)



INDUSTRY PROFIT

Kenya Gross written Premium for the period 2007-2012



Source: AKI

Statement of Comprehensive Income (KES Bn)	2008	2009	2010	2011	2012	CAGR
Gross Earned Premium	46.32	53.92	63.47	70.92	84.38	16.18%
Net Earned Premium	36.48	42.80	50.17	55.30	64.42	15.28%
Investment & Other Income	11.75	15.10	23.98	19.36	34.13	30.54%
Net Incurred Claims	24.83	30.66	39.50	37.69	48.36	18.13%
Total Commissions & Expenses	18.35	21.41	25.12	27.29	35.39	17.84%
Profit/(loss) before tax	5.05	5.83	9.53	9.68	14.80	30.84%
Profit/(loss) after tax	3.85	4.29	7.80	7.64	11.82	32.37%

Source: AKI

2012 Gross Written Premium per Class

Class of business (KES Bn)	Amount	% of Total Premium
Motor commercial	17.4	24.3
Motor Private	12.7	17.8
Medical	13.1	18.3
Fire(Domestic & Industrial)	8.3	11.6
Others	20	28
Total	**71.5**	**100**

Source: AKI Report 2012

RATIO ANALYSIS

Loss Ratio

	2007	2008	2009	2010	2011	2012
Enterprise group(Ghana)	-	52.49%	-	92.39%	107.46%	-
Liberty Kenya	-	-	84.90%	76.90%	58.60%	78.10%
Britam	65.60%	56.00%	60.20%	104.40%	60.70%	61.70%
Jubilee Insurance	54.30%	50.10%	51.40%	49.50%	50.10%	54.80%
Kenya Re insurance	49.30%	43%	42.90%	40.30%	43.80%	54%
CIC insurance	34.80%	28.70%	32.80%	32.90%	36.50%	63.70%
AIICO (Nigeria)	0.90%	4.08%	54.72%	54.49%	50.61%	40.92%
African Alliance (Nigeria)	12.97%	23.28%	25.14%	18.14%	16.93%	85.48%
Sanlam Ltd (South Africa)	29.13%	28.97%	29.26%	26.93%	27.02%	27.65%
Liberty Holdings (South Africa)	-	-	-	-	-	-

Expense Ratio

	2007	2008	2009	2010	2011	2012
Enterprise group(Ghana)	-	-	-	62.97%	78.68%	-
Liberty Kenya	-	-	-	38.40%	44.00%	54.90%
African Alliance(Nigeria)	53.46%	45.15%	50.99%	30.88%	43.49%	35.42%
CIC insurance	28.10%	29.10%	30.10%	29.00%	28.20%	-
Britam	32.20%	25.20%	28.10%	26.20%	26.00%	25.90%
Jubilee Insurance	29.40%	26.30%	24.20%	24.50%	24.60%	23.50%
Pan Africa	15.30%	40.20%	36.80%	17.00%	22.20%	16.70%
AIICO(Nigeria)	16.59%	17.70%	11.60%	11.60%	27.87%	31.14%
Kenya Re insurance	20.10%	21.40%	17.60%	16.30%	13.50%	15.40%
Liberty Holdings (S.A)	-	-	-	-	-	-
Sanlam Ltd (S.A)	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%

Combined Ratio

	2007	2008	2009	2010	2011	2012
Enterprise group(Ghana)	-	52.49%	-	155.37%	186.14%	-
Liberty Kenya	-	-	-	115.20%	102.60%	132.90%
Britam	97.80%	81.20%	88.30%	130.60%	86.70%	87.60%
Jubilee Insurance	83.60%	76.40%	75.60%	74.00%	74.70%	78.30%
African Alliance(Nigeria)	66.22%	68.43%	76.14%	49.02%	60.42%	120.90%
Kenya Re insurance	69.30%	64.40%	60.50%	56.60%	57.20%	69.40%
CIC insurance	62.90%	57.80%	62.90%	61.80%	63.70%	63.70%
AIICO(Nigeria)	17.49%	21.78%	66.32%	66.09%	78.48%	72.06%
Sanlam Ltd (S.A)	29.13%	28.97%	29.26%	26.93%	27.02%	27.65%
Liberty Holdings (S.A)	-	-	-	-	-	-

Investment Income/Total Income

	2007	2008	2009	2010	2011	2012	2013
Liberty Kenya	-	-	15.20%	29.40%	25.50%	34.70%	35.6%
Jubilee Insurance	31.70%	30.10%	18.80%	22.00%	25.50%	22.00%	20.5%
Britam	51.40%	19.60%	18.70%	13.20%	38.3%	16.8%	18.2%
Kenya Re insurance	14.60%	14.10%	22.30%	25.90%	17.90%	25.00%	20.0%
Pan Africa	17.90%	12.80%	10.60%	8.70%	18.10%	15.80%	18.0%
CIC insurance	5.90%	8.00%	6.60%	6.00%	8.90%	8.90%	7.0%

COMPARATIVE ANALYSIS

Net Profit Margin

	2007	2008	2009	2010	2011	2012	2013
Kenya Re insurance	118.3%	133.9%	34.6%	30.9%	28.9%	35.3%	31.1%
Britam	137.3%	63.0%	67.1%	114.8%	-34.9%	36.8%	30.0%
African Alliance(Nigeria)	30.22%	25.57%	20.33%	16.27%	-1.32%	14.99%	-
Jubilee Insurance	14.60%	10.90%	11.70%	20.70%	14.90%	13.70%	12.7%
Enterprise group(Ghana)	15.95%	16.23%	5.53%	5.27%	19.86%	18.70%	-
AIICO(Nigeria)	6.53%	6.88%	27.77%	31.02%	-0.15%	7.80%	-
CIC insurance	5.40%	7.90%	8.60%	12.40%	9.60%	17.00%	14.0%
Pan Africa	9.70%	-3.8%	4.6%	15.4%	12.2%	12.8%	23.5%
Sanlam Ltd (South Africa)	10.42%	12.51%	7.21%	8.18%	9.48%	6.37%	-
Liberty Holdings (S.A)	2.92%	4.84%	0.10%	4.66%	5.49%	4.97%	-
Liberty Kenya	-	-	-27.10%	5.40%	14.90%	12.80%	14.9%

Price to Book (P/B)

	2007	2008	2009	2010	2011	2012	2013
Liberty Kenya	-	-	-	-	0.21	0.68	2.12
Jubilee Insurance	2.66	1.93	1.53	1.78	1.37	1.29	1.57
Kenya Re insurance	-	-	-	0.63	0.38	0.51	0.77
Britam	-	-	-	-	0.93	0.91	2.38
Pan Africa	3.32	2.51	1.63	1.72	0.94	1.47	3.91
CIC insurance	-	-	-	-	-	1.41	2.91
Sanlam Ltd (south Africa)	1.6	1.21	1.53	1.72	1.64	2.35	-
Liberty Holdings (South Africa)	2.1	1.54	1.88	1.77	1.72	2.06	-
Nigerian company(AIICO)	2.04	1	-	-	0.36	0.38	-
Nigerian co(African Alliance)	-	-	-	-	-	1.35	-
Enterprise group(Ghana)	-	-	2.2	1.11	1.25	0.63	-

Price to Earnings (P/E)

	2007	2008	2009	2010	2011	2012	2013
Liberty Kenya	-	-	-	-	0.64	4.21	10.48
Jubilee Insurance	15.54	8.7	6.76	4.97	4.7	4.94	7.30
Kenya Re insurance	-	-	-	4.3	2.29	2.68	4.61
Britam	-	-	-	-	-	4.29	15.19
Pan Africa	-	-	15.57	5.33	4.49	5.54	10.42
CIC insurance	-	-	-	-	-	5.55	13.93
Sanlam Ltd (S.A)	10.08	12.56	10.15	10.74	11.13	14.98	-
Liberty Holdings (S.A)	7.18	8.81	10.67	7.48	7.75	7.74	-
AIICO (Nigeria)	42.18	19.97	-	-	-	3.29	-
African Alliance (Nigeria)	-	-	-	-	-	-	-
Enterprise group(Ghana)	-	-	-	-	-	-	-

Return on Equity (ROE)

	2007	2008	2009	2010	2011	2012	2013
Kenya Re insurance	52.8%	57.3%	14.60%	14.60%	16.60%	19.20%	16.7%
Jubilee Insurance	17.2%	22.3%	24.1%	33.0%	28.5%	26.3%	21.6%
Enterprise group(Ghana)	25.5%	22.10%	8.10%	9.53%	34.48%	36.86%	-
CIC insurance	18.4%	23.20%	23.80%	18.60%	13.60%	25.40%	20.9%
Pan Africa	14.0%	8.10%	10.50%	32.20%	20.90%	26.60%	37.5%
Liberty Holdings (S.A)	26.9%	13.14%	0.40%	21.53%	21.45%	26.41%	-
Britam	60.0%	42.9%	9.50%	12.00%	-22.9%	20.2%	15.7%
Sanlam Ltd (S.A)	18.8%	8.75%	15.32%	17.98%	15.75%	15.99%	-
African Alliance(Nigeria)	15.3%	15.72%	13.61%	10.72%	-0.92%	17.92%	-
AIICO(Nigeria)	5.0%	6.64%	17.13%	19.80%	-.0.16%	12.45%	-
Liberty Kenya	-	-	-42.80%	5.60%	22.80%	16.40%	20.2%

Return on Assets (ROA)

	2007	2008	2009	2010	2011	2012	2013
Kenya Re insurance	29.40%	33.60%	8.90%	8.90%	10.00%	11.80%	10.6%
Enterprise group(Ghana)	9.68%	9.20%	3.34%	3.87%	14.21%	13.82%	-
African Alliance(Nigeria)	11.48%	11.64%	9.21%	6.73%	-0.51%	7.49%	-
CIC insurance	4.30%	5.80%	6.80%	6.50%	5.30%	9.90%	8.2%
AIICO(Nigeria)	2.81%	3.72%	11.26%	14.16%	-0.08%	4.12%	-
Britam	16.60%	2.20%	2.80%	4.20%	-7.6%	7.0%	5.7%
Jubilee Insurance	3.7%	3.5%	3.9%	6.0%	5.0%	4.8%	4.1%
Pan Africa	3.30%	-1.60%	1.80%	5.50%	3.90%	4.20%	5.9%
Sanlam Ltd (south Africa)	1.62%	0.75%	1.34%	1.59%	1.39%	1.37%	-
Liberty Kenya	-	-	-4.50%	1.10%	3.90%	3.20%	3.5%
Liberty Holdings (S.A)	0.69%	0.51%	0.02%	1.05%	1.09%	1.38%	-

Regulatory Developments

- **Introduction of Electronic Regulatory System (ERS)**

In 2014, the Insurance Regulatory Authority (IRA) launched an electronic regulatory system (ERS).This is a web based system that enables regulated insurance entities log into the system using a portal to complete and submit all required returns online.

ERS will improve data depth, consistency, quality and accessibility which will enable the authority to achieve a dynamic model of supervision known as Risk based Supervision that is in line with international standards. This will improve efficiency and effectivess in regulation enhancing financial stability of the industry.

This sytem will be value adding to the insurance industry. It will enable insurance companies to submit data and information in a less cumbersome manner hence. As a result, it will offer convenience and ensure efficiency and accuracy in the returns received from insurers.

- **Adoption of Solvency II**

Plans are underway to adopt Solvenvy II standard f

Plans are in place for the insurance companies to adopt the Solvency II standard formula by using specific parameters in calculating their risk capital. This is an important element of the solvency II standard formula because it allows for better assessment of undertaking-specific risk profiles in the standard formula which in turn lead to a more accurate calculation of the solvency capital requirement.

A more pinpointed assessment of unique risks is important for specialist undertakings, as it allows them to produce a solvency capital requirement that is calibrated for the specific risk environment that will better reflect a company's risk profile

The current regulation on solvency ratio stands at 10.0%. Adoption of this standard will put pressure on the insurance companies' capital adequacy ratios.

- **Establishment of a Fraud Unit**

A fraud unit was established in 2011 to curb fraud in the insurance industry.

Fraud constitutes some of the reasons that have contributed to the negative perception and image of the insurance industry by the public and has been cited as the number one reason for the financial woes that have befallen most companies.

In response to the escalating cases of fraud in the industry, there was need for establishing an insurance investigations fraud unit (The Kenya Police Anti-Fraud Insurance Unit) which was launched in September 2011.

This is expected to curb fraud in the insurance industry that affects insurers' profitability as well as eroding consumer and shareholder confidence.

- **Breakdown of Composite insurance**

The regulation states that insurance business should be separated into life and non-life business

Based on the revised version of the Insurance Act 2013, an insurer that carries more than one class of long term insurance business or more than one class of general insurance business, shall keep separate accounts of receipts and payments in respect of each prescribed class of insurance business carried on by the company.

The regulation is on separation of insurance business into long-term (life) and short-term (general) business for easier monitoring by the regulatory bodies and better accountability.

One of the impacts of separation of business units will be the new capital requirements. Insurers must have a realistic assessment of both present and projected liabilities/surplus assets as well as projected solvency assessment of the demerged units.

Another key element will be an assessment of whether the existing cost structures are optimal and profit testing of existing products using the expected post demerger cost structure.

Most demerged Kenyan insurance companies are adopting the use of a shared services model which involves centralization of services such as branding, research and development, legal services and customer service.

This regulation is expected to create opportunities for the composite insurer to acquire demerged units from other insurers which might be on sale or lead to consolidation. In extreme circumstances a composite insurer might decide to dispose off the non-core business line if it does not make business sense to run the unit on a stand-alone basis.

- **Motor insurance cap on premium**

The IRA has put a minimum cap of 7.5% for private motor insurance.

The insurance regulatory authority has put a minimum cap of 7.5% for new insurance covers on private motor insurance and a discount of upto a minimum of 3.5% can be given subsequently on renewal after zero caims.

Although this was done to curb the current unethical behavior of rate undercutting seen among the players, industry sources still insist that the undercutting prevails due to companies competing for good business at a minimal cost to the insured.

KEY THEMES

- **Micro Insurance**

Microinsurance is the development of insurance products specifically targeted to the large population at the bottom of the pyramid.

Over 12 million Kenyans earn between USD 2.00 and USD 10.00

According to The Centre forFinancial Regulation and Inclusion (Cenfri), over 12 million Kenyans earn between USD 2.00 and USD 10.00 per day, forming a significant market segment for micro insurance.

In addition, World Bank statistics show that out of the 2 million adults that are formally employed, only 30.0% (600,000) of the individuals currently use any form of insurance, including the mandatory National Hospital Insurance Fund (NHIF) and National Social Security Fund (NSSF).

About 3 million Kenyans have not been reached

Market sources estimate that there are approximately 600,000 life policies on record which indicates that out of the potential market of 3,584,952 people classified as the middle class by FinAcess (adult population earning above KES 10,000 per month), about 3 million Kenyans have not been reached and are a potential market for insurance companies.

According to the World Bank, the improving economic conditions over the past decade have led to an improved living standard for most Kenyans. Kenya's poverty rate is currently estimated at between 34.0% from 47.0% in 2008.

Some micro-insurance products offered by Panafric Life like M-bima, which is a funeral cover benefit of KES 25,000 is charged at KES 60 per month while a medical cover by Britam called Linda Jamii charges KES 12,000 per annum for a sum assured of KES 250,000. This shows that the 12 million Kenyans can afford such products. This would translate to KES 152.6 billion in annual revenues (Gross written premiums), assuming they each take a funeral and medical cover.

Therefore, micro insurance holds the key to the growth of insurance penetration given the large informal sector that has no access to financial services coupled with the untapped formally employed population.

- **Alternative distribution channels**

i) Bancassurance

Bancassurance involves partnerships between insurers and banks to distribute insurance products

This involves partnerships with banks to distribute insurance products through their branch and agency networks. There are 5.4 million Kenyans estimated to hold bank accounts compared to 600,000 with life insurance policies in 2011. This presents a huge opportunity in the untapped bankable population that is uninsured.

Furthermore, according to Cenfri, 85.0% (or 3.9 million) Kenyan adults with bank accounts do not currently have any form of insurance product.

Bancassurance offers a cheapers alternative route-to-market

Banking penetrates further into rural communities than insurance often does leading to cost-efficient access to insurance products. Bancassurance thus offers a cheaper alternative route-to-market. Leveraging on the banks' branches also offers an effective route given the dynamism and understanding of banking services as compared to insurance services. This partnership enables banks to enrich some of the financial products by offering insurance protection as additional benefits.

According to world bank, bancassurance has had a dramatic impact on increasing sales volumes.

According to World Bank, in some developed countries it has had a dramatic impact on increasing sales volumes attaining market shares in excess of 40% in life and more than 10% in non-life.

The table below shows countries where the Bancassurance market share has shown important growth and exceeds 40% (life) or 10% (non-life):

Country	Bancassurers' Life Premium Share(%)	Bancassurers' Non-Life share(%)
Australia	43%	Very Small
Belgium	48%	6%
Brazil	55%	13%
Chile	13%	19%
France	64%	9%
Italy	59%	2%
Malaysia	45%	10%
Portugal	88%	10%
Spain	72%	7%

Source: World Bank report on Bancassurance as a valuable tool for developing Insurance (2012)

ii) Technology

Local insurance companies are increasingly adopting technology enabled platforms to distribute insurance products. Listed insurance companies that have adopted technology in distributing insurance products include Pan Africa (BimaMkononi), Britam (Linda Jamii), CIC Insurance (M-Bima) and Jubilee Insurance (yuCover). Partnerships with mobile telecommunication service providers have helped insurance companies reach the uninsured population through mobile phones.

According to CCK statistics, mobile subscribers in Kenya have increased from 11.9 million in 2008 to 31.3 million in 2013.

Accessibility of mobile phones and evolution of technology has made this channel the most efficient way of reaching the uninsured masses. According to a report by Communications Commission of Kenya (CCK), the use of mobile phone financial services rose from 49.4% in 2011/12 to 61.5% in 2012/13.

CCK statistics show that mobile subscribers have increased from 11.9 million in 2008 to 31.3 million in 2013 while mobile penetration has grown from 35.3% to 76.9% during the same period.

Insurers can also reduce their service costs by increasing the use of self-service options among mobile customers.

With 19.7 milliom internet users, the internet is also a channel that can be used to reach the uninsured.

The internet is also a channel that can be used to reach those who are not insured. The report by CCK reveals that there are 19.7 million internet users (internet penetration of 48.3% compared to 35.5% in the previous year).

Furthermore, 1 in 4 Kenyans at the bottom of the pyramid (mobile phone owners) browse the internet on their mobile handset.

Under-investing in these channels today means turning away from the future and the next generation of younger, digitally savvy consumers. Developing and utilizing low-cost direct-sales channels (internet and mobile) should reduce the reliance and cost of intermediaries for distribution like the traditional agents whose cost is up to 40.0% of premiums.

Why is insurance penetration in Kenya low?

Insurance penetration in Kenya stand at 3.2%.

According to AKI, the level of insurance penetration in Kenya is at 3.2% and has constantly remained below the African average which is currently at 3.6%.

Some of the reasons we see for the low insurance penetration in the country include:

62.9% of Kenyans earn below KES 5,000 monthly

Unaffordability due to low income levels: According to a 2013 survey by FinAccess and Central bank of Kenya, approximately 62.9% of Kenyans earn below KES 5,000 monthly as shown in the table below.

The population figures were based on the 2009 census results. Using the total number of the adult population (19,483,435), we computed the absolute figures for the number of adults in the different income levels.

Monthly Income (KES)	Percentage of Adult Population	Population Level Estimates
0	3.9%	759,854.0
0-1,000	18.6%	3,623,919
1000-3000	22.9%	4,461,707
3000-5000	17.5%	3,409,601
5000-10000	18.7%	3,643,402
10000-20000	9.9%	1,928,860
20000-50000	6.4%	1,246,940
50000-100000	1.3%	253,285
>10000	0.8%	155,867
TOTAL	**100%**	**19,483,435**

The cost of basic food and non-food items per month is KES 2,900 in rural areas and KES 5,400 in urban areas.

According to the last Kenya Integrated Household Budget Survey done in 2005, the cost of basic food and non-food needs per month for one adult was established at KES 1,562 for rural areas and KES 2,913 for urban areas. *Throughout this report, the poverty rate or headcount refers to people living in households with per adult equivalent expenditures below these amounts.*

Adjusting for increases in prices since 2005 to 2012 using the Consumer Price Index (CPI), the approximate cost levels have increased to KES 2,900 per month for rural areas and KES 5,400 per month for urban areas. Therefore, a Kenyan earning KES 5,000 and living in the urban area will find it difficult to pay insurance premiums. Based on our table above, approximately 3.6 million Kenyans earning KES 10,000 and above can afford an insurance product.

Insurance companies should target the low income earners

In order to increase the level of insurance penetration in the country, insurance companies should target the low income earners who constitute the largest segment of the society through tailor-making and packaging affordable micro-insurance products. In addition to this, increased investment in brand awareness and product sensitization should be a priority to penetrate across all classes of the uninsured population.

Llack of trust of insurers by the public.

Negative perception towards insurance: There is a general lack of trust of insurers by the public which has reduced consumer confidence and reduced uptake of insurance products.

Collapse of Insurance companies in the past.

Collapsed Insurers: There is a general fear regarding sustainability of insurance companies and capability to meet their obligations. This has been exacerbated by companies that have collapsed in the past and caused policy holders to incur losses or have delayed settlement of claims.

Below is a table highlighting some of the insurers that have collapsed:

Name of Insurer	Class of business	Year
Kenya National Assurance Co ltd	Composite(life & general)	1996
Access Insurance Co ltd	General	1998
Stallion Insurance Co ltd	General	2002
Lake star Insurance Co ltd	General	2002
Liberty Insurance Co ltd	General	2003
United Insurance Co. Ltd	Composite	2005
Blue shield Insurance	Composite	2011

Lack of awareness of and understanding

Inadequate consumer education and awareness: Majority of Kenyans are unaware of the need to mitigate the numerous potential risks like death, fire, accident, illness, theft and natural disasters such as flood and drought. Insurance companies need to invest in product awareness and improve general education in terms of nurturing high rsik awareness in order to write more premiums.

Culture and Religion: The African Culture hinders insurance uptake especially life covers that are perceived to encourage discussion surrounding planning for one's death which is considerd a taboo in some cultures and an abomination in some religions. Different cultural groups demand different kinds of insurance e.g according to muslims, conventional insurance is not aligned to shariah(Islamic law) since it involves fixed interest, excessive risk taking, uncertainity and unclear terms and investment in unacceptable industries such as breweries or gambling.

GROWTH DRIVERS

- **GDP growth**

There is a strong positive correlation between gross earned premium growth and GDP growth

Data from the World Bank indicates that Kenya GDP growth improved from 3.0% in 2009 to 5.0% in 2012. The chart below depicts the strong correlation (0.87) between gross earned premium growth and GDP growth over the 2009–2012 period.

The world bank estimates that Kenya's GDP will increase by 5.2% in 2014

The World Bank estimates that Kenya's GDP will increase by 5.2% (2014 and 2015) and by 5.4% in 2016. As a result, we expect gross earned premium to maintain growth at its average rate (18.5% 2009-2012).

Average income and wealth will rise in line with the growing economy as evidenced by increasing Gross Domestic Product(GDP) per capita .

Increased disposable income leads to acquisition of wealth and assets that need to be insured.

According to the Kenya National Bureau of Statistics, Gross National Disposable Income grew at an average of 13.4% (2009-2011) with Gross National Disposable Income per Capita growing by 10.4% during the same period. Increased disposable income leads to acquisition of wealth and assets that need to be insured against their respective risks. This in turn creates demand for insurance products to cater for these needs.

- **Population Growth and Favourable Demographics**

Favorable demographics such a large youth population are indicative of a promising growth potential.

Key demographic trends show not only specific areas of growth potential, but also highlight liability imbalances, and reveal impending growth limitations when viewed in conjunction with penetration figures.

Favorable demographics, such as a large youth population, are indicative of promising growth potential.

According to a World Bank research on what drives the development of the insurance sector, a large population produces not only a potential clientele for insurance products but also provides for a larger risk pool. Furthermore, population density has a positive effect on insurance due to reduction in marketing cost and ease in distribution.

The table below shows the population growth of the country from 2008 to 2012 according to

	2008	2009	2010	2011	2012	CAGR
Population(Mn)	37.75	38.77	39.82	40.91	42.03	2.72%

Source: World Bank Estimates

The data above shows that population growth was on an upward trend in the last 5 years. in the boundless opportunities presented by the massive consumer potential.

- **Government spending**

The Kenya government has earmarked key development projects such as the KES 1.2 trillion standard Gauge railway, the KES 41.3 billion Nairobi bypass and the KES 20.0 billion expansion and modernization of Jomo Kenyatta International Airport.

Insurance companies are set to benefit from infrastructure investment

Insurance companies are set to benefit from infrastructure investment and government spending together with it's development partners. The occupational safety and health act provides for all persons lawfully present at workplaces, whether temporary or permanent, to have insurance cover to protect them from work related injuries or other health hazards.

This provides a huge opportunity for the insurance industry to grow their premiums through provision of insurance.

In addition, on completion of these project, insurance companies come in as risk mitigators against large unforeseen losses.

- **Urbanization**

Urbanization and growth of towns and cities will present insurers with opportunities

According to the World bank, 24.0% of the total population live in the urban areas with an annual rate of urbanization at 4.36%. This is an indication that more and more Kenyans will move to the urban centers with time.

This rapid growth of towns and cities will present insurers with opportunities in terms of risk management and business development. Growth in urban centres presents an opportunity for growth of insurance in terms of property insurance, covers for protection against fire and terrorism. With increased formal employment as companies open up their branches in these new cities, there will be increased co-operate covers in medical and group life insurance.

Furthermore, the need to accommodate ever-growing urban populations will entail huge infrastructure investments which may yield construction cover premiums.

Urbanization brings fundamental socio-economic change and a new risk landscape. With higher population density and concentration of assets, towns and cities are more vulnerable to health hazards and prone to large losses should they be hit by natural disasters and environmental issues such as air and water pollution. Purchasing power in the urban areas tends to generally be higher than the rural areas.

- **Regional expansion**

Regional expansion by local insurance companies will increase their presence

Local insurance companies have continue to increase presence in regional countries in order to tap into the growing potential in those markets. CIC insurance is currently in the process of partnering with regional savings & cooperatives in Uganda, Malawi and South Sudan. Britam acquired Real insurance with a presence in Mozambique, Malawi and Tanzania. Jubilee insurance has also mentioned plans to expand into new markets.

Low penetration rates in potential markets.

According to Insurance regulatory bodies in Uganda and Tanzania , Insurance penetration level in Uganda stands at 0.65% and 0.89% in Tanzania. South Sudan has an insurance penetration rate of less than 1.0 % and Malawi's stands at 1.45%. The low penetration levels provide headroom for growth.

- **Devolution/County governments**

Devolution and formation of counties has increased public expenditure t

Following the formation of counties, increased public expenditure is expected at the county level. The Treasury allocated KES 198.7 billion towards county governments during the 2013/2014 financial year. The new Ministry of Devolution and Planning was allocated KES 84.8 billion of which KES 68.3 billion was set aside for development expenditure.

The large portions dedicated towards development expenditure are indicative of increased economic activities that provide new opportunities for insurance companies. Majority of the insurance companies are looking to form partnerships with the 47 county governments and are leveraging on their branches, brokers and bancassurance in order to cash in on the new markets.

KEY INDUSTRY RISKS

The main risks in the insurance industry is fraud and price undercutting

Fraud: Insurance fraud has led to an increase in the cost of premiums and has thus limited the number of people who can afford insurance.It is estimated that about 40.0% of all claims paid out by insurance companies in Kenya are fraudulent. The collapse of more than ten insurance companies in Kenya in the last two decades has been attributed to fraudulent claims.

Price undercutting: One of the major challenges facing the insurance industry is premium price under-cutting that has led to unfair competition. In our observation, poor pricing strategies can lead to short-term business expansion at the expense of sustainable financial position. Under-pricing leads to lower margins and also leads to poor estimations of reserving needs (an insurer's capacity to reserve adequately for future claims).

CONCLUSION

Our sample comparables consist of insurance companies in Sub-Saharan countries with insurance penetration levels higher (South Africa, Namibia and Mauritius) and lower (Nigeria and Ghana) than Kenya's.

RECOMMENDED COMPARABLES

	Combined Ratio	Loss Ratio	Expense Ratio	P/B	P/E	ROE	ROA
NIGERIA							
Custodian & Allied	69.8	44.25	25.56	0.51	3.23	16.18	6.98
Continental Re	111.19	57.94	53.25	0.79	6.31	12.73	7.13
GHANA							
Enterprise Group	-	-	-	4.12	12.32	26.1	15.6
SOUTH AFRICA							
Sanlam	26.88	26.88	-	2.75	14.02	20.88	1.61
Liberty Holdings	-	-	-	2.01	7.93	23.64	1.21
NAMIBIA							
Santam	85.54	69.29	16.24	3.78	18.81	19.24	5.29
Sanlam	26.88	26.88	0	2.71	13.83	20.88	10.62
MAURITIUS							
Mauritius Union Assurance	77.6	68.09	9.51	1.84	11.43	16.55	2.78
Mauritian Eagle Insurance	74.73	54.63	20.1	1.37	7.59	19.86	3.2
Average				**2.21**	**10.61**	**19.56**	**6.05**
Median				**2.01**	**11.43**	**19.86**	**5.29**

Notably, the listed Kenyan insurance companies had a higher average ROE (22.5% - 2012) than majority of our sample comparables and are trading at relatively lower P/B multiples than their Sub-Saharan counterparts.

BRITISH AMERICAN INVESTMENT COMPANY LTD (Britam)

Bloomberg Ticker	BRIT:KN
Fair Value (KES)	23.97
Price in KES - 07.05.2014	17.70
Issued Shares (Mn)	2,150.00
Market Cap (KES Mn)	38,055.00
Market Cap (USD Mn)	437.41
Year End	Dec 31st
Free Float (%)	55.44
KES/USD (87.00)	

Source: Bloomberg

Investment Summary

BUY recommendation on Britam

We initiate coverage on Britam, with a **BUY recommendation** and a price target of KES 23.97. This represents an upside potential of 35.4% from the current share price of KES 17.70 (as at 7th May 2014).

Britam is a financial services group in East Africa with primary investments in composite insurance, asset management services, banking and property.

Shareholding structure

The table below shows the shareholding structure of Britam as at 28th February 2014.

Sharholder	Shares	Percentage
British American (Kenya) Holdings Limited	452,504,000	21.05%
Equity Holdings Limited	405,000,000	18.84%
Jimnah Mwangi Mbaru	219,300,000	10.20%
Benson Irungu Wairegi	100,298,400	4.67%
Kenya Commercial Bank Nominees A/C 915F	91,404,035	4.25%
James Mwangi	75,000,000	3.49%
Peter Kahara Munga	75,000,000	3.49%
Co-op Bank Custody A/C 4012	60,000,000	2.79%
Filimbi Limited	58,453,600	2.72
Standard Chartered Nominee Account KE16521	17,165,300	0.80%
Others	337,326,515	15.69%
Totals	1,891,451,850	100.00%

Our recommendation is informed by the following key growth drivers:

Britam launches linda Jamii in FY2014

Microinsurance: In the beginning of FY2014, Britam launched Linda Jamii, its first microinsurance product. The product is priced at KES 6,000 for 6 months or KES 12,000 for an insurance period of one year. The benefits for the different insurance periods include; KES 200,000 and KES 75,000 inpatient limit per family for the 12 month and 6 month insurance cover respectively.

Britam invests KES 2 billion in an ICT platform

Technology: Britam is investing KES 2 billion in an ICT platform which will result in increased efficiencies in the various business lines. As a result, we expect the staff costs to gross earned premiums ratio to decline.

Real acquisition

The Real Deal: Through the acquisition of Real Insurance Company, the firm will increase its presence from the current 4 countries to 7 countries, with the addition of Tanzania, Malawi and Mozambique. All of these countries have lower insurance penetration than Kenya.

	FY2011	FY2012	FY2013	FY2014F	FY2015F
Gross Earned premium (KES '000)	5,607,622	6,849,693	8,847,166	11,389,992	14,813,694
Return on Average Equity (ROaE)	-24.5%	24.0%	18.0%	18.3%	18.9%
Return on Average Assets (ROaA)	-8.5%	8.2%	6.4%	6.4%	6.4%
P/E x	-20.60	16.00	15.19	12.05	9.99
P/B x	4.71	3.23	2.38	2.05	1.76
EPS	-0.90	1.16	1.22	1.53	1.85
BVPS	3.93	5.72	7.77	9.03	10.53
Loss Ratio (Net claims/ Net earned premiums)	60.7%	61.6%	62.3%	63.0%	62.3%

Source: Annual report & Faida Estimates

Brief History

Britam was incorporated on 26th July 1995

Britam was incorporated in Kenya on 26th July 1995. Britam is a financial services group in East Africa with primary investments in composite insurance, asset management services, banking and property.

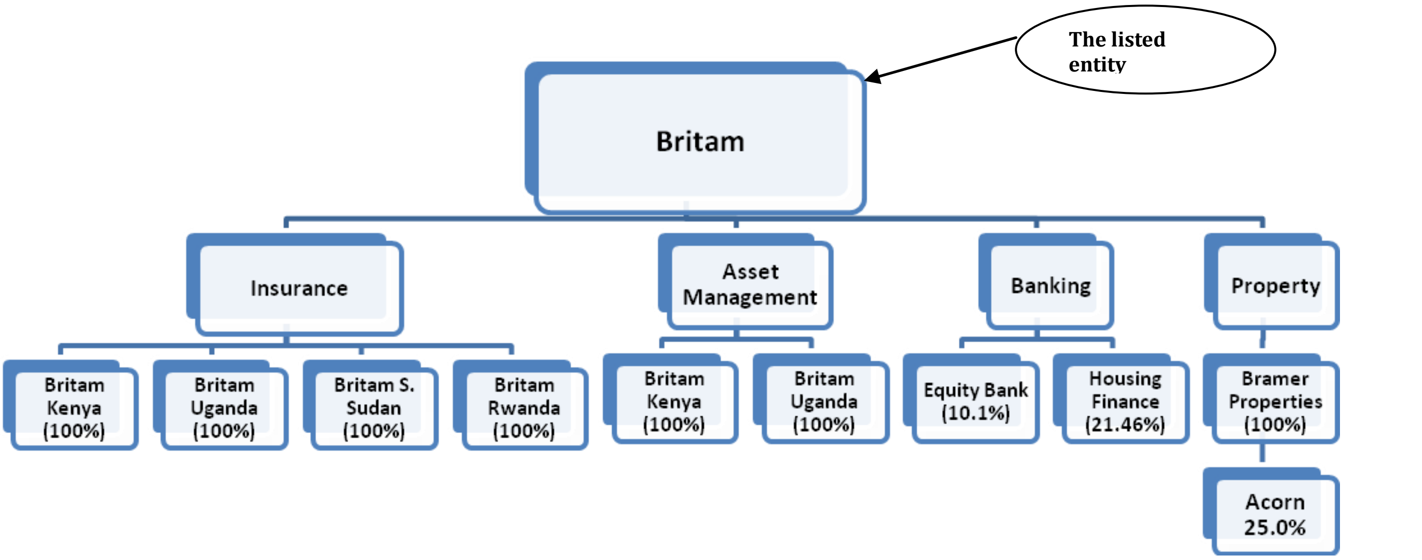
The Kenyan operation, British American Insurance Company, was established in 1965 and has been known as a provider of both life and general insurance. In 2004, the owners of British-American Insurance Company formed British-American Investments Company which in turn established British-American Asset managers limited.

Britam was listed In the NSE

Britam was listed on the Nairobi Securities Exchange (NSE) on 2nd September 2011 through an initial price offering (IPO) and at a price of KES 9.00.

Business profile and subsidiaries

The chart below represents an overview of the business structure of Britam together with its investments in other business lines, subsidiaries and associates.



Source: Britam

Britam has a market share of 4.4% in general business

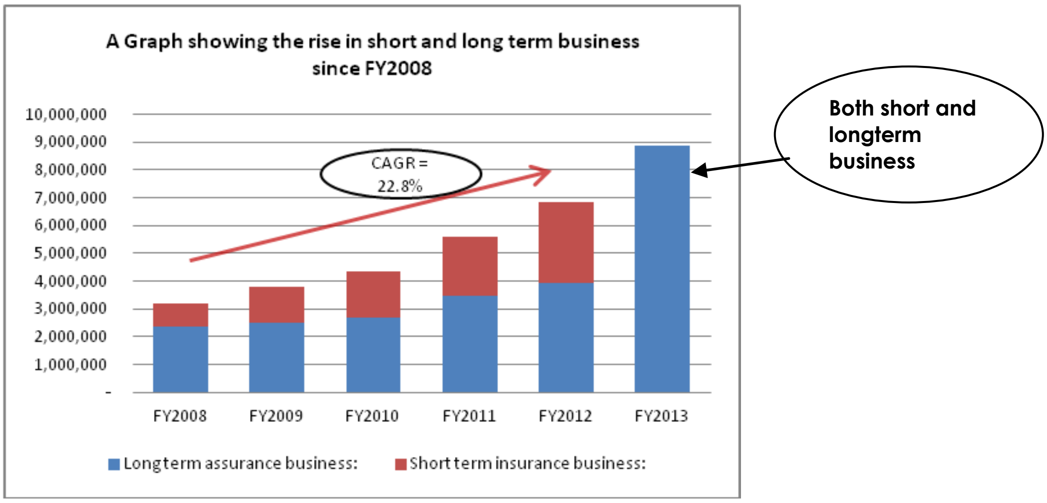
Ordinary life market share 23.3%

Insurance

Britam insurance has evolved over the years from a small insurance company to a composite insurance company with a market share of 4.4% in general business in 2012.

During the same year, Britam had the largest market share in ordinary life insurance (23.3%). The group life business was the third largest in the industry with an 11.0% market share.

The insurance premiums for the group have grown at a compounded annual growth rate (CAGR) of 22.8% from KES 3.2 billion in FY2008 to KES 8.8 billion in FY2013 as shown in the graph below.



Source: Company & Faida Estimates

General business grew at a CAGR of 37.2%

During the 5 years under review, the company's general business grew at a much faster rate (CAGR of 37.2%) than the life insurance business (CAGR of 13.9%). This was in line with the industry growth trends, an indication of higher uptake of general insurance compared with life insurance.

Life premiums collected by the industry represented 33.7% of total premiums

According to the Association of Kenya Insurers (AKI), the industry's life business and non life business over the same period grew at a CAGR of 14.8% and 15.6% respectively. Total industry life premiums collected in 2012 accounted for 33.7% of total premiums while the remaining 66.3% came from non-life business.

As the table below shows, the contributions by general business to the total revenues for Britam have constantly been increasing over the review period;

	FY2008	FY2009	FY2010	FY2011	FY2012
Long term business	74.1%	66.1%	61.7%	62.0%	57.6%
Short term business	25.9%	33.9%	38.3%	38.0%	42.4%
Total	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**

Source: Annual report

Premiums from general business are expected to surpass life business

Going forward, we expect premiums from the general business to surpass those from the long term business, driven mainly by the acquisition of Real Insurance. In 2012, Real Insurance Group was able to write a total of KES 3.9 billion compared to Britams' KES 6.8 billion (KES 3.9 billion and KES 2.9 billion written for long term and general business respectively). The Kenyan business of Real Insurance had total premiums amounting to KES 2.2 billion (about 56.4% of the total profits earned by the company).

Asset Management

BAM was started in 2004

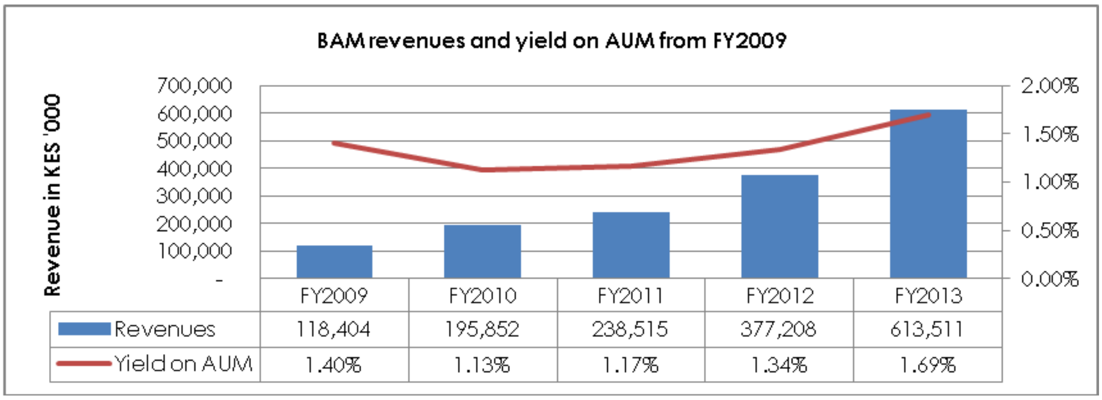
Britam Asset Managers (BAM) was started in 2004 with the purpose of offering asset management and investment advisory services to individuals and institutional clients among them Britam Insurance.

The main source of revenue earned by a fund management firm include fund management fee which is calculated as a percentage of the funds under management. This percentage ranges between 0.25% - 0.75% for discretionary funds and 1.0% - 2.0% for unit trusts.

Revenues grew at a CAGR of 50.9%

Britam's revenues from this business line grew at a CAGR of 50.9% from KES 118.4 million (FY2009) to KES 613.5 million in FY2013. The assets under management grew at a CAGR of 43.9% to KES 36.3 billion (FY2013) from KES 8.5 billion (FY2009).

The yield on AUM rose steadily from 1.1% in FY2010 to 1.7% in FY2013 as shown in the graph below.



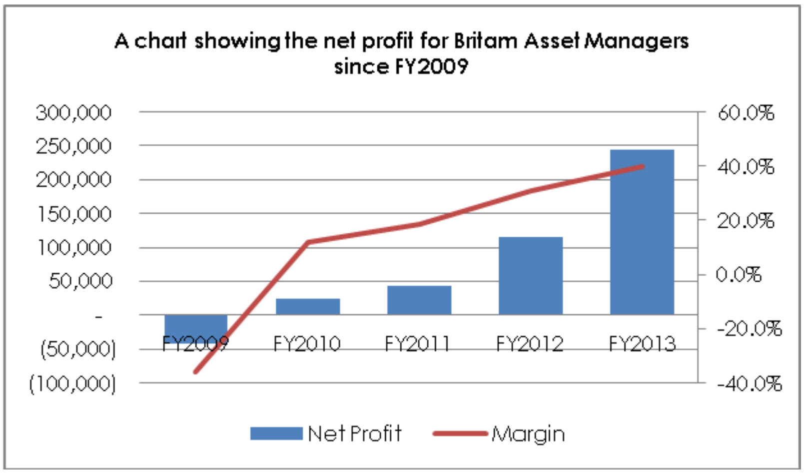
Source: Annual Report & Faida estimates

Yield on AUM dropped to 1.1%

However, the yield on AUM in FY2010 dropped to 1.1% from 1.4% in FY2009 which we attribute to increased competition in the industry resulting in undercutting and lowering of management fees.

Net profit on an upward trend.

The net profit was on an upward trend, rising from a loss of KES 42.6 million (FY2009) to a profit of KES 243.6 million (FY2013). Net profit margin grew by 9.0% to 39.7% from the 2012 level of 30.7%.



Source: Britam Annual Reports & Faida Estimates

Banking

Britam is the second largest single shareholder in Equity bank.

Britam is the second largest single shareholder in Equity Bank with a 10.6% stake. This investment was done in 2004 and the bank subsequently listed on the Nairobi Securities Exchange through introduction in 2006. The market capitalization of Equity Bank has grown by more than 3X (352.0%) from KES 25.2 billion in December 2006 to KES 113.9 billion in December 2013.

Britam's share of investment in associate has grown by 128.7% to KES 181.7 billion in FY2013 from KES 79.4 billion in FY2011.

Slower but steady increase in capitalization

Going forward, we are likely to see slower but steady increases in market capitalization as the bank positions itself to go after the Small and Medium sized Enterprises.

Britam invested in Housing Finance in 2007 and has a 21.46% stake in the firm. Housing finance is one of the largest mortgage companies in East Africa. With a housing deficiency of over 150,000 per annum against a supply of 30,000 houses annually, the bank is exposed in an undersupplied industry poised for growth.

Growth Drivers

Micro Insurance

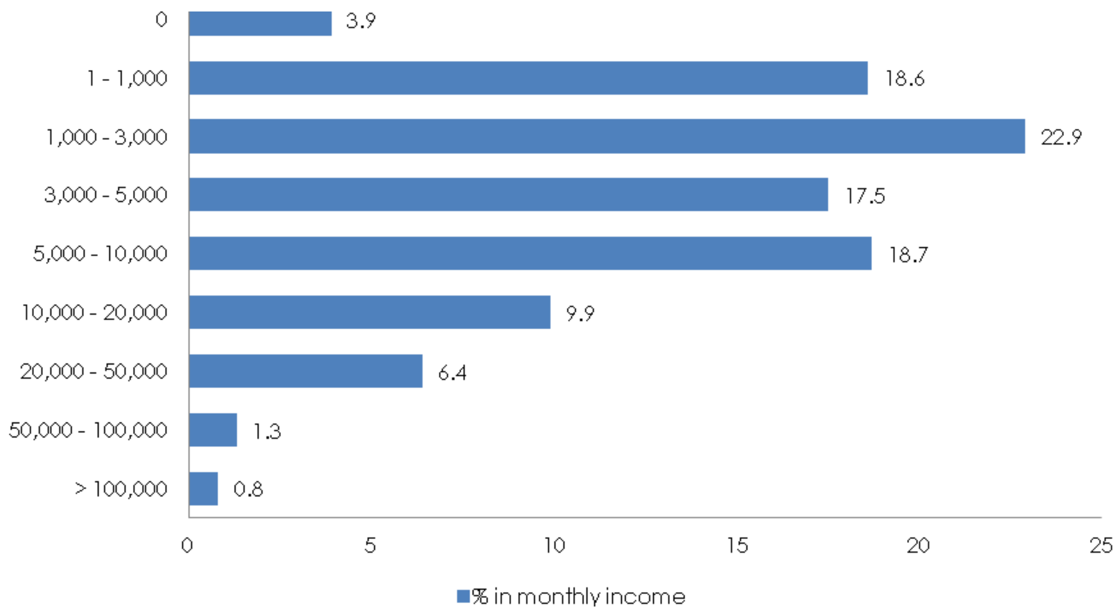
Britam partners with safaricom

At the beginning of FY2014, Britam in partnership with Safaricom launched a micro insurance product called Linda Jamii. This is a micro health cover that provides medical insurance to the lower middle segment of the economy.

The linda Jamii product is priced at KES 6,000 for 6 months or KES 12,000 for an insurance period of one year. The benefits for the different insurance periods include; KES 200,000 inpatient and KES 75,000 inpatient limit per family for the 12 month and 6 month insurance cover respectively.

The company budgeted to spend KES 100 million this financial year for marketing of Linda Jamii.

A chart showing the % of the population at different income levels of the population in Kenya



Source: FinAccess Survey 2013

35.0% of the population earn KES 5,000 to KES 50,000

As the chart above shows, 35.0% of the population earn between KES 5,000 to KES 50,000 per month which is a potential market for micro insurance.

Britam targets to underwrite 1 million policies in the current FY2014. This translates to total annual written premiums of approximately KES 12 billion on the year of launching the product.

Assuming they achieve a 10.0% success rate on their target (which is more realistic in our view), the microinsurance product could contribute approximately KES 1.2 billion in FY2014.

Technology

23.0% of total premiums paid agents and commissions

Since 2007, Britam spent an average of 23.0% of total premiums in paying commissions to agents/brokers for bringing in insurance business. By FY2013, commissions payable stood at KES 1.9 billion.

In order to lower the cost attributed to this distribution channel, the company is leveraging on technology to reach a wider population at the lowest unit cost possible.

The partnership with Safaricom will also facilitate payment of premiums through the Mpesa platform.

Safaricom provides first contact

Safaricom, through its wide customer base, approximately 20 million customers, facilitates first contact with the potential customers. Consequently, this opens up an avenue for further communication for marketing of a wide array of insurance products.

Investing KES 2 billion in an ICT platform

Additionally, Britam is investing KES 2 billion in an ICT platform which will result in increased efficiencies in the various business lines. As a result, we expect the staff costs to gross earned premiums ratio to decline. This ratio has been declining steadily from 8.2% in 2008 to 6.9% in 2012. However, we expect this ratio to rise slightly to 7.5% in the short term, given the Real Insurance expansion.

Real Estate

Bramer properties owns a 25.0% stake in Acorn

Bramer Properties, a fully owned subsidiary of Britam is a property investment company which owns 25.0% stake in Acorn, a property development company.

The investment proposition for Britam to go into the property development space is to play on both the supply and demand side.

AUM of KES 36.3 billion

Supply Side: *With Assets under management of KES 36.3 billion, Britam is able to fund these developments. According to management, the capital requirement for the real estate investments being done by the company in 2014 stands at KES 3 billion for a total of 15 deals in 5 broad categories, i.e.*

- ✓ *Mixed use development (commercial and retail)*
- ✓ *Business class hotels (in the outskirts of Nairobi)*
- ✓ *Shopping malls*
- ✓ *Master plan community*
- ✓ *Class A buildings such as the Britam towers*

Demand side: *With a network of High net worth individuals and pension funds coupled with experience in development of investment products such as unit trusts, the company is able to tailor make products to be used as exit channels. An example of an exit channel is the use of Real Estate Investment Trusts (REITs). Exit via REITS wil earn the company returns on their investments faster than putting the property in the market for a buyer.*

Regional Subsidiaries/ Real Insurance

Britam has a presence in 4 countries

Britam currently has a presence in a total of 4 countries in the region, i.e. Kenya, Uganda, South Sudan and Rwanda. In FY2013, Britam made a bid to acquire 99.0% of Real Insurance.

Real insurance has a presence in 4 countries including Kenya

Real Insurance Company, formerly known as Royal Insurance Company East Africa Ltd has a presence in 4 African countries; Kenya, Tanzania, Malawi and Mozambique, where its an underwriter of general business. Through this acquisition, Britam will increase its presence in Africa to a total of 7 countries.

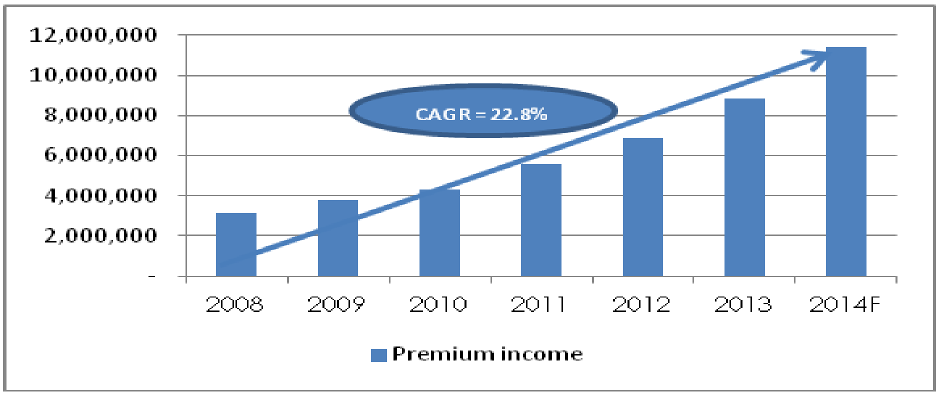
The table below shows the penetration levels of insurance business in the particular countries Real Insurance and Britam are exposed

Country	Insurance Penetration
Kenya	3.20%
Uganda	0.65%
Tanzania	0.89%
Rwanda	2.30%
Malawi	1.45%
Mozambique	1.50%

Full integration of Real Insurance into Britam is likely to be completed by the end of 2014. Management expects the 1H2014 results to be consolidated with Real Insurance results.

Full integration likely to be completed end of FY2014

Financial Analysis & Forecasting



Source: Annual Report & Faida Estimates

Steady premium income growth: Britam's premium income grew consistently at a CAGR of 22.8% from FY2008 to FY2013 as shown by the graph above. This growth was buoyed by a strong agency business which has seen the company's commissions payable as a percentage of total earned premiums average at 22.7% since FY2007 to FY2013.

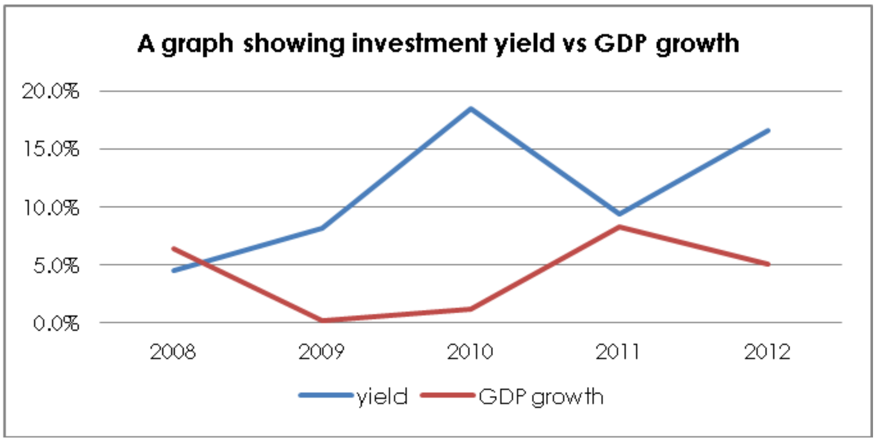
Premium income grew consistently at a CAGR of 22.8%

Going forward, we are likely to see the premium income for the group continue with its upward trajectory. As a result, we forecast premiums of about KES 11.4 billion in FY2014, largely boosted by the acquisition of Real Insurance.

Investment income: As the graph below shows, Britam maintained a yield on investment income above the real GDP for the country since 2009. Going forward, we are likely to see the group achieve the same trend, of returns above the economic growth, given the higher yielding investments the group is exposed in such as property.

Yield on investment income above real GDP

According to management, the average investment income yield on property for the group is about 29.0%.



Government of Kenya projects GDP to grow by 5.1% in 2014

The Government of Kenya projects the country's GDP to grow by 5.1% in 2014 and reach the 7.0% target in 2017, we are likely to see financial services firms benefit from this growth as GDP per capita also increases with the rise in GDP.

The Government of Kenya also intends to raise USD 2 billion through a Eurobond which, if successful, is likely to result in a drop in interest rates and an increase in liquidity. This will then result in an upsurge of the listed equity market, increase loan book growth for banks and result in a drop in government bond rates.

Income Statement (KES '000)	FY2011	FY2012	FY2013	FY2014F	FY2015F	FY2016F
Gross earned premium	5,607,622	6,849,693	8,847,166	11,389,992	14,813,694	16,443,201
Outward reinsurances	(670,914)	(893,001)	(1,095,967)	(1,357,458)	(1,700,545)	(1,894,187)
Net earned premiums	**4,936,708**	**5,956,692**	**7,751,199**	**10,032,534**	**13,113,150**	**14,549,014**
Fund management income	238,315	377,208	613,511	925,628	1,396,530	1,550,149
Investment income	1,296,161	1,971,010	2,759,463	3,545,900	4,316,733	4,936,786
Commissions earned	237,900	307,639	370,521	510,911	664,485	737,578
Other income	62,960	53,184	47,096	65,528	72,736	80,737
Total income	**3,382,675**	**11,743,379**	**15,130,058**	**18,872,469**	**23,772,718**	**26,526,346**
Net Claims and Policyholders benefits	2,999,016	3,669,331	4,826,720	6,322,799	8,170,619	9,069,387
Commissions payable	1,192,335	1,476,086	1,873,286	2,585,609	3,362,814	3,732,724
Operating and other expenses	1,760,544	2,286,578	3,210,990	4,133,883	5,376,481	4,651,626
Total Expenses	**5,186,206**	**9,040,823**	**12,115,583**	**15,024,528**	**19,110,198**	**19,896,051**
Share of results of associate	**79,436**	**146,845**	**181,685**	**180,928**	**200,830**	**222,921**
Profit before tax	**(1,724,095)**	**2,849,401**	**3,196,161**	**4,028,869**	**4,863,350**	**6,853,217**
Profit after tax	**(1,957,314)**	**2,519,456**	**2,653,789**	**3,345,191**	**4,038,065**	**5,690,261**
Earnings per share						

Balance Sheet (KES '000)	FY2011	FY2012	FY2013	FY2014	FY2015	FY2016
Shareholders' funds	**8,557,448**	**12,472,324**	**16,934,797**	**19,680,067**	**22,957,789**	**27,048,544**
Assets						
Investment in associate	1,360,608	1,459,826	1,867,081	2,072,460	2,300,431	2,553,478
Investment properties	1,405,294	1,706,057	3,782,181	3,492,083	4,214,121	5,052,754
Equity investments	4,281,483	6,084,289	7,632,998	9,003,726	10,952,885	13,324,004
Government securities	4,590,787	6,862,342	8,731,227	10,499,843	12,651,505	13,981,010
Deposits in financial institutions	2,463,976	1,975,913	2,591,418	3,336,236	4,339,070	4,816,368
Total Assets	**25,639,245**	**35,820,165**	**46,902,578**	**56,957,599**	**68,635,529**	**79,150,137**
Liabilities						
Total gross insurance liabilities	7,370,421	10,467,211	12,137,169	14,218,140	16,934,272	19,949,177
Unearned premiums reserve	982,778	1,292,195	1,889,452	2,432,513	3,163,698	3,511,705
Total Liabilities	**17,081,796**	**23,347,841**	**29,967,781**	**37,277,531**	**45,677,740**	**52,101,592**
Net Assets	**8,557,448**	**12,472,324**	**16,934,797**	**19,680,067**	**22,957,789**	**27,048,545**

VALUATION

Valuation using price to book multiple

We valued Britam using Price to Book multiple methodology, whereby we used the 2013 forecasted BVPS and a sample Sub-Saharan trailing P/B to arrive at our price target.

Our valuation methodology was informed by the fact that insurance companies as is the case with other financial institutions, mark to market a majority of their balance sheet.

P/B Multiple Valuation	
Current Market Price (7.05.14)	18.00
Trailing sample P/B	2.65X
Trailing company P/B	2.38X
Forecasted BVPS: 2014	KES 9.03
Target Price	**23.97**
Upside Potential	**33.1%**

RECOMMENDATION

BUY recommendation

We initiate coverage on Britam, with a **BUY recommendation** and a price target of KES 23.97. This represents an upside potential of 35.4% from the current share price of KES 17.70 (as at 7th May 2014).

CIC GROUP LTD (CIC)

Bloomberg Ticker	CIC:KN
Fair Value (KES)	11.56
Price in KES - 07.05.2014	11.05
Issued Shares (Mn)	2,179.62
Market Cap (KES Mn)	24,084.75
Market Cap (USD Mn)	276.84
Year End	Dec 31st
Free Float (%)	21.0
KES/USD (87.00)	

Source: Bloomberg

Investment Summary

We maintain our **NEUTRAL** recommendation on CIC Group Ltd (CIC) with a target price to KES 11.56 which represents a potential upside of 4.7% from the current share price of KES 11.05 (As at 8th May 2014).

Since we our initiation of coverage in 2012, the market capitalization for the company risen by 150.6% from KES 7.7 billion in December 2012 to KES 19.3 billion in April 2014.

The table below shows the top 10 shareholders of CIC as at 28th February 2014

NEUTRAL recommendation

Market capitalization has gone up by 150.6%

Shareholder	Number of shares	Percentage
Co-operative Insurance Society LTD	1,619,534,420	74.3%
Gideon Maina Muriuki	102,001,920	4.7%
Standard Chartered Nominee Non Resident A/C 9011	20,351,700	0.9%
Welton Weda	12,269,000	0.7%
Nelson Chege	11,591,500	0.5%
Peter Mutarura Mwaura	10,286,280	0.5%
Kenya Reinsurance Corporation	9,000,000	0.4%
NIC Custodial Services A/C 077	8,281,200	0.4%
Standard Chartered Nominee A/C KE 18361	7,917,000	0.4%
Standard Chartered Nominee A/C KE 9598	7,200,000	0.3%
Subtotal	**1,808,433,020**	**83.0%**
Others	371,182,420	17.0%
Total	**2,179,615,440**	**100.0%**

Our rating is informed by the following developments, which also serve as key growth drivers:

Micro-Insurance: In FY2013, CIC wrote micro insurance premiums worth KES 600 million. It expects to write KES 1 billion micro insurance business in FY2014, with an annual growth of KES 1 billion thereafter.

Co-operative Bank of Kenya has been the most successful Bancassurance partner

Bancassurance: In FY2013, Bancassurance accounted for 15.4% of the total insurance premiums written by the firm. One of the most successful Bancassurance partnership for the group has been The Co-operative Bank of Kenya which owns 25.0% of the company through the Co-operative Insurance Society LTD.

Co-operative Societies: CIC continues to present itself as the preferred insurer for co-operative societies given their partnership in the past and the shareholding they command in the company. 70.0% of the premiums written by the life company in FY2013 were attributed to the co-operative societies.

	FY2011	FY2012	FY2013	FY2014F	FY2015F
Gross earned premiums (KES '000)	6,116,421	8,168,717	10,067,665	12,964,973	16,160,924
Return on average Equity (ROaE)	16.9%	28.4%	23.1%	28.2%	29.3%
Return on average Assets (ROaA)	6.3%	11.1%	9.0%	10.5%	10.5%
P/E x	33.58	14.13	13.93	9.31	7.76
P/B x	4.66	3.59	2.91	2.39	2.17
EPS	0.27	0.64	0.65	0.97	1.16
BVPS	1.93	2.51	3.09	3.76	4.15
Loss Ratio (Net claims/Net earned premiums)	58.9%	63.7%	65.8%	57.4%	57.4%

Source: Annual report & Faida Estimates

Background

We initiated coverage on CIC on 19th July 2012

We initiated coverage of CIC Group (CIC) on 19th July 2012 following its listing on the Nairobi Securities Exchange (NSE) on 18th July 2012. The company was listed through an introduction of 2.1 billion shares at a price of KES 3.50.

Since then the market capitalization for the firm has risen by 150.6% from KES 7.7 billion in December 2012 to KES 19.3 billion in April 2014.

CIC Growth Drivers

Alternative Distribution Channels

General insurance is primarily distributed through agents

CIC distributed insurance primarily through agents and brokers, especially for general insurance business. In FY2013, approximately 50.0% of general insurance business was attributed to agents, 35.0% to brokers and 15.0% to Bancassurance.

70.0% of life business is distributed by Co-operative societies

For the life business, approximately 70.0% of business was attributed to co-operative societies, 15.0% to M-Bima, 10.0% to brokers and 5.0% to marketing executives.

Going forward, the company plans to optimize on its use of agents as well as Bancassurance channels to accelerate premium growth.

- **Agents:** We believe the insurance agents & broker distribution channel is yet to be fully utilized by the firm. According to AKI, Britam had 38% (19) of the top 50 earning agents in the country in 2013 while CIC only had 4% (2).

8.5% of gross earned premiums paid out to agents

From FY2007 to FY2013, the company spent an average of 8.5% (FY2013: KES 843.6) of the gross earned premiums compared to Britam's 23.0% (FY2013: KES 1.9 billion) on commissions to agents for business generated.

Although CIC underwrites more insurance business than Britam (KES 10.1 billion compared to KES 8.8 billion in FY2013), partly due to its loyal customer base with the co-operative society, increase of agency and broker business will significantly boost the topline for the company.

CIC plans to increase the number of insurance agents to 250 agents

Going forward, CIC plans to increase the number of its insurance agents from the current 150 agents to 250 agents countrywide. The company has also formed partnerships with already existing insurance agents in Narok and Naivasha where it has branded their offices. In return, they underwrite majority of the business being generated by these agents. Sometimes the agents are given a premium target to meet every year.

Although this will likely result in a higher commissions payable as a % of premiums, due to the new business being generated by the agents, we expect the bottom line to grow in tandem due to the passthrough effects based on higher levels of written premiums.

- **Bancassurance: In FY2013,** the total premiums attributed to Bancassurance amounted to KES 1.7 billion. Out of this, KES 1 billion was genarated by Equity Bank while Co-operative Bank of Kenya generated close to KES 646 million.

Total premiums attributed to Bancassurance amounted to KES 1.7 billion

The customer base of the 2 banks stands at approximately 3.4 million customers and 8 million customers for Co-operative Bank of Kenya and Equity Bank respectively. This provides a good avenue for CIC to source for new business not only from the existing bank clients but also new clients from the banks' expansion of various distribution channels.

Sell micro insurance products through the agents of banks

The insurer also plans to sell its micro insurance products through the agents of banks such as The Co-operative Bank of Kenya's " Co-op Kwa Jirani". Through this model, we expect the firm to tap into the high population density areas at minimal cost. The only cost likely to be incurred will be the training of the bank's agents to increase their understanding and expertise in handling of insurance products pushed through them.

CIC seeks to fully optimise the partnership with Co-operative Bank to boost premium growth. It targets to write KES 2 billion insurance from Bancassurance in 2014, a 17.6% increase y-o-y.

- **Shopassurance:** It is the distribution of insurance to the shop customers through the shop outlets/branches. CIC has formed a partnership with Tusky's supermarkets, (the largest retail supermarket in Kenya in terms of branches), to use its 40 branch network to sell insurance to its customers.
In addition, Tuskys has made a bid to acquire 6 of the stores of Ukwala in Nairobi.

CIC has formed a partnership with Tusky's supermarkets

In the medium term, we expect this channel to become a source of data for insurance companies in understanding consumer behaviour patterns, their willingness and ability to take up insurance products as well as opening new contact points.

Micro-Insurance

The company has developed various micro insurance products targeted to the low income, "bottom of the pyramid" population, making it the leading micro insurer in Kenya.

Some of these micro insurance products include:-

Leading micro insurer in the country

- ✓ **Jijenge Savings:** This is a savings plan with a basic insurance cover where clients can save on a weekly or even daily basis using the mobile phone. It has minimum monthly instalments of KES 600 and a minimum life cover of KES 50,000.

- ✓ **Jikinge:** This is a micro insurance product for security guards under one group policy with individual benefits in funeral cost, weekly amount paid in case of hospitalization, medical expenses, artificial appliances such as crushes, etc.

Savings product

- ✓ **Nuru ya Jamii:** This is a product that gives an individual or families opportunities to insure their household goods for KES 480 per year.

Micro insurance for security guards

- ✓ **CIC Biashara salama:** This is a micro insurance product sold through Micro finance institutions (MFI's). The package will include comprehensive credit life cover for the insured borrower and cover on financed stocks and business related tools against risks such as fire & lighting, burglary etc

- ✓ **M-Bima:** This is a product designed to provide insurance protection to proprietors of M-Pesa shops. The insurance cover, covers loss of moneywhile in transit or in the insured premises, fidelity guarantee insurance and work insurance benefit act (WIBA) insurance all in one.

Sold through micro finance institutions

In FY2013, CIC wrote micro insurance premiums worth KES 600 million. It targets to write KES 1 billion in micro insurance business in FY2014, and grow it by KES 1 billion every year thereafter.

In order to develop, distribute and market these products, CIC has partnered with various stakeholders such as USAid, Safaricom and International Labour Organisation (ILO).

Target to write KES 1 billion worth of micro insurance

ILO assists the insurer with the development of the micro insurance product. USAid in partnership with ILO assist in meeting part of the marketing cost incurred by CIC on sensitizing the public on its products, which can be upto 50% of total marketing cost.

Co-operative Societies

CIC continues to present itself as the preferred insurer for co-operative societies given their partnership in the past and the shareholding they command in the company. In addition, 70.0% of the premiums written by the life company in FY2013 were attributed to the co-operative societies.

In 2013, the company formed strategic alliances and Memorandum of Understanding (MoU) with 80 co-operative societies. In FY2014, it plans to sign MoU's with 200 Sacco's.

CIC presents itself as a preferred insurer for Co-operatives

Given that CIC is 75.0% owned by Co-operative movement, the business proposition to the co-operatives is that they come in to support one of their own companies.

In addition to targeting the remaining co-operative societies, the insurer also plans to go directly to the members of the co-operative societies. Currently, over 10 million Kenyans are members of various co-operative societies such as;

Agribusiness Co-operatives, transport Co-operatives, housing co-operatives and Savings & Credit Co-operatives.

According to Cefri (The Centre for Financial Regulation and Inclusion), 81.0% of SACCO members do not have any kind of microinsurance product.

CIC plans to go directly to members to market insurance

In addition, the total life policies in the country stand at 600,000, including micro insurance, which is a paltry 6% of the total membership of the co-operative society, this shows the huge untapped potential customer base in the co-operative societies.

Regional expansion

CIC currently has 17 branches in the country and regional managers in each of the eight provinces in the country.

It has plans to increase its regional presence by going into 3 new markets during FY2014 i.e. Uganda, Malawi and South Sudan. The low penetration levels in these countries provides headroom for increased penetration.

CIC plans to tap into 3 new markets

CIC to own 49% of the insurance company in Uganda

CIC to own 60% of the insurance company in Malawi

CIC to own 69% of the insurance company in South Sudan

- ✓ **Uganda:** The set up of Uganda is going to be on a minority stake, where the company will own 49%, while the Co-operative Society of Uganda will own the remaining 51%. According to the Uganda Insurers Association, the country has a total of 22 insurance companies and an insurance penetration rate of 1.0%. Therefore, CIC's model of entering the Uganda with a partnership with their co-operative society is going to give the company an advantage in terms of a loyal customer base.
- ✓ **Malawi:** In Malawi, CIC plans to set up an insurance company and the shareholding structure will be a 60% (CIC), 40% (Malawi Union of Savings and Credit (MUSCCO) ownership.

  MUSCCO was established on 15th September 1980, with a mandate to promote sevices and support SACCO's in Malawi. Nearly 90% of people live in rural areas and are subsistence farmers. As a result, SACCO's appear to be the more convenient financial institution for the marjority because of their extensive rural outreach.

  As at 2011 MUSSCO had about 115,000 SACCO members and had loaned out MK 2.4 billion (USD 567 million). It had Savings of MK 2.7 billion (USD 632 million). MUSSCO has in the past insured the loans loaned out to clients in order to mitigate risk of loss in the event of death of the debtor.
- ✓ **South Sudan:** The subsidiary will be owned 69% by CIC and 31% by Co-operative Bank of South.

  We view the venture into the South Sudan market as a good opportunity for the firm to capitalize on the growth prospects of a new country. We see a lot of opportunities for cash rich businesses with longterm funds, such as life insurance companies, to enter the real estate market in the country. According to Knight Frank LLC, the rental yields in South Sudan are 12.0%.

Financial Analysis and Forecast

Income Statement (KES '000)	FY2011	FY2012	FY2013	FY2014F	FY2015F
Gross earned premium	6,116,421	8,168,717	10,067,665	12,964,973	16,160,924
Outward reinsurances	(772,125)	(880,537)	(911,983)	(1,223,702)	(1,540,527)
Net earned premiums	**5,344,296**	**7,288,180**	**9,155,682**	**11,741,271**	**14,620,396**
Investment income	537,943	790,517	756,848	1,062,976	1,186,862
Commissions earned	150,681	201,282	303,354	306,954	392,401
Total income	**6,020,050**	**8,901,993**	**10,887,100**	**13,311,663**	**16,422,126**
Net Claims and Policyholders benefits	(3,149,838)	(4,644,800)	(6,020,059)	(6,740,159)	(8,392,622)
Commissions payable	(557,373)	(641,300)	(843,552)	(904,914)	(1,136,160)
Operating and other expenses	(1,505,785)	(1,956,564)	(2,351,499)	(2,832,458)	(3,493,192)
Profit before tax	**787,238**	**1,649,591**	**1,671,095**	**2,809,275**	**3,372,312**
Profit after tax	**584,238**	**1,388,201**	**1,408,032**	**2,106,956**	**2,529,234**

Balance Sheet (KES '000)	FY2011	FY2012	FY2013	FY2014	FY2015
Shareholders' funds	**4,294,142**	**5,470,960**	**6,736,541**	**8,200,056**	**9,054,895**
Assets					
Investment properties	1,306,745	2,554,472	3,894,489	4,292,119	5,486,923
Reinsurance arising out of direct insurance arrangements	704,490	1,144,634	1,502,690	1,807,451	2,006,270
Deposits in financial institutions	2,763,034	3,727,723	3,343,407	5,902,480	6,551,753
Total Assets	**11,040,612**	**14,069,551**	**17,093,566**	**22,871,426**	**25,340,946**
Liabilities					
unearned premium reserve	2,158,409	3,092,113	4,070,695	4,548,497	5,048,831
Total gross insurance liabilities	2,595,700	3,197,799	3,103,300	5,499,541	6,104,491
Total Liabilities	**6,826,654**	**8,598,591**	**10,357,025**	**14,671,370**	**16,286,052**
Net Assets	**4,213,958**	**5,470,960**	**6,736,541**	**8,200,056**	**9,054,894**

Premium has grown by approximately KES 2 billion every year

Steady growth in premium income as they acquire market share: Since FY2011, we note that the company has grown its premium income by approximately KES 2 billion every year. KES 2.1 billion in FY2012 and KES 1.9 billion in FY2013. This growth was driven by the strong business proposition and firm customer base with the Co-operative societies coupled with the microinsurance product offering.

According to AKI the market share for CIC has grown from 5.7% in 2010 to 7.6% in 2011 and 9.2% in 2012.

VALUATION

Price to Book valuation used

We valued CIC using Price to Book multiple methodology, whereby we used the 2013 forecasted BVPS and a sample Sub-Saharan trailing P/B to arrive at our price target.

Our valuation methodology was informed by the fact that insurance companies as is the case with other financial institutions, mark to market a majority of their balance sheet.

P/B Multiple Valuation	
Current Market Price (07.05.14)	KES 8.85
Trailing sample P/B	3.07X
Trailing company P/B	2.91X
Forecasted BVPS: 2014	KES 3.76
Target Price	**11.56**
Upside Potential	**4.7%**

RECOMMENDATION

NEUTRAL recommendation

We maintain our **NEUTRAL** recommendation on CIC Group Ltd (CIC) with a target price to KES 11.56 which represents a potential upside of 4.7% from the current share price of KES 11.05 (As at 8th May 2014).

JUBILEE INSURANCE HOLDINGS LTD (JUBILEE)

Bloomberg Ticker	JBIC:KN
Fair Value (KES)	516.85
Price in KES - 07.05.2014	310.00
Issued Shares (Mn)	59.90
Market Cap (KES Mn)	18,567.45
Market Cap (USD Mn)	213.42
Year End	Dec 31st
Free Float (%)	54.5
KES/USD (87.00)	

Source: Bloomberg

Investment summary

We initiate coverage on Jubilee Holdings (Jubilee) with an **BUY** recommendation and a target price of KES 516.85 which represents a potential upside of 66.7% from the current share price of KES 310.00 (As at 8th May 2014).

Jubilee is an investment holding company incorporated in Kenya and with subsidiaries in Kenya, Uganda, Tanzania, Burundi and Mauritius.

The table below shows the top 10 shareholders of Jubilee as at 28th February 2014

BUY recommendation

Jubilee is an investment holding company incorporated in Kenya

Shareholder	Shares	Percentage
Aga Khan Fund for Economic & Development	22,751,025	38.0%
Ameerali K Abdulrasul Somji	4,466,887	7.5%
Ameerali K Abdulrasul & Hanif Mohamed Somji	1,108,734	1.9%
United Housing Estates Limited	1,086,734	1.8%
Adam's Brown And Co.Ltd	1,070,109	1.8%
Freight Forwarders Kenya Limited	1,018,101	1.7%
Gulshan Noorali Sayani	299,593	0.5%
Ariff Aziz Shamji & Farah Bahadur Alibhai Ukani	274,838	0.5%
Kenya General Agency (MSA) Limited	264,500	0.4%
Gulzar Shamshudeen Somji	206,737	0.4%

Our recommendation on Jubilee is informed by the following key growth drivers:

Regional business: Jubilee is currently the largest insurance company in the region with a presence in 5 countries. It plans to increase its presence to 12 markets across Africa over the next 3 years. Expansion will be via acquisition instead of greenfield investments.

Bancassurance: Jubilee is currently the second market leader in Bancassurance with KES 1 billion of total written premiums.

Aga Khan Fund for Economic Development (AKFED): We believe Jubilee benefits from this through insurance business from the other companies in the fund. The fund is active in 16 countries in the developing world i.e. Afghanistan, Bangladesh, Burkina Faso, The Democratic Republic of Congo, Ivory Coast, Kenya, Uganda, Tanzania, Kyrgyz Republic, Mali, Mozambique, Pakistan, Senegal, Syria, Tajikistan. In 2010, the fund recorded revenues of USD 2.3 billion.

	FY2011	FY2012	FY2013	FY2014F	FY2015F
Gross Earned premiums (KES '000)	12,058,816	15,399,514	18,087,946	21,271,958	25,070,919
Return on Average Equity (ROaE)	31.1%	29.6%	24.7%	26.5%	26.3%
Return on Average Assets (ROaA)	5.6%	5.3%	4.6%	5.1%	5.0%
P/E x	9.56	8.00	7.30	5.38	4.65
P/B x	2.72	2.10	1.57	1.30	1.15
EPS	31.90	38.14	41.79	56.73	65.63
BVPS	112.06	145.25	193.67	233.98	265.74

Source: Annual Report & Faida Estimates

History

Incorporated in the Repulblic of Kenya

Jubilee Insurance Holdings Ltd (Jubilee) is incorporated in the Republic of Kenya under the companies act and registered as a foreign company in the Republic of Uganda and the United Republic of Tanzania.

The history of Jubilee can be traced back to 1937. It began selling life insurance in 1938.

In 1984 Jubilee shares were offered to the public at KES 5.00 through an initial public offering (IPO). A decade later, in 1994, the company acquired the life business of Prudential Assurance Company.

For the subsidiary businesses, the company revived operations in Uganda in 1992 and in 1998 it revived the Tanzanian business.

In 2006, Jubilee shares were cross listed in the Uganda Stock Exchange and Tanzania Stock Exchange. Four years later, in 2010, Jubilee Burundi was formed.

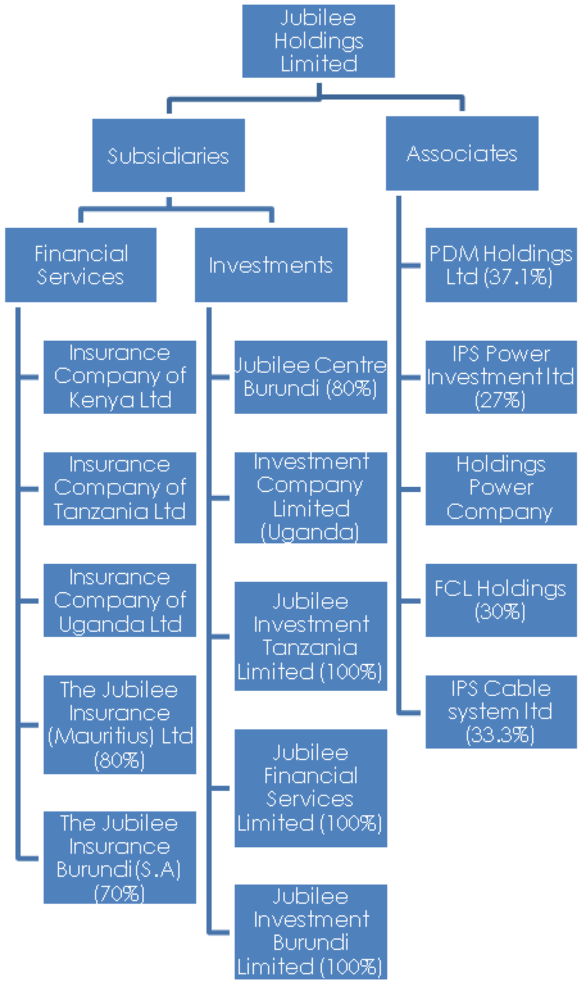
Company Structure

Subsidiaries in Kenya, Uganda, Tanzania, Mauritius and Burundi

Jubilee is an investment holding company with several subsidiaries: The Jubilee Insurance Company of Kenya Limited, The Jubilee Insurance Company of Uganda Limited, The Jubilee Insurance Company of Tanzania Limited, and The Jubilee Insurance Company Burundi all of which transact both general and long term insurance business) while Jubilee Insurance (Mauritius) Limited (which underwrites general insurance business).

The company also owns investment companies in Uganda, Burundi and Tanzania and a fund management company in Kenya (Jubilee Financial Services Limited).

The chart below shows the business structure of Jubilee holdings:



Source: Jubilee Insurance Company

Jubilee's Growth Drivers

Regional business

Presence in 5 countries

Jubilee is currently the largest insurance company in the region with a presence in 5 countries; i.e. Kenya, Uganda, Tanzania, Burundi and Mauritius. It plans to increase its presence to 12 markets across Africa over the next 3 years.

Expansion strategy through acquisition

The expansion strategy will be through acquisition of existing insurance companies instead of greenfield investments. Based on its asset base of KES 61.2 billion and net assets of KES 11.6 billion, Jubilee has the financial muscle to do buy outs in the region.

In order to tap into upcoming new towns and urban areas in the region, Jubilee targets to open 2 new branches in Tanzania in FY2014, while at the same time stabilizing the existing 14 branches in Kenya.

Bancassurance

Jubilee is currently the second market leader in insurance distribution through Bancassurance with KES 1 billion of total written premiums.

Bancassurance partners include Barclays Bank of Kenya, Standard Chartered Bank and Diamond Trust Bank

Its main Bancassurance partners include:- Barclays Bank of Kenya, Standard Chartered Bank and Diamond Trust Bank. The main insurance products sold via this channel include Motor, Credit life and Medical covers.

Going forward, the firm plans to leverage on these partnerships as well as forming new ones so as to boost premium growth using the bank clients. Given the amendment in bank regulation in 2013, allowing banks to act as agents of insurance companies, the environment is accommodative for insurance products to be distributed using the bank networks.

This is likely to see insurance companies with strong partnerships with banking institutions benefit with increased premium income from this distribution channel.

Aga Khan Fund for Economic Development (AKFED)

AKFED is the largest shareholder in Jubilee

The largest shareholder for Jubilee is AKFED with a 38.0% shareholdong (22.8 million shares).

AKFED is an international development agency which focuses on building enterprises in parts of the world that lack sufficient foreign direct investment.

Therefore, as one of the companies on the AKFED portfolio, we believe Jubilee is able to benefit from this through insurance business from the other companies in the fund's portfolio.

The fund Is active in 16 countries

The fund is active in 16 countries in the developing world i.e. Afghanistan, Bangladesh, Burkina Faso, The Democratic Republic of Congo, Ivory Coast, Kenya, Uganda, Tanzania, Kyrgyz Republic, Mali, Mozambique, Pakistan, Senegal, Syria, Tajikistan.In 2010, the fund recorded revenues of USD 2.3 billion.

Jubilee is in 3 of these countries (Kenya, Uganda and Tanzania). It plans to increase presence to 7 countries in the short term and 12 countries in the medium term. In terms of investments in these countries, the fund has investments in tourism, banking, media services, energy and airline.

Largest investor in TPS East Africa

In the tourism sector the fund is the largest investor in TPS East Africa (32.4% shareholding) which owns and runs a group of hotels in Kenya, Uganda and Tanzania. As at 2012, TPS East Africa had a total of 9 hotels and resorts in Kenya and 10 in Tanzania, generating revenues of KES 5.3 billion.

Largest investor in Diamond Trust Bank

In banking, the fund is the largest investor (17.3%) in Diamond Trust Bank (DTB) which commands an asset base of KES 166.5 billion. The bank is present in 4 countries in the region, i.e. Kenya, Uganda, Tanzania and Burundi. It is worthy to note that Jubilee is the third largest shareholder in DTB at 10.5% with 20.6 million shares.

Largest investor in Nation Media Group

In media, the fund is the largest investor in Nation Media Group (44.7% shareholding), the largest independently owned media house in East and Central Africa with operations in Kenya, Uganda and Tanzania. Nation Media Group had an asset base of KES 8.3 billion and revenues of KES 13.3 billion as at FY2013.

In the airline industry, through its aviation investment arm, Celestair, it has invested in Air Uganda which was formed in 2007 to fill a void left when the national carrier Uganda Air collapsed in 2000.

Therefore, as a strategic investor in Jubilee and these other investments, business synergies and mutually beneficial partnerships are likely to be enjoyed whereby Jubilee is able to write insurance to support the businesses being run and invested by AKFED.

Product innovation

Formed a partnership with CITADEL

During the current financial year, FY2014, Jubilee insurance formed a partnership with CITADEL Micro Insurance and Umande. The partnership aims at boosting the insurer's portfolio while at the same time increasing insurance penetration in Kenya.

Jubilee plans to use Umande to distribute insurance

Umande Trust is a rights- based agency with outlets in the informal settlements in Nairobi, Kisumu, Nakuru, Homa Bay and Embu. Jubilee plans to use Umande as a distribution outlet for its micro insurance products and Safaricom Kenya will provide the payment platform for the premiums through M-pesa.

Citadel Micro Insurance E.A Agency is a registered insurance intermediary whose ultimate objective is sourcing and availing affordable micro insurance products and services.

One of the products launched include Tumaini ya Jamii

One of the products launched includes, Tumaini ya Jamii which was done in partnership with Matatu Welfare Association (MWA), an organization with representatives of the service providers in the public transport sector in Kenya. This product covers family funeral expenses, permanent disability, domestic fire and material damage and the sum assured ranges from KES 10,000 to KES 100,000 with premiums ranging from KES 450 to KES 4,200 annually.

Technology

Jubilee invested in ICT to help grow its insurance business

In 2012, Jubilee invested in Information Communication and Technology (ICT), which plans to leverage on to grow the insurance business. This saw the company go live with a new life insurance system (Penta ISF) and commenced deployment of a new medical insurance system (Actisure) which was to be fully operational in FY2013.

The firm is in the process of establishing an online sales platform in order to push its micro insurance products.

In addition, Jubilee currently sells other products such as personal accident and travel insurance via the internet

Strong associate business

As shown in the chart on the company's structure, Jubilee has a strong associate business with investments in the following companies:

IPS Power investment Limited: This is an investment vehicle which has invested in the equity of Tsavo Power Company Limited (TPC). TPC owns a thermal power plant that generates and sells power to Kenya Power. In 2012, IPS power investments Ltd generated revenues of KES 4.9 billlion and a profit of KES 735.2 million.

Invested in Tsavo Power Company

Bujagali Holding Power Company: This is an investment vehicle company which has invested in the equity of Bujagali Energy Limited (BEL). BEL is an electricity generating company in Uganda which is responsible for the development of Bujagali Hydropower Project, 250 MW power generating facility. In 2012, Bujagali Holdings power Company returned a profit of KES 1.4 billion while Jubilee earned KES 325.8 million from its investment in the company.

Invested in the Bujagali Energy Limited

PDM Holdings LTD (37.1% shareholding): This is an investment vehicle company which conducts property investment, development and management. In FY2012, PDML Holdings Limited earned a profit of KES 577.9 million. Going forward the company plans on looking at development and selling as well as renting of housing projects.

Conducts property investments

Farmers Choice Holdings Limited (FCL): This is an investment vehicle which has invested in the equity of Farmers Choice Limited who sell fresh and processed meat products. In FY2012, FCL Holdings reported revenues of KES 6.4 billion with a profit of KES 634.4 million. Jubilee's share of profit in FCL during the same period stood at KES 190.3 million.

Invested in Farmers Choice Limited

Invested in Seacom

IPS Cable Systems Ltd: This is an investment vehicle company which has invested in Seacom, a 15,000 Km submarine fibre optic cable project which earned revenues of KES 1.1 billion and a profit of KES 881.5 million in FY2012.

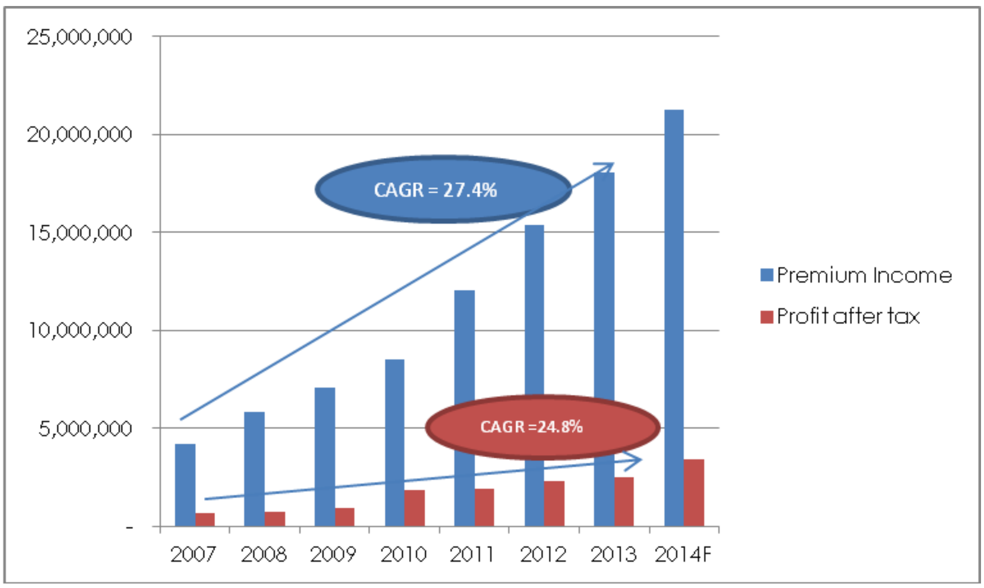
During the review period, we note that the company's share of investment in associate has grown at a CAGR of 90.9% from KES 47.2 million in FY2007 to KES 1.2 billion in FY2012, accounting for 52.3% of the total profits of Jubilee.

Financial analysis/Forecast

Income Statement (KES '000)	FY2011	FY2012	FY2013	FY2014F	FY2015F
Gross earned premium	12,058,816	15,399,514	18,087,946	21,271,958	25,070,919
Outward reinsurances	(4,716,820)	(6,026,532)	(7,314,561)	(8,273,404)	(9,750,952)
Net earned premiums	**7,341,996**	**9,372,982**	**10,773,385**	**12,998,554**	**15,319,967**
Investment income	2,692,387	3,156,981	3,697,032	4,329,467	5,070,090
Commissions earned	863,644	1,352,848	1,684,345	1,980,839	2,334,598
Total income	**10,568,863**	**14,326,358**	**18,042,639**	**21,634,914**	**25,306,574**
Net Claims and Policyholders benefits	6,114,019	8,555,537	10,985,554	12,721,390	14,815,233
Commissions payable	1,580,420	2,020,857	2,345,153	2,820,711	3,324,462
Operating and other expenses	1,804,331	2,203,878	2,483,628	3,110,464	3,665,962
Profit before tax	**2,143,891**	**2,693,303**	**3,151,188**	**4,059,619**	**4,696,686**
Profit after tax	**1,910,390**	**2,284,501**	**2,502,817**	**3,397,919**	**3,931,147**

Balance Sheet (KES '000)	FY2011	FY2012	FY2013	FY2014	FY2015
Shareholders' funds	**6,711,651**	**8,699,689**	**11,599,582**	**14,014,500**	**15,916,379**
Assets					
Investment properties	3,587,623	3,752,785	4,445,591	5,266,297	5,845,589
Investment in associates	5,078,237	6,128,566	6,465,583	7,176,797	7,966,245
Reinsurance arising out of direct insurance arrangements	1,647,111	1,918,436	3,563,752	4,191,078	4,939,562
Deposits in financial institutions	2,639,679	5,540,923	6,161,262	8,129,507	9,581,356
Total Assets	**38,039,832**	**47,417,562**	**61,159,185**	**72,393,326**	**83,998,692**
Liabilities					
unearned premium reserve	4,681,437	5,338,620	6,355,840	7,968,438	9,391,522
Total gross insurance liabilities	10,493,015	12,187,603	15,274,972	18,933,181	22,314,460
Total Liabilities	**31,328,181**	**38,717,873**	**49,559,603**	**58,378,826**	**68,082,313**
Net Assets	**6,711,651**	**8,699,689**	**11,599,582**	**14,014,500**	**15,916,378**

A graph showing the growth in revenue and profit for Jubilee



DISCLAIMER: The information contained herein is obtained from sources, which to the best of our knowledge are deemed reliable. As such, we are not responsible or liable for any factual errors arising thereof. Any opinions expressed herein are ours and are bound to change anytime at no notice.

Source: Annual report & Faida estimates

Consistent top and bottom line growth

We note that Jubilee has shown a consistent growth in both the top and bottom line as shown by the graph above. Premium income grew at a CAGR of 27.4% from KES 4.2 billion in FY2007 to KES 18.1 billion in FY2013.

The profit after tax grew at a CAGR of 24.8% from KES 663.1 million in FY2007 to KES 2.5 billion in FY2013. We attribute this growth to an increase in the firm's regional business coupled with a solid customer base in the AKFED related companies.

Bottom line growth has been sustained by leveraging on its scale and size which enables it to pool large amount of risk coupled with a strong associate business in IPS Cables, FCL holdings and Bujagali dam.

VALUATION

Price to Book valuation was used

We valued Jubilee using Price to Book multiple methodology, whereby we used the 2013 forecasted BVPS and a sample Sub-Saharan trailing P/B to arrive at our price target.

Our valuation methodology was informed by the fact that insurance companies as is the case with other financial institutions, mark to market a majority of their balance sheet.

P/B Multiple Valuation	
Current Market Price (07.05.14)	KES 310.00
Trailing sample P/B	2.21X
Trailing company P/B	1.57X
Forecasted BVPS: 2014	KES 233.98
Target Price	**516.85**
Upside Potential	**66.7%**

RECOMMENDATION

BUY recommendation

We initiate coverage on Jubilee Holdings (Jubilee) with an **BUY** recommendation and a target price of KES 516.85 which represents a potential upside of 66.7% from the current share price of KES 310.00 (As at 8th May 2014).

KENYA REINSURANCE CORPORATION LIMITED (KENYA RE)

Bloomberg Ticker	KNRE:KN
Fair Value (KES)	26.10
Price in KES - 09.05.2014	19.75
Issued Shares (Mn)	699.95
Market Cap (KES Bn)	13823.99
Market Cap (USD Mn)	158.90
Year End	Dec 31st
Free Float (%)	37.83
KES/USD (87.00)	

Investment Summary

We place a BUY recommendation on Kenya Re

We initiate coverage on Kenya Re with a **BUY recommendation** with a price target of KES 26.10, which represents a 31.7% upside potential based on the prevailing market price of KES 19.75 (07.05.2014).

Kenya Re trading at a relatively low P/B multiple

Despite the outlined investment risks, the company still has massive potential for growth and is trading at a relatively low P/B. The company is trading at a trailing P/B multiple of 0.77 and a forward P/B multiple of 0.68.

Government is majority shareholder with a 60.0% stake

Major Shareholders	Number of shares	% Shareholding
Permanent Secretary to the Treasury of Kenya	420,000,000	60.00
Cooperative Bank Custody A/C 4003A	15,204,072	2.17
Standard Chartered Nominees A/C 9537	11,219,100	1.60
National Social Security Fund	10,737,910	1.53
Gidjoy Investments Limited	10,271,382	1.47
CFC Stanbic Nominees A/C NR1030624	8,991,100	1.28
Standard Chartered Nominees A/C 9230	8,004,717	1.14
CFC Stanbic Nominees A/C NR1030685	7,575,700	1.08
Investment & Mortgages Nominees AC 028917	7,080,500	1.01
Standard Chartered Nominees A/C 9389	6,471,800	0.92
	505,556,281	72.20

Key Investment Considerations Include:

Exposed to relatively nascent insurance industries

Riding on Nascent Insurance Industry: With business in more than 159 companies across 45 countries in Africa, the company is exposed to relatively nascent insurance industries. We expect the positive correlation between Kenya Re's gross written premium and the industrys' premiums to continue given the former's dependance on industry performance.

Portion of international business rose to 48.0% in FY2012

Leveraging on International Broker Networks and Representative Offices: The portion of international business to gross written premium rose consistently from 38.0% in FY2008 to 48.0% in FY2012. We expect the upward trend to continue going forward ultimately leading to international business being the top contributor to gross written premiums in the short-term.

Compulsory cessations se to end in FY2015

Mandatory Cessation: The compulsory cessations are set to end in FY2015 and is subject to Government renewal. Going forward, we believe that the compulsory cessations will be extended given the government's majority shareholding and their current fiscal position.

Proactive Approach In Building Industry Capacity: By building local capacity in the industry, Kenya Re is ensuring that insurance for the oil and gas sector can be handled by local firms instead of international insurance companies.

Increasing Competition Not a Big Threat: Historically, the company has managed to fair well in the competitive environment and continues to claim more business in the international front. Going forward, we expect strong growth from the international business to cushion it from the threat of increased competition locally.

	FY2010	FY2011	FY2012	FY2013	FY2014F	FY2014F
Net Earned Premium (KES '000)	4,273,913	5,734,678	7,054,315	8,581,830	10,035,426	11,671,921
EPS (KES)	2.57	2.74	4.00	4.29	4.67	5.45
BVPS (KES)	15.11	16.47	20.88	25.61	28.89	32.09
P/E x	4.30	2.67	2.67	3.65	4.23	3.62
P/B x	0.73	0.44	0.51	0.61	0.68	0.62
ROaE	15.7%	17.3%	21.4%	18.4%	17.1%	17.9%
ROaA	9.6%	10.5%	13.1%	11.5%	10.9%	11.3%
Loss Ratio	47.9%	51.3%	57.6%	55.0%	55.1%	52.6%

Brief History

Kenya Re established in December 1970

Kenya Reinsurance Corporation (Kenya Re) was established through an Act of Parliament in December 1970 and commenced business in January 1971.

Kenya Re's core business is providing reinsurance services for most classes of business. The company has business with more than 159 companies spread out in over 45 countries in Africa, Middle East and Asia. It has a representative office in Ivory Coast.

GROWTH DRIVERS

Riding on Nascent Insurance Industry: With business in more than 159 companies across 45 countries in Africa and the Middle East, the company is exposed to relatively nascent insurance industries.

Gross Written Premium recorded a 23.0% CAGR from FY2008 to FY2013

Kenya Re recorded a Compounded Annual Growth Rate (CAGR) of 23.0% in gross written premiums from KES 3.4 billion in FY2008 to KES 9.6 billion in FY2013 on the back of increased written premiums in the target markets it operates in. Although the company attributes this to aggressive marketing in selected markets, we believe that the growth is also aided by the organic industry-wide growth displayed in the target markets.

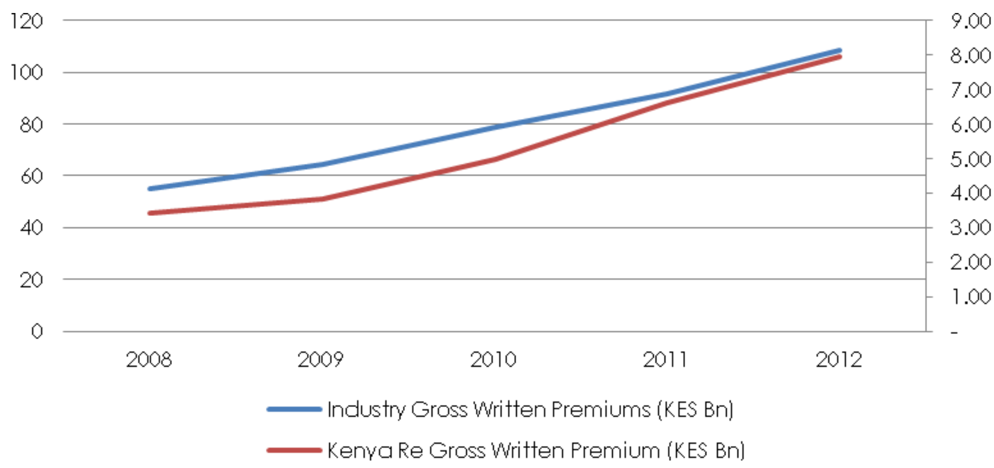
Different markets with their respective insurance penetration rates are displayed below. Comparative analysis with developed and developing markets demonstrates the headroom for growth in the industry.

Total Penetration (%)	2010	2011	2012
South Africa	14.8	11.6	14.2
Namibia	7.3	8.0	8.0
Mauritius	5.9	5.2	5.9
Kenya	2.8	3.0	3.2
Angola	1.0	1.1	1.0
Egypt	0.7	1.0	0.7
Nigeria	0.5	0.9	0.7
Africa			
Africa	3.9	3.6	3.6
Emerging Markets			
India	5.1	4.1	4.0
Brazil	3.1	3.2	3.7
China	3.8	3.0	3.0
Mexico	1.9	1.9	2.0
Russia	2.3	2.4	1.3
Advanced Markets			
Japan	10.1	11.0	11.4
UK	12.4	11.8	11.3
USA	8.0	8.1	8.2
Germany	7.2	6.8	6.7

Source: AKI Annual Reports, Swiss Re, FSC Mauritius, KPMG

Kenya accounted for about 52.0% of gross premium in FY2012

Kernya accounted for about 52.0% of Kenya Re's gross premiums in FY2012. The chart below depicts the strong positive correlation (0.99) between Kenya Re's gross written premium and Kenya's total gross written premium from FY2008 to FY2012.



Source: AKI, Company Reports, FIB Estimates

Significant potential in both local and international insurance markets

We expect the positive correlation between Kenya Re's gross written premium and the industrys' premiums to continue given the former's dependance on industry performance. Given the potential in both the local and international insurance markets, Kenya Re is set to benefit from increased reinsurance premium going forward.

Regional branch office in Ivory Coast launched in FY2012

Leveraging on International Broker Networks and Representative Offices: To generate new business, the company has relied on the use of brokers and representative offices. This translated to KES 3.8 billion (48.0% of gross written premiums) in FY2012. A regional branch office in Abidjan, Ivory Coast was officially launched in FY2012 and is in the process of being converted into a compliant and adequately-capitalized subsidiary.

Plans are also underway to open representative offices in Southern Africa with Zimbabwe, Zambia, Mozambique and Botswana as target markets.

According to Global Credit Rating (GCR) in their 3Q2013 affirmation rating of the company, the portion of international business to gross written premium rose consistently from 38.0% in FY2008 to 48.0% in FY2012. The upward trend shows the effectiveness of the use of brokers and the representative office in acquiring international business. We expect the upward trend to continue ultimately leading to international business being the top contributor to gross written premiums in the short-term.

Compulsory cessations set to end in FY2015

Mandatory Cessation: Kenya Re is currently a beneficiary of a mandatory cessation agreement that obliges local insurance companies to reinsure with it at a rate of 18.0% of all reinsurance premiums paid. The compulsory cessations are set to end in FY2015 and is subject to Government renewal.

Kenya Re's Share of Total Reinsurance Premiums	FY2012
Industry Non-Life Reinsurance Premiums ceded (KES Bn)	18.1
Industry Life Reinsurance Premiums ceded (KES Bn)	2.4
Total Industry Reinsurance Premium (KES Bn)	**20.50**
Kenya Re share of total reinsurance premiums (KES Bn)	**4.1**
Kenya Re share of total reinsurance premiums (%)	**20.2%**

Source: AKI, FIB Estimates

Kenya Re's share of total reinsurance premiums indicates that the company managed to get an additional 2.0% above the mandatory 18.0% cessation rate.

Assuming a 10.0% growth rate in total reinsurance premium and a 20.2% share of the total reinsurance premium for Kenya Re, we estimate a growth of KES 400 million in company premiums in FY2013.

	2011	2012	2013E
Total Reinsurance Premium (KES Bn)	15.2	20.5	24.6
% Growth		34.9%	10.0%
Kenya Re share of total reinsurance premiums (%)		**20.2%**	**20.2%**
Kenya Re share of total reinsurance premiums (KES Bn)		**4.1**	**4.5**

Source: AKI, FIB Estimates

In this regard, the mandatory cessation rate acts as a top line driver for the company.

Strong growth in international business would cushion Kenya Re's business

What happens if the mandatory cessations are not extended? Should the cessations cease to exist, we are of the opinion that strong growth in international business would cushion Kenya Re's business. International busines recorded a (CAGR) of 30.8% from KES 1.30 billion (FY2008) to KES 3.8 billion (FY2012).

Below is a scenario analysis showing the probable gross written premium should the mandatory cessation end in FY2015. Assumptions include a 30.8% annual growth in international business, 20.0% annual growth in Kenya total reinsurance premium and 2.2% share of total reinsurance premium post-mandatory cessation.

	2012	2013E	2014F	2015F	2016F
International Business Contribution (%)	**48.0%**	**50.1%**	**52.2%**	**91.6%**	**92.3%**
International Business Contribution (KES)	3.81	4.99	6.52	8.53	11.16
CAGR (FY2008 - FY2012)	**30.8%**	**30.8%**	**30.8%**	**30.8%**	**30.8%**
Kenya Total Reinsurance Premium (KES Bn)	**20.5**	**24.6**	**29.5**	**35.4**	**42.5**
y-o-y % Growth	34.9%	20.0%	20.0%	20.0%	20.0%
Kenya Re share of total reinsurance premiums (%)	20.2%	20.2%	20.2%	2.2%	2.2%
Kenya Re share of total reinsurance premiums (KES Bn)	4.1	4.9	6.0	0.8	0.9
Kenya Re total Premium	**7.95**	**9.96**	**12.49**	**9.31**	**12.10**

Source: AKI, FIB Estimates

We believe that the compulsory cessations will be extended

Going forward, we believe that the compulsory cessations will be extended given the government's majority shareholding and their current fiscal position. This could also act as a protective shield from the stiff competition in the reinsurance industry.

Notably, most local insurance companies in our research universe confirmed their intentions to continue ceding premiums to Kenya Re should the mandatory cessation end.

Kenya Re spearheading relevant training so as to build local capacity

Proactive Approach In Building Industry Capacity: Following the recent oil discoveries in Uganda and Kenya and the discovery of gas along the Mozambique and Tanzanian coast, Kenya Re is spearheading relevant training so as to build local capacity and competence. The professional and consultancy fees increased from KES 19 million in FY2010 to KES 63 million in FY2012.

Kenya Re is currently working with an Australian company, Total Risk Solutions, to create local capacity and expertise in handling the needs of the sector in anticipation of commercialization of the deposits. The company is also investing in training insurance professionals in East Africa on Marine and Hull insurance.

The opportunity in oil and gas sector is huge with various forms of insurance needed for the exploration and production phases. Such insurance covers that may be needed include Public Liability insurance, Employers' Liability, Motor, Property, Construction All Risk insurance and General Third Party Liability.

By building local capacity in the industry, Kenya Re is ensuring that insurance for the oil and gas sector can be handled by local firms instead of international insurance companies. In addition, it is expected to foster good relations with insurance companies, resulting in increased written premiums in the oil and gas sector should commercialization take place.

Officially launched Sharia Supervisory Board

Islamic Reinsurance: Kenya Re offically launched a Sharia Supervisory Board in FY2013 to guide and monitor the Retakaful business and ensure compliance with Sharia rules and principles.

Although local uptake of Retakaful has been slow, it has been operational in South Sudan for over ten years. Premium attributable to the Retakaful business was KES 96 million in FY2012.

We expect a slow take-off of Retakaful from South Sudan given their current situation. However, potential lies in predominantly Muslim countries in North Africa and Middle East.

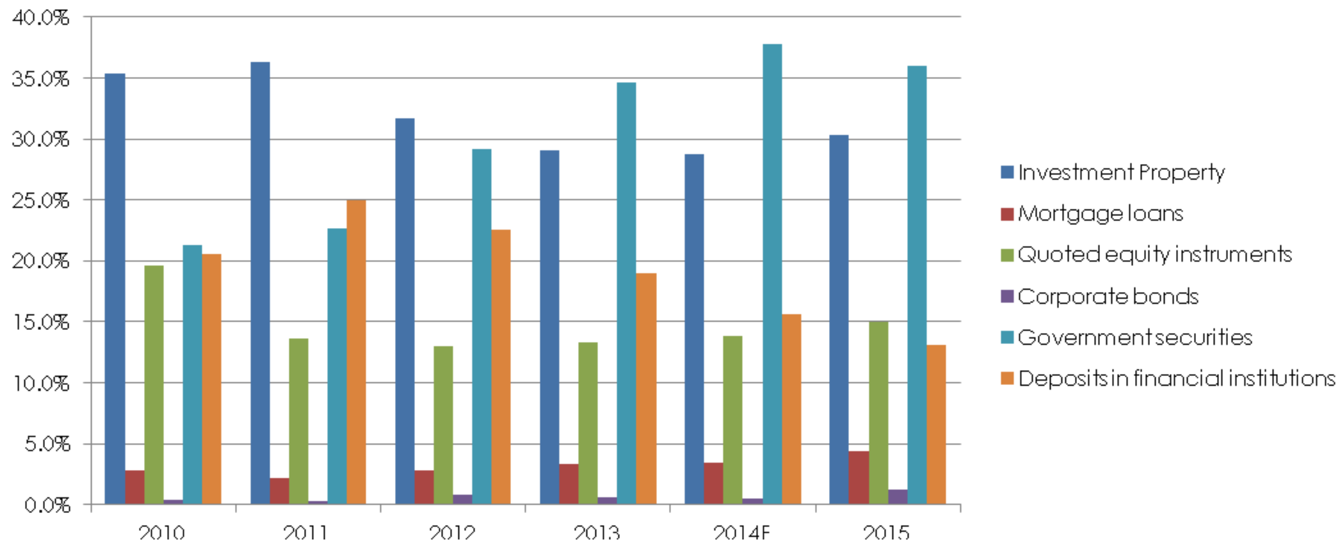
Investment Mix Geared Towards Increased Rental income going forward: Over the past five years (FY2009 – FY2013) Kenya Re has managed to grow its investment income at a CAGR of 19.4% to KES 2.3 billion. Notably, the 86.7% spike in investment income in FY2012 was largely attributable to a non-recurring profit on sale of property. Specific growth rates that stand out in investment income are interest on government securities, interest on corporate bonds, fair value gains on quoted equity instruments and interest on deposits with financial institutions.

	2009	2010	2011	2012
Interest on government securities	272,131	276,236	339,947	520,185
% Change		1.5%	23.1%	53.0%
Interest on corporate bonds	1,040	5,752	5,838	11,567
% Change		453.1%	1.5%	98.1%
Fair value gains on quoted equities	-	430,824	237,162	314,209
% Change			-45.0%	32.5%
Interests on deposits with financial institutions	66,474	114,560	194,244	630,382
% Change		72.3%	69.6%	224.5%
Rental Income from Investment properties	437,716	479,393	499,796	574,594
% Change		9.5%	4.3%	15.0%

Key drivers of investment income to originate from quoted equities and investment properties

Going forward, we expect key drivers of investment income growth to originate from increased investment on quoted equity instruments and rental income from investment properties.

The chart below shows Kenya Re's investment mix for the past four years.



Kenya Re is in the process of building its 5th commercial building

Kenya Re is in the process of building its 5th commercial building in Nairobi's Upper Hill area targeted at local corporates and multi-nationals. Data from the 2013 Hass Consult Annual Report shows that Upper Hill recorded the highest increase (23.0%) in suburb rental prices during the year.

KEY INVESTMENT RISKS

The reinsurance industry in Kenya has attracted major players

Increasing Competition: The Reinsurance industry in Kenya has attracted major players such as Africa Re, Zep Re and Munich Re. Furthermore, Kenya Re is exposed to other international markets within Africa where it doesn't enjoy a mandatory cessation cushion.

The company may find it hard to win business from larger reinsurance companies that have more capital and capacity to handle more risk. Africa Re, for example, had USD 609 million in total shareholders' funds (FY2012) compared to Kenya Re's USD 169 million at the time.

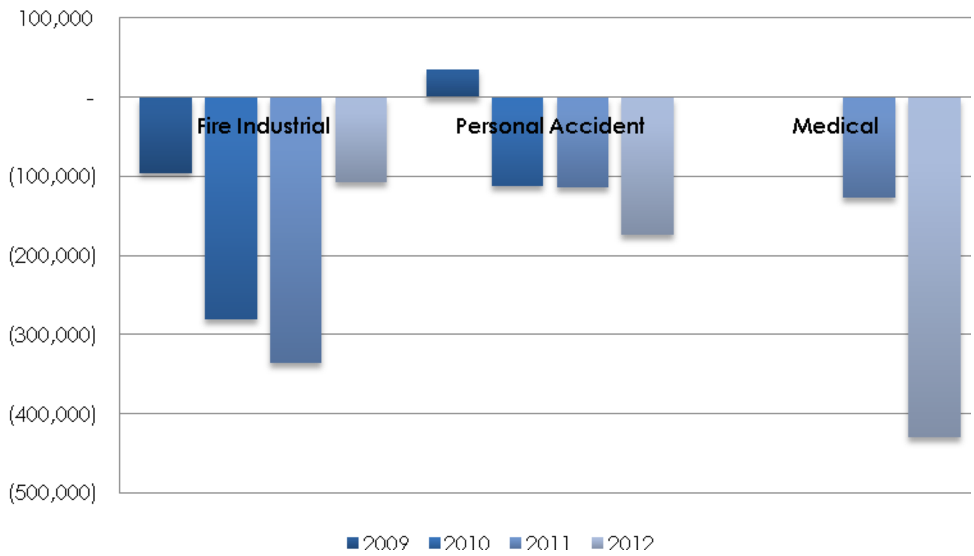
The company continues to claim more business in the international front

Historically, the company has managed to fair well in the competitive environment and continues to claim more business in the international front. Going forward, we expect strong growth from the international business driven by the company's marketing strategies, innovative products such as Retakaful and good client relations fostered by the trainings they sponsor.

Combined ratios of over 100.0% in fire (industrial), personal accident and medical classes

Underwriting loss on Fire, Personal Accident and Medical: For the past three years, Kenya Re has been struggling with perennial combined ratios of over 100.0% in the fire (industrial), personal accident and medical classes.

Although we anticipate moderate growth in net earned premiums for the highlighted classes, an offset is expected principally due to the high claims and management expenses associated with the classes. With strategy on how to tame expense and claims growth rates remaining unclear, we expect underwriting losses in the mid-term.



Source: Company Reports

DISCLAIMER: The information contained herein is obtained from sources, which to the best of our knowledge are deemed reliable. As such, we are not responsible or liable for any factual errors arising thereof. Any opinions expressed herein are ours and are bound to change anytime at no notice.

FINANCIAL PERFORMANCE

Income Statement

Income Statement (KES '000)	FY2010	FY2011	FY2012	FY2013	FY2014F	FY2014F
Gross premiums written	4,980,900	6,613,884	7,944,183	9,645,151	11,431,553	13,295,717
Less: Change in unearned premiums	(426,994)	(513,276)	(505,533)	(620,442)	(727,454)	(846,081)
Less: Retrocession premiums	(279,993)	(365,930)	(384,335)	(442,879)	(752,339)	(875,024)
Net earned Premiums	**4,273,913**	**5,734,678**	**7,054,315**	8,581,830	10,035,426	11,671,921
Investment Income	1,683,210	1,419,902	2,651,422	2,277,749	2,557,928	2,777,395
Commissions receivable	29,229	27,202	70,194	26,966	29,270	31,799
Revaluation of investment properties	378,064	684,498	523,008	441,588	465,880	516,974
Other income	64,945	72,093	94,254	76,472	76,472	76,472
NET INCOME	**6,429,361**	**7,938,373**	**10,393,193**	**11,404,605**	**13,164,976**	**15,074,561**
Gross claims incurred	(2,198,438)	(3,263,744)	(4,221,576)	(5,246,003)	(6,219,962)	(6,830,055)
Amounts recoverable from retrocessionaires	151,460	323,889	159,999	522,833	688,783	687,873
NET CLAIMS INCURRED	**(2,046,978)**	**(2,939,855)**	**(4,061,577)**	**(4,723,170)**	**(5,531,179)**	**(6,142,182)**
Commissions payable	(1,276,881)	(1,729,908)	(2,041,855)	(2,493,960)	(2,978,137)	(3,465,417)
Operating and other expenses	(698,273)	(773,051)	(1,084,141)	(1,014,768)	(1,178,639)	(1,296,134)
Provision for doubtful debts	(476,484)	(646,559)	(466,919)	(160,904)	(214,575)	(249,566)
TOTAL EXPENSES	**(2,801,638)**	**(3,149,518)**	**(3,592,915)**	**(3,669,632)**	**(4,371,352)**	**(5,011,118)**
Share of profit of associate	79,271	187,777	205,934	257,000	295,386	320,049
Profit before taxation (PBT)	**1,660,016**	**2,036,777**	**2,944,635**	**3,268,803**	**3,557,831**	**4,241,310**
Profit for the year	**1,541,391**	**1,914,584**	**2,801,892**	**3,000,431**	**3,266,089**	**3,817,179**

Gross written premium grew at a CAGR of 23.0%

Market Expansion drives gross written premium: Gross written premium has sustained strong growth with a CAGR of 23.0% from KES 3.4 billion in FY2008 to KES 9.6 billion in FY2013. Various insurance classes such as ordinary life, theft and fire posted strong growth rates over the past four (FY2009 – FY2012) years at an average of 42.7%, 23.6% and 21.7% respectively.

Non-recurring profit on sale of property in FY2012

Lower interest rates dent investment income growth in FY2013: Favourable interest rates and improved returns from the equities market led to strong returns from treasury bills, bonds, bank deposits and the securities market leading to an average growth rate of 30.3% from FY2009 to FY2012. Investment income increased significantly by 86.7% to KES 2.7 billion in FY2012 from KES 1.4 billion in FY2011. However, there was a non-recurring profit on sale of property that occurred in FY2012 of KES 310 million. FY2013 recorded a 14.1% y-o-y decrease in investment income to KES 2.3 billion attributable to a lower interest rate environment.

Increased payouts: Gross claims incurred increased by 24.3% to KES 5.2 billion in FY2013 mainly attributable to increased payouts from both the short term and long term businesses.

However, the loss ratio (Net claims/Net earned premiums) dropped from 57.6% in FY2012 to 55.0% in FY2013. Net claims incurred increased by 16.3% to KES 4.7 billion in FY2013 from KES 4.1 billion in FY2012.

Balance Sheet

Balance Sheet (KES '000)	FY2010	FY2011	FY2012	FY2013	FY2014F	FY2015F
ASSETS						
Investment properties	4,616,500	5,365,000	5,935,000	6,459,000	7,167,378	7,953,446
Investment in associate	952,730	1,133,445	1,340,048	1,652,940	2,017,566	2,461,917
Receivables arising out of reinsurance arrangements	1,228,234	1,248,975	1,518,502	2,002,956	2,384,168	2,772,958
Corporate bonds	51,209	48,393	153,970	141,846	130,677	120,387
Quoted equity instruments	2,567,509	2,008,823	2,436,749	2,959,490	3,465,441	3,859,808
Government securities	2,776,617	3,357,582	5,459,118	7,693,954	9,422,192	11,118,186
Deposits with financial institutions	2,693,330	3,687,082	4,217,389	4,217,002	3,909,520	3,489,246
TOTAL ASSETS	**17,240,929**	**19,096,441**	**23,787,957**	**28,222,587**	**31,803,493**	**35,611,920**
LIABILITIES						
Long term reinsurance contracts	2,150,640	2,285,709	2,073,032	2,094,357	2,133,794	2,307,964
Short term reinsurance contracts	2,212,251	2,373,622	3,049,991	3,702,715	4,296,822	4,994,969
Unearned premiums	1,643,433	2,156,709	2,662,244	3,282,685	3,767,775	4,382,193
Payables arising out of reinsurance arrangements	288,097	394,555	709,445	701,912	769,024	894,430
TOTAL LIABILITIES	**6,667,427**	**7,569,956**	**9,174,802**	**10,300,205**	**11,581,455**	**13,153,994**
SHAREHOLDERS' FUNDS	**10,573,502**	**11,526,485**	**14,613,155**	**17,922,382**	**20,222,038**	**22,457,926**

Shareholders' funds increased by 22.6% to KES 18.0 billion (FY2013) from KES 14.6 billion (FY2012). The company issued an additional 100 million shares in FY2012. Fair value reserve increased by 36.1% y-o-y to KES 1.8 billion while retained earnings increased by 23.3% y-o-y to KES 11.0 billion in FY2013.

UNDERWRITING BUSINESS

Underwriting Profit	2011	2012	2013	2014F	2015F
Net earned premium	5,734,678	7,054,315	8,581,830	10,035,426	11,671,921
Net Claims & Benefits Payable	(2,939,855)	(4,061,577)	(4,723,170)	(5,531,179)	(6,142,182)
Commissions earned	27,202	70,194	26,966	29,270	31,799
Commissions Payable	(1,729,908)	(2,041,855)	(2,493,960)	(2,978,137)	(3,465,417)
Operating & other expenses	(773,051)	(1,084,441)	(1,014,768)	(1,178,639)	(1,296,134)
Underwriting profit/ (Loss)	**319,066**	**(63,364)**	**376,898**	**376,741**	**799,986**
Underwriting profit/ (Loss) Margin	5.6%	-0.9%	**4.4%**	**3.8%**	**6.9%**

KEY RATIOS

Underwriting Ratios	2011	2012	2013	2014F	2015F
Loss Ratio	51.3%	57.6%	55.0%	55.1%	52.6%
Managements' Expense Ratio	13.5%	15.4%	11.8%	11.7%	11.1%
Combined Ratio	**64.7%**	**72.9%**	**66.9%**	**66.9%**	**63.7%**

Profitability Ratios	2011	2012	2013	2014F	2015F
Net Profit Margin	28.9%	35.3%	31.1%	28.6%	28.7%
ROE	16.6%	19.2%	16.7%	16.2%	17.0%
ROA	10.0%	11.8%	10.6%	10.3%	10.7%
Investment Yield	0.2%	0.4%	0.1%	0.1%	0.1%

We expect the combined ratio to be maintained in FY2014.

FY2013 saw Kenya Re record an underwriting profit principally due to higher net earned premiums and lower operating expenses. We expect the combined ratio to be maintained in FY2014.

VALUATION

We used the P/B Multiple valuation approach to obtain our target price. The target price was obtained using our forecasted BVPS and a sample P/B multiple derived from comparable reinsurance companies globally. The sample comparables were chosen based on business likeliness and investment return measures.

Our valuation methodology was informed by the fact that insurance companies as is the case with other financial institutions, mark to market a majority of their balance sheet.

Sample Reinsurance Comparables	**P/B x**
Continental Re	0.75
Saudi Re	1.61
Kuwait Re	0.51
Everest Re	1.04
MNRB Holdings	0.70
Singapore Re	0.81
Average	**0.90**

P/B Multiple Valuation	
Current Market Price (7.05.14)	19.75
Trailing BVPS:2013	25.61
Trailing P/B	0.77
Forecasted BVPS: 2014	28.89
Average P/B	0.90
Target Price	**26.00**
Upside Potential	**31.7%**

RECOMMENDATION

We initiate coverage on Kenya Re with a BUY recommendation

We initiate coverage on Kenya Re with a **BUY recommendation** with a price target of KES 26.10, which represents a 31.7% upside potential based on the prevailing market price of KES 19.75 (07.05.2014).

Despite the outlined investment risks, the company still has massive potential for growth and is trading at a relatively low P/B. The company is trading at a trailing P/B multiple of 0.77 and a forward P/B multiple of 0.68.

LIBERTY KENYA HOLDINGS LIMITED (LIBERTY)

Bloomberg Ticker	CFCI:KN
Fair Value (KES)	24.33
Price in KES - 09.05.2014	22.50
Issued Shares (Mn)	517.27
Market Cap (KES Bn)	11638.58
Market Cap (USD Mn)	133.78
Year End	Dec 31st
Free Float (%)	12.95
KES/USD (87.00)	

Investment Summary

We initiate coverage on Liberty Kenya with a **NEUTRAL recommendation**. Our target price of KES 24.33 provides an 8.1% upside potential from the current share price of KES 22.50. (7.5.2014). We are of the opinion that Liberty Kenya Holdings lags behind the competition in regards to flexibility, tact and aggressiveness to succeed in the local dynamic insurance industry.

We initiate coverage on Liberty Kenya with a **NEUTRAL** recommendation

Major Shareholders	Shares Held	% Shareholding
Liberty Holdings South Africa	292,762,096	56.82
African Liaison and Consultant Services Limited	155,747,166	30.23
Sovereign Trust Limited	14,441,154	2.8
Standard Chartered Nominees Non-Resd A/C 9866	9,932,200	1.93
Alcher & Wilcock Limited	6,125,000	1.19
Kingsway Nominees Limited	5,198,498	1.01
Permanent Secretary to the Treasury of Kenya	4,342,548	0.84
Kenyalogy.com Limited	1,186,636	0.23
CFC Stanbic Nominees A/C NR1030653	1,171,400	0.23
CFC Stanbic Nominees A/C NR1030819	890,600	0.17

Liberty Holdings South Africa is the majority shareholder

Key investment considerations include:

Diversification from Traditional Distribution Channels: Both Heritage and CFC Life have partnered with various banks such as CFC Stanbic and Chase Bank to leverage on their branch networks and agents to access potential customers. This saves the company on brick and mortar costs of setting up physical branches.

Use of technology in distributing products: The planned partnerships that are expected to come in place in the short term between Liberty and telecommunication companies could be the impetus for increased premiums written.

Heritage setting up new ERP

Efficiency via Investment in IT: Heritage Insurance is currently in the process of setting up a new ERP (Enterprise Resource Program) that is expected to rationalize operating expenses and increase efficiency.

Difficulties trying to catch up with competition

Does Liberty Have a Competitive advantage? In our view, Liberty Kenya Holdings will have difficulties trying to catch up with competition in terms of product innovation.

Conservative Investment Strategy

Conservative investment strategy: Liberty has maintained a conservative investment strategy with bulk of investments held in money markets and bonds (4 year average of 56.4% of total investment mix) and minimal exposure to quoted equities and investment property.

	FY2011	FY2012	FY2013	FY2014F	FY2015F
Net Earned Premium	4,237,933	3,982,386	4,067,127	4,101,724	4,218,407
EPS (KES)	1.84	1.72	2.15	2.70	3.00
BVPS (KES)	8.10	10.52	10.61	11.01	11.58
P/E x	3.55	2.06	7.55	8.33	7.49
P/B x	0.81	0.34	1.53	2.04	1.94
ROaE	21.5%	18.5%	20.3%	25.0%	26.6%
ROaA	4.0%	3.4%	3.8%	4.3%	4.4%
Loss Ratio	58.6%	78.1%	75.7%	72.2%	77.2%

Source: Company Reports, FIB Estimates

Brief History

Liberty Kenya is the holding company of CFC Life and Heritage Insurance

Liberty Kenya Holdings is the holding company of CFC Life Assurance Company (CFC Life) and Heritage Insurance Company. Formerly known as CFC Insurance Holdings Limited, the holding company changed its name in 2012 as an initial step to align its operations to its Parent Company, Liberty Group, based in South Africa.

CFC Insurance Holdings was originally under CFC Stanbic Holdings until a split between the banking and insurance business units occurred in FY2010.

Heritage Insurance manages non-life insurance

Heritage Insurance manages non-life (general) insurance through Heritage Insurance Kenya and its subsidiary Heritage Insurance Company Tanzania (60.0% ownership interest). Heritage Insurance also has a 43.0% holding in specialist medical provider Strategis Insurance Tanzania.

CFC Life manages the long-term business

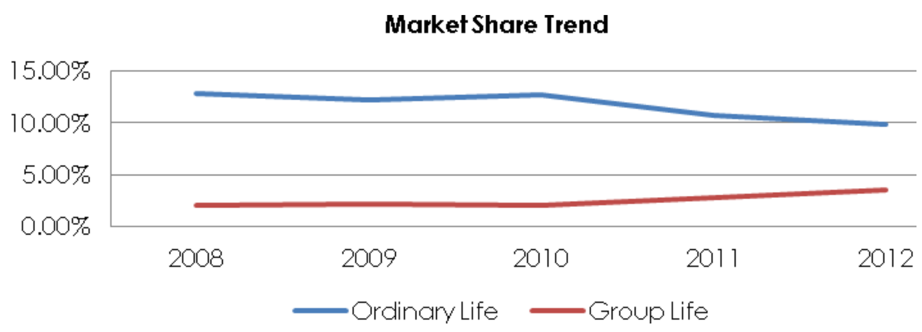
CFC Life manages the life (long-term business) assurance and has been in operation since 1964. Complete transfer of business to the respective companies (Life Business to CFC Life and General Business to Heritage) was finalized in 2012.

CFC LIFE HIGHLIGHTS

Group life market share rose to 3.6% in FY2012

Increasing Group Life Market Share with drop in Ordinary Life Market Share: According to data from the Association of Kenya Insurers (AKI), CFC Life's group life written premiums grew at a 5 year CAGR of 39.1% from KES 95 million in FY2008 to KES 357 million in FY2012. Group life market share rose to 3.6% in FY2012 from 2.1% in FY2008.

Ordinary life premiums on the other hand experienced a more conservative 5 year CAGR of 6.1% from KES 913 million in FY2008 to KES 1.1 billion in FY2012. Ordinary life market share deteriorated from a high of 12.9% in FY2008 to 9.9% in FY2012. We attribute this to the stiff competition in the market.



Source: AKI 2012

Company is losing out on premium income to competitors in ordinary life

Although ordinary life premium recorded a 5 year CAGR of 6.1%, the deteriorating market share indicates that the company is losing out on premium income to competitors. Group life premium growth can be attributed to innovative products such as the last expense protection plan that covers the costs of funeral/burial expenses of employees and/or spouses.

We expect group life to continue with the upward trend in the short term given its current success in winning business from competition. We expect ordinary life market share to hold at current levels in the short term.

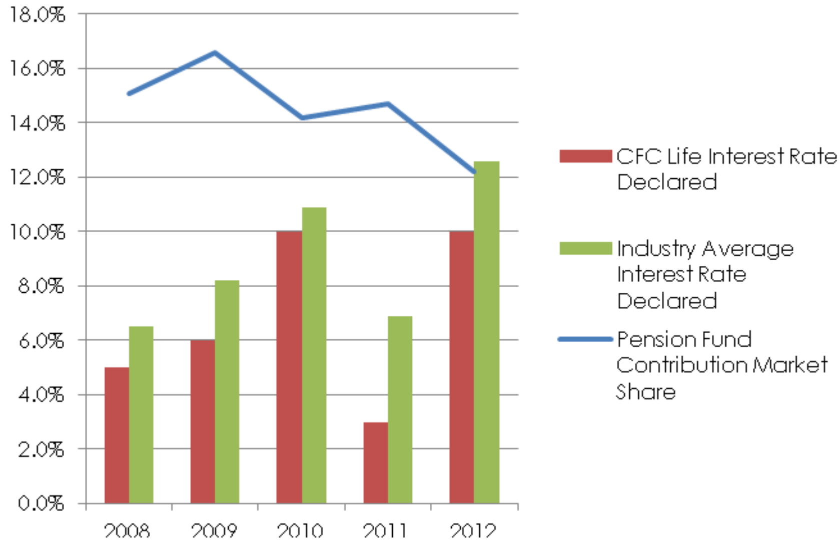
Market tends to shy away from risk based products

Product Range and Innovation: According to management, the market tends to shy away from risk based products and tends to prefer investment and saving products more.

CFC Life identifies its Endowment Plan, Income Builder (Savings Plan) and Lifevest plan (Unit-linked) product as its flagship products. Notable efforts in product development include Msiba Plan launched during 1Q2013 that offers insurance cover for natural and accidental loss of life and impairment caused by an accident.

Sub-par interest rates declared on deposit administration contracts

Pension Fund Contribution and Performance: Over the past five years, CFC Life has displayed a declining trend in its annual pension fund contributions market share. This essentially indicates that the firm is losing out on pension fund contributions to other competitors. This could be attributed to the sub-par interest rates declared on the deposit administration contracts by CFC Life as compared to the industry.



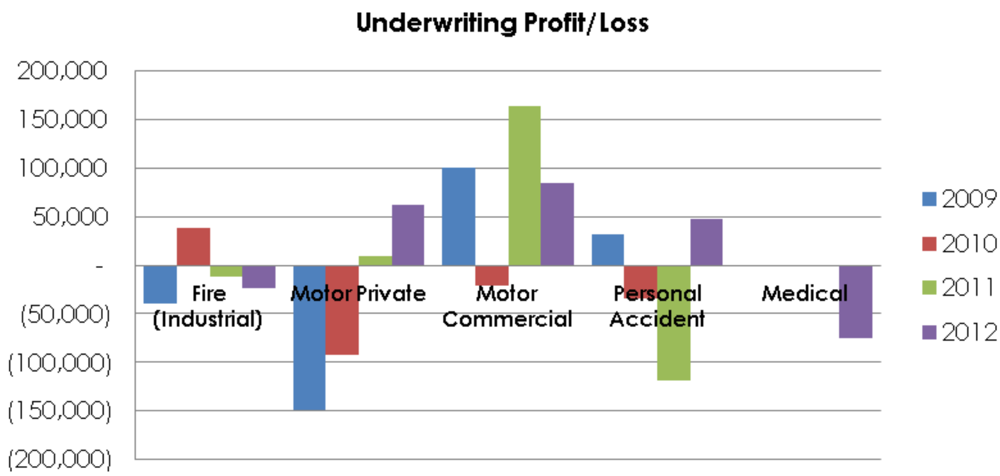
Source: AKI

We expect CFC Life to find it challenging to compete for the pension funds

If the trend on lower interest on pension funds, compared to the industry average, is sustained, we expect CFC Life to find it challenging to compete for the pension funds.

HERITAGE INSURANCE HIGHLIGHTS

Mixed Performance in Key Insurance Classes: Heritage Insurance managed to turn around underwriting losses in motor and personal accident insurance classes in FY2011 and FY2012 respectively. However, Fire (Industrial) has been unable to make underwriting profit since FY2011. The Medical Insurance class contributed to underwriting losses in FY2012. The Medical Book was fully transferred from CFC Life in FY2012.



Source: Company Reports

Committed to strict discipline in ratings and valuation

Management is committed to strict discipline in ratings and valuation in order to curb rising claims in motor and personal accident classes of business. This led to a 49.5% drop in Insurance contract liabilities (FY2012).

We expect slow growth in the long term in contract liabilities in the long term, given the strict ratings and valuation policies. Equally, we expect modest growth in premiums due to the same strict ratings.

Underwriting profit in fire industrial and medical highly volatile

However, underwriting profit in fire industrial and medical is highly volatile given the high claims and expenses incurred respectively. We still expect to see underwriting losses in the short term on both classes given the fierce competitive pressure on premiums and the typical nature of the classes that involve high claims payouts.

Disposed its 45.0% stake in Alliance Insurance Corporation (Tanzania)

Tanzania Subsidiaries and Associates: Liberty Kenya Holdings disposed its 45.0% stake in Alliance Insurance Corporation (Tanzania) Limited that was owned indirectly through Heritage Insurance Company. Heritage had initially invested to access retail life business in the Tanzanian market. The disposal of its stake in Alliance Insurance was informed by a strategic decision to consolidate operations and interests within the subsidiary.

Liberty has a 40.3% stake in Strategis Insurance

Liberty has a 40.3% stake in Strategis Insurance, a medical underwriting company. Management described the Tanzanian market as challenging especially in a difficult class of business such as medical. Furthermore, rate-cutting also seems to be a persistent problem in the market. Despite this, management expects a positive outcome for the subsidiary that posted a 23.0% growth in gross earned premium in FY2012 and operates in a market with low insurance penetration. According to the Tanzania Insurance Regulatory Authority (TIRA), the insurance penetration stood at 0.9% in 2011.

GROWTH DRIVERS

Primarily relied on brokers and agents to distribute its products

Diversification from Traditional Distribution Channels: Liberty Kenya has primarily relied on brokers and agents to distribute its products with CFC Life having about 400 agents and about 50.0% of Heritage Insurance business coming from brokers.

Both Heritage and CFC Life have partnered with various banks such as CFC Stanbic and Chase Bank to leverage on their branch networks and agents to access potential customers. This saves the company brick and mortar costs of setting up physical branches. It is worthy to note that a major portion (management estimate of about 90.0%) of CFC Life premium earned through bancassurance is from the bank itself in terms of covers for credit risk, mortgage default and the bank staff.

Use of Technology in Distributing Products: The expected partnerships between Liberty and telecommunication companies could be the impetus for increased written premiums. This however hinges on the combination of appropriate products and strategies employed to reach the target market.

Difficulties catching up with competitors

Plans are also in place to partner with mobile operators to develop products that can be pushed through the mobile phone. Although it is a strategic decision, we expect Liberty to have difficulties catching up with competitors that have already launched and are maximizing on their first-mover advantage.

According to the Kenya Finaccess National Survey 2013, more than double the number of adults use mobile phone financial services (11.5 million) compared with banks (5.4 million). The use of mobile phone financial services more than doubled from 28.0% in 2009 to 62.0% in 2013 with 75.0% of the urban population citing mobile money agents as the closest financial services provider. This provides a huge market to be reached through the mobile phone.

Local competitors have the flexibility to adapt quickly

The key competitors, being local have the flexibility to adapt to the quickly changing underlying market environment. Since no one has struck the right model to revolutionize and increase uptake of insurance products, we believe there will be a lot of trial and error, which will require companies to constantly evolve.

Efficiency via Investment in IT: Heritage Insurance is currently in the process of setting up a new ERP (Enterprise Resource Program) that should be implemented during 1H2014. This is expected to rationalize operating expenses and increase efficiency. Going forward, we expect a decrease in staff costs (KES 843 million for FY2014 from KES 996 million for FY2012).

KEY INVESTMENT RISKS

Rampant rate under-cutting in both the Kenyan and Tanzanian insurance industries

Does Liberty Have a Competitive advantage? In our view, Liberty Kenya Holdings will have difficulties trying to catch up with competition in terms of product innovation. Additionally, rampant rate under-cutting in both the Kenyan and Tanzanian insurance industries poses a threat to Liberty. This is evidenced by the declining ordinary life market share in CFC Life and the drop in earned premiums from Motor Commercial Insurance Class in Heritage Insurance.

Going forward, we believe that Liberty Kenya's conservative approach in underwriting and investments could lead to the company lagging behind competitors who are capable and flexible enough to adapt to the local market conditions.

FINANCIAL ANALYSIS

Income Statement

	FY2010	FY2011	FY2012	FY2013	4 Year CAGR	FY2014F	FY2015F
Gross earned premium	4,819,293	6,389,035	6,953,842	7,397,981	15.4%	7,739,102	8,271,386
Less: ReInsurance premium ceded	(1,287,384)	(2,151,102)	(2,971,456)	(3,330,854)	37.3%	(3,637,378)	(4,052,979)
Net earned premiums	**3,531,909**	**4,237,933**	**3,982,386**	**4,067,127**	**4.8%**	**4,101,724**	**4,218,407**
Commissions earned	217,184	513,025	660,441	657,492	44.7%	619,128	636,897
Investment Income	1,581,130	1,640,630	2,591,896	2,629,519	18.5%	2,808,986	3,084,499
Administration Fees	17,079	13,937	13,292	15,897	-2.4%	14,793	15,810
Other Income	27,351	27,730	212,849	8,574	-32.1%	7,739	8,271
Total Income	**5,374,653**	**6,433,255**	**7,460,864**	**7,378,609**	**11.1%**	**7,552,370**	**7,963,884**
Claims and policyholder benefits payable	(2,804,362)	(3,379,417)	(3,337,436)	(8,088,006)	42.3%	(5,354,933)	(5,915,731)
Change in insurance contract liabilities	(182,732)	(39,214)	(480,031)	(490,432)	39.0%	(514,972)	(583,645)
Amounts recoverable from reinsurers	272,622	936,137	708,545	5,501,597	172.3%	2,909,902	3,242,383
Net insurance benefits and claims	**(2,714,472)**	**(2,482,494)**	**(3,108,922)**	**(3,076,841)**	**4.3%**	**(2,960,002)**	**(3,256,993)**
Commissions payable	(638,652)	(1,003,068)	(892,089)	(833,885)	9.3%	(773,910)	(744,425)
Finance costs	(75,395)	(74,233)	(95,179)	(25,512)		-	-
Acquisition costs	(145,341)	-	-	-		-	-
Other operating expenses	(1,354,640)	(1,863,626)	(2,185,477)	(2,136,123)	16.4%	(2,159,432)	(2,117,508)
Total expenses and commissions	**(2,214,028)**	**(2,940,927)**	**(3,172,745)**	**(2,995,520)**	**10.6%**	**(2,933,342)**	**(2,861,933)**
Result of operating activities	446,153	1,009,834	1,179,197	1,306,248	43.1%	1,659,026	1,844,959
Earnings from associates	36,782	2,381	23,704	(7,387)	-158.6%	(7,387)	(7,387)
Profit before taxation	**482,935**	**1,012,215**	**1,202,901**	**1,298,861**	**39.1%**	**1,651,639**	**1,837,572**
(Loss)/profit for the year	**260,014**	**950,418**	**886,671**	**1,105,919**	**62.0%**	**1,391,513**	**1,548,162**

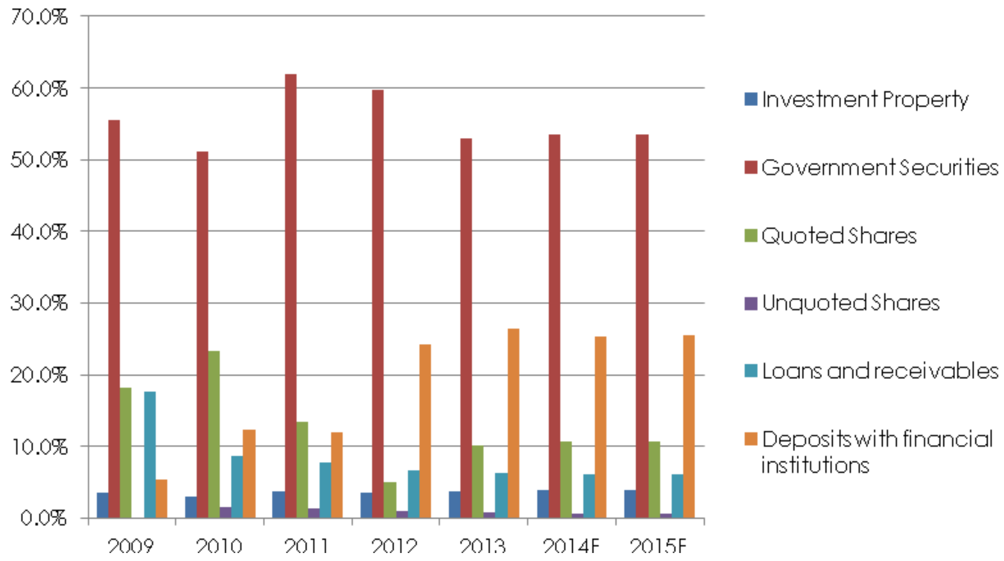
Growth mainly propelled by short-term business

Short Term business propelled gross earned premium: Gross earned premium grew at a CAGR of 15.4% from KES 4.8 billion (FY2010) to KES 7.4 billion (FY2013). Growth was mainly propelled by short-term business particularly in personal accident and medical (3 year CAGR of 61.8%), Fire (3 year CAGR of 53.2%) and Motor (3 year CAGR of 13.9%). Retail life however posted a negative CAGR of 15.5% to KES 1.2 billion (FY2012) from KES 1.6 billion (FY2010).

One off income from disposal of Alliance Insurance: Other income recorded a negative 4 year CAGR of 32.1% to KES 9 million (FY2012) from KES 27 million (FY2010). The spike in growth in other income (FY2012) was on the back of a one-off profit on sale of investment of associate (Disposal of 45.0% stake in Alliance Insurance Tanzania).

Conservative investment strategy: Liberty has maintained a conservative investment strategy with bulk of investments held in money markets and bonds (5 year average of 56.2% of total investment mix) and minimal exposure to quoted equities and investment property.

Minimal exposure to quoted equities and investment property



Source: Company Reports, FIB Estimates

Management indicated their intention to allocate more towards quoted equities and investment property given the recent rallies in the stock market and significant gains in real estate.

Lower Staff Costs Lead to Reduced Growth in Total Expenses and Commissions: Total expenses and commissions grew at a CAGR of 10.6% to KES 3.0 billion (FY2013) from KES 2.2 billion (FY2010). Negative year-on-year growth of 5.6% was recorded in FY2013. This could be attributed to lower staff costs that dropped by 1.0% to KES 996 million. Notably, staff costs in CFC Life dropped by 22.1% in FY2012 as a result of staff rationalization arising from business reorganization.

Balance Sheet

	FY2010	FY2011	FY2012	FY2013	4 Year CAGR	FY2014F	FY2015F
Shareholders' Funds	**4,676,659**	**4,174,597**	**5,421,591**	**5,464,882**	**5.3%**	**5,672,706**	**5,965,586**
ASSETS							
Property and Equipment	1,092,963	1,056,551	1,097,599	1,084,901	-0.2%	1,087,430	1,090,440
Investment Property	545,000	623,553	710,449	842,200	15.6%	973,479	1,070,827
Financial Investments - Held To Maturity	4,175,977	8,900,449	9,346,452	6,495,960	15.9%	7,148,481	7,865,964
Financial Investments - Available for sale	9,355,871	4,278,039	4,124,310	8,018,693	-5.0%	8,919,415	9,795,677
Financial Investments - Loans and Receivables	1,552,862	1,332,388	1,362,600	1,352,055	-4.5%	1,490,755	1,645,753
Deposits with financial institutions	2,181,279	2,038,661	4,951,216	5,735,655	38.0%	6,293,438	6,943,829
Total Assets	**23,827,329**	**24,293,533**	**27,390,346**	**31,452,640**	**9.7%**	**33,775,344**	**36,925,059**
LIABILITIES							
Insurance Contract Liabilities	6,027,195	6,689,310	7,538,857	10,320,927	19.6%	12,261,233	14,591,128
Deposit Administration Liabilities	8,703,273	9,237,856	10,104,276	11,103,757	8.5%	11,388,877	11,754,460
Unearned Premium Reserve	1,853,053	2,242,031	2,325,287	2,664,554	12.9%	2,786,077	2,894,985
Borrowings	500,000	504,621	479,796	-		-	-
Total Liabilities	**19,150,670**	**20,118,936**	**21,968,755**	**25,987,308**	**10.7%**	**28,102,638**	**30,959,473**

UNDERWRITING BUSINESS

UNDERWRITING PROFIT/(LOSS)	FY2010	FY2011	FY2012	FY2013	FY2014F	FY2015F
Net earned premium	3,531,909	4,237,933	3,982,386	4,067,127	4,101,724	4,218,407
Net Claims & Benefits Payable	(2,714,472)	(2,482,494)	(3,108,922)	(3,076,841)	(2,960,002)	(3,256,993)
Commissions earned	217,184	513,025	660,441	657,492	619,128	636,897
Commissions Payable	(638,652)	(1,003,068)	(892,089)	(833,885)	(773,910)	(744,425)
Operating & other expenses	(1,354,640)	(1,863,626)	(2,185,477)	(2,136,123)	(2,159,432)	(2,117,508)
Underwriting profit/ (Loss)	**(958,671)**	**(598,230)**	**(1,543,661)**	**(1,322,230)**	**(1,172,492)**	**(1,263,622)**
Underwriting profit/ (Loss) Margin	**-27.1%**	**-14.1%**	**-38.8%**	**-32.5%**	**-28.6%**	**-30.0%**

KEY RATIOS

UNDERWRITING RATIOS	FY2010	FY2011	FY2012	FY2013	FY2014F	FY2015F
Loss Ratio	76.9%	58.6%	78.1%	75.7%	72.2%	77.2%
Managements' Expense Ratio	38.4%	44.0%	54.9%	52.5%	52.6%	50.2%
Combined Ratio	115.2%	102.6%	132.9%	128.2%	124.8%	127.4%

PROFITABILITY RATIOS	FY2010	FY2011	FY2012	FY2013	FY2014F	FY2015F
Net Profit Margin	5.4%	14.9%	12.8%	14.9%	18.0%	18.7%
ROaE	8.9%	21.5%	18.5%	20.3%	25.0%	26.6%
ROaA	1.5%	4.0%	3.4%	3.8%	4.3%	4.4%
Investment Yield	8.6%	9.2%	12.3%	11.3%	11.1%	11.1%

VALUATION

We used the P/B Multiple valuation approach to obtain our target price. The target price was obtained using our forecasted BVPS and the average P/B multiple of the recommended comparables.

Our valuation methodology was informed by the fact that insurance companies, as is the case with other financial institutions, mark to market a majority of their balance sheet.

P/B Multiple Valuation	
Current Market Price (7.05.14)	22.50
Trailing BVPS:2013	10.52
Trailing P/B	2.14
Forecasted BVPS: FY2014	11.01
Sub-Saharan African Sample	2.21
Target Price	**24.33**
Upside Potential	**8.1%**

RECOMMENDATION

We initiate coverage on Liberty Kenya with a NEUTRAL recommendation

We initiate coverage on Liberty Kenya with a **NEUTRAL recommendation**. Our target price of KES 24.33 provides an 8.1% upside potential from the current share price of KES 22.50. (7.5.2014). We are of the opinion that Liberty Kenya Holdings lags behind the competition in regards to flexibility, tact and aggressiveness to succeed in the local dynamic insurance industry.

PAN AFRICA INSURANCE KENYA

Bloomberg Ticker	PAIL:KN
Fair Value (KES)	144.43
Price in KES - 09.05.2014	136.00
Issued Shares (Mn)	96.00
Market Cap (KES Bn)	13056.00
Market Cap (USD Mn)	150.07
Year End	Dec 31st
Free Float (%)	23.34
KES/USD (87.00)	

Investment Summary

We initiate coverage on Pan Africa with a **NEUTRAL recommendation.** Our price target of KES 144.43 represents a 6.2% upside potential from the current share price of KES 136.00 (07.05.2014).

We initiate coverage on Pan Africa with a NEUTRAL recommendation

Major Shareholders	Shares Held	% Shareholding
Hubris Holdings Limited	53,585,600	55.82
Patel Baloobhai Chhotabhai	19,186,800	19.99
Mayfair Insurance Company	817,700	0.85
Thammo Holdings	742,242	0.77
APA Insurance	720,038	0.75
Anjay Vithalbhai Patel	576,600	0.60
Financial Futures Limited	574,474	0.60
Standard Chartered Nominees A/C 9595	568,400	0.59
Canon Assurance	496,476	0.52
Leverton Ltd	400,000	0.42
	77,668,330	80.91

Key Investment considerations include:-

Significant potential in life insurance: The life insurance industry in the country remains largely untapped. Industry players estimate that there are about 600,000 life policies, out of an estimated 3.6 million people in the middle class category, and a penetration level of 1.1% (2012). We believe that Pan Africa's written premiums will grow driven mainly by the strong market position of the company and the growing middle class.

Bima Mkononi: Pan Africa partnered with Airtel Kenya and Microensure to launch Bima Mkononi in 4Q2013. Given the significant potential for life insurance in Kenya (life penetration of 1.1%), this product with the key features of affordability and accessibility could give Pan Africa direct access to the millions of the people who are uninsured.

Top position in group life with a 31.4% market share

Resurgence in Corporate Business: FY2012 saw Pan Africa reclaim its top market position in group life written premiums with a 31.4% market share (22.2% market share in 2011). We expect Pan Africa to post moderate growth in the medium-term.

Alternative Distribution Channels: Pan Africa has traditionally relied on insurance brokers and agents as the main distribution channels for its products. In order to scale back on the costs incurred in acquisition of new business, Pan Africa is building relationships with banks (bancassurance) so as to leverage on their extensive networks provided by their branches and agents.

	FY2011	FY2012	FY2013	FY2014F	FY2014F
Gross Premium Income (KES '000)	3,648,492	5,440,654	5,324,099	5,483,822	5,770,354
EPS (KES)	4.62	7.27	13.05	14.88	14.69
BVPS (KES)	22.11	27.38	34.78	42.05	50.46
P/E x	4.49	5.53	10.42	9.14	9.26
P/B x	0.94	1.47	3.91	3.23	2.70
ROE	20.9%	26.6%	37.5%	35.4%	29.1%
ROA	3.9%	4.2%	5.9%	5.8%	5.1%
Managements' Expense Ratio	22.2%	16.7%	18.8%	20.2%	20.4%

BRIEF HISTORY

Pan Africa underwrites all classes of long-term business with the exception of industrial life business

Pan Africa Insurance Holdings Limited was incorporated in 1946 with the principal activity of the group carried out through its subsidiary Pan Africa Assurance Limited. Pan Africa Assurance underwrites all classes of long-term insurance business with the exception of Industrial Life business. The group also has interests in Pan Africa Securities, Sanlam Investment (wholly owned subsidiary), Mae Properties Limited (wholly owned subsidiary) and Runda Water Limited (24.9% shareholding).

BUSINESS GROWTH DRIVERS

Estimate of about 600,000 life policies in the market

Significant potential in life insurance: The life insurance industry in the country remains largely untapped. Industry players estimate that there are about 600,000 life policies out of an estimated 3.6 million people in the middle class category and a penetration level of 1.1% as at 2012.

Pan Africa has consistently managed to retain the second position in Individual life market share for the past five years (2008 – 2012) behind market leader Britam. It maintained the top position in group life market share in 4 out of the past 5 years (second position in 2011).

We believe that Pan Africa written premiums will grow in line with the growth in the industry total life business premiums (5 year CAGR of 16.7%). This is supported by the large position in market share Pan Africa enjoys out of a total of 23 competitors in the life business and the growth of the middle class segment of the population.

Product Innovation

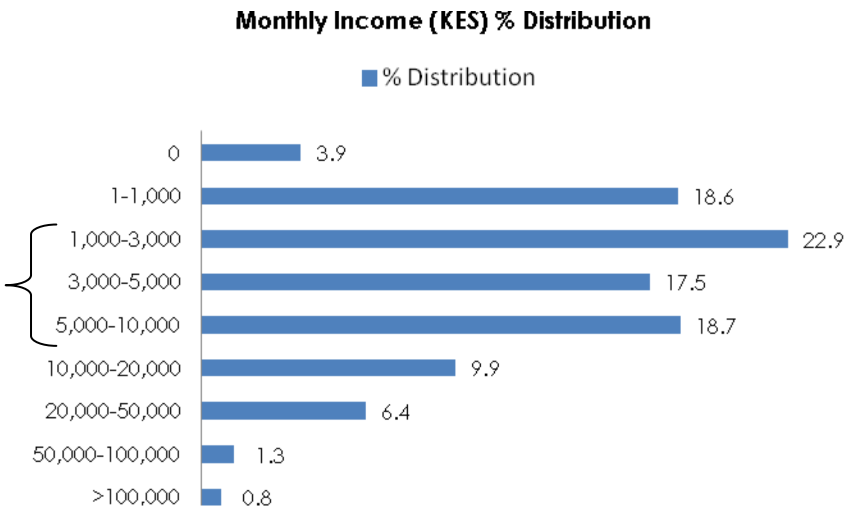
Bima Mkononi is a mobile-phone based product

- ***Bima Mkononi:*** Pan Africa partnered with Airtel Kenya and Microensure to launch Bima Mkononi in 4Q2013. Bima Mkononi is a mobile-phone based product primarily targeted at the bottom of the pyramid income segment. It offers a predetermined lump sum payment in the event of death and disability of the insured. With its relatively cheap weekly premium structure, the product demystifies the widely-held notion that life assurance is an expensive product reserved for the upper and middle class.

Monthly Premium	Weekly Premium	Subscriber cover	Family Member Cover
KES 60.00	KES 15.00	KES 25,000	KES 25,000
KES 100.00	KES 25.00	KES 50,000	KES 50,000
KES 140.00	KES 35.00	KES 75,000	KES 75,000
KES 180.00	KES 45.00	KES 100,000	KES 100,000

Given the high potential for life insurance in Kenya (life penetration of 1.1%), this product with the key features of affordability and accessibility could give Pan Africa direct access to the millions of the people who are uninsured.

Ideal product for monthly income between KES 1,000 and KES 10,000



Source: **Finaccess 2013, FIB Estimates**

Key features of affordability and accessibility

The KES 1,000 to KES 10,000 monthly income bracket accounts for 59.1% of total income distribution according to the Kenya Finaccess October 2013 report. We believe that the product would be most suitable for those earning between KES 1,000 and KES 10,000 monthly, where the monthly premiums would account for a range between 18.0% and 0.6% of monthly income.

Achieving potential dependent on product awareness and reach

However, we believe that achieving this potential is largely dependent on the strategy to create product awareness and the reach of the mobile network operator (Airtel) involved in distribution. Data from the Communications Commission of Kenya (CCK) shows that Airtel had a market share of 17.6%, second behind Safaricom which commanded a 66.5% market share as at 3Q2013.

We expect moderate uptake of the product in the mid-term.

Strong uptake of Umash Funeral Package

Umash Funeral Package: Pan Africa partnered with Umash funeral services in 3Q2011 to provide a burial cover for the insured, spouse, children of up to two years and parents aged up to 75 years. At a minimum annual premium of KES 1,200, the product offers the same level of affordability with Bima Mkononi.

Monthly Premium	Weekly Premium	Funeral Package cover	Cash Pay Out Cover
KES 100.00	KES 25.00	KES 100,000	N/A
KES 200.00	KES 50.00	KES 200,000	N/A
KES 150.00	KES 37.50	N/A	100,000
KES 233.33	KES 58.33	N/A	200,000

Management indicated strong uptake of the product that has close to 50,000 policies and is exhibiting positive growth.

The key risk inherent in this product is the cultural barrier of the elderly that tend to hold death as an extremely sensitive issue.

Appropriate product for the growing middle class

However, the company's understanding of the target market has led to strong uptake of the product. This could be a signal of a younger enlightened generation that appreciates the benefit of the cover.

Ghana is a good example of a country that has embraced funeral cover and has strong uptake of funeral-based products. Enterprise Group, (a leading Ghanaian insurance company), benefit payments increased by 48.0% y-o-y in FY2012 with funeral products accounting for 99.0% of all benefit payments made. Enterprise Life's funeral insurance policy accounts for more than 65.0% of revenue.

	2008	2009	2010	2011	2012
Total Registration of Deaths	199,567	189,048	175,760	174,487	173,912

Source: Kenya National Bureau of Statistics

With an average death rate of 182,555 per year for the past 5 years (2012-2008), this burial cover serves as the appropriate product for the growing middle class given its affordability (average premium of KES 200 per month).

Below is a scenario showing the probable premiums earned from the Umash Funeral Cover product given a subjective annual growth rate of 10.0% and the minimum annual payment of KES 1,200.00.

	2013	2014F	2015F
Number of policies	50,000	55,000	60,500
% Growth Rate		10.00%	10.00%
Premium Income (KES '000)	**60,000**	**66,000**	**72,600**

Source: FIB Estimates

We expect the contribution of the product to individual life premium to grow moderately in the medium-term.

Stiff competition in corporate business

Corporate Business: The group life assurance business in Kenya is competitive with over 20 companies targeting the same market. This environment has forced competitors to resort to price undercutting in order to win business.

FY2012 saw Pan Africa reclaim its top market position in group life written premiums with a 31.4% market from 22.2% market share in FY2011.

Individual (Ordinary Life) also posted a marginal increase in market share to 19.7% in FY2012 from 19.3% in FY2011.

	2009	2010	2011	2012
Individual Life	19.9%	19.8%	19.3%	19.7%
Group Business	27.0%	32.6%	22.2%	31.4%

Source: AKI

Group business market share demonstrated volatility from FY2009 to FY2012 mainly due to stiff competition in the market. However, with innovative products, superior service delivery and leverage on appropriate and effective distribution channels, we expect Pan Africa to post moderate growth in the medium-term.

Full acquisition of Sanlam Investment in 3Q2013

Strategic Acquisition: Pan Africa fully acquired Sanlam Investment in 3Q2013. This was a strategic move by the company to facilitate easier distribution of investment products by its financial advisors. Management had indicated its intention to create unit trusts following the acquisition of Sanlam.

We expect Sanlam Investment to record growth in fee, interest and investment income and contribute marginally to the company's bottom line. However, we do not see this as a significant revenue driver of revenue in the short term given the industry's low net profit margins for unit trusts.

As of FY2012, the investment segment of the group recorded a KES 367 million profit after tax with a 512.5% increase in interest income to KES 129 million and a 47.2% drop in investment income to KES 43 million.

Alternative distribution channels: Pan Africa has traditionally relied on insurance brokers and agents as the main distribution channels for its products. Although effective, this channel is expensive as evidenced by the high commissions payable that stood at 13.6% of gross written premiums in FY2013.

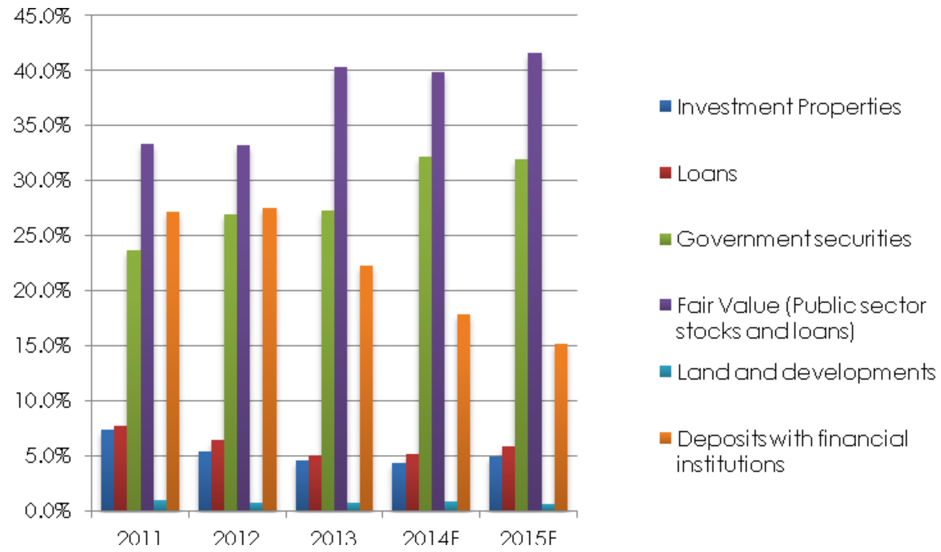
Bancassurance saves the company significant costs

In order to scale back on the costs incurred in acquisition of new business, Pan Africa is building relationships with banks (bancassurance) so as to leverage on the extensive networks provided by their branches and agents. This saves the company significant costs of setting up physical branches and costs associated with upkeep of financial advisors and agents. Since the launch of bancassurance, it has yet to contribute a substantial amount of premium to the top line.

Bima Mkononi, as previously alluded to, offers a cheaper channel through which premiums can be collected. Management indicated that commission expense for agents could cost up to 40.0% while commission expense for bancassurance and alternative distribution channels could cost up to 15.0%.

Increased concentration in investment properties, loans, equities and deposits with financial institutions

Changing Investment Mix: Pan Africa has over the past 3 years adopted a more aggressive approach towards investment with increased concentration in investment properties, loans, equities and deposits with financial institutions. This translated into increased rental income, interest income and realized and unrealized gains from financial assets.



The average yields (FY2009 to FY2012) from gross rental income, loans and receivables interest income, held-to-maturity financial assets (Government securities) and cash and cash equivalents stood at 6.4%, 8.2%, 10.0% and 5.7% respectively.

	2011	2012	2013	2014F	2015F
Investment Income/Total Revenue	18.1%	15.8%	18.0%	19.4%	18.9%

Deposits with financial institutions are expected to drop marginally

In the short term, we expect increased exposure to equities, investment property, land and developments and loans. Deposits with financial institutions are expected to drop marginally in the medium term given the relatively lower interest rate environment. Moderate growth is expected in the Government securities given that the company's investments are regulated by the Insurance Regulatory Authority (IRA).

KEY INVESTMENT RISKS

Competitors utilize price undercutting tactics to win business

Price Undercutting: As mentioned earlier, over 20 companies are in the life insurance business in Kenya with Pan Africa achieving 2nd position in market share in ordinary life and 1st position in group life as at the end of FY2012. A key industry issue is the price undercutting tactic utilized by competitors to win business.

KEY RATIOS

KEY RATIOS	FY2010	FY2011	FY2012	FY2013	FY2014F	FY2015F
Net Profit Margin	15.4%	12.2%	12.8%	23.5%	26.1%	24.4%
ROE	32.2%	20.9%	26.6%	37.5%	35.4%	29.1%
ROaE	37.3%	22.4%	29.4%	42.0%	38.7%	31.8%
ROA	5.5%	3.9%	4.2%	5.9%	5.8%	5.1%
ROaA	6.5%	4.0%	5.0%	6.7%	6.2%	5.4%
Investment Yield	6.3%	7.0%	8.6%	8.0%	7.7%	7.2%
Management's expense ratio	17.0%	22.2%	16.7%	18.8%	20.2%	20.4%

FINANCIAL PERFORMANCE

Income Statement	FY2010	FY2011	FY2012	FY2013	FY2014F	FY2015F
Gross premium income	3,830,693	3,648,492	5,440,654	5,324,099	5,483,822	5,770,354
Premium ceded to reinsurers	(287,744)	(348,437)	(315,020)	(222,272)	(274,191)	(299,012)
Net premium income	**3,542,949**	**3,300,055**	**5,125,634**	**5,101,827**	**5,209,631**	**5,471,342**
Commission income	66,639	84,589	75,866	52,680	54,260	75,718
Investment return	420,398	697,015	1,244,574	1,534,084	1,750,066	1,826,861
Fair value gains/(losses)	689,884	(895,668)	879,863	1,168,709	1,315,569	1,505,390
Other operating revenue	128,684	664,793	554,694	685,054	714,635	765,264
Total other revenue	1,305,605	550,729	2,754,997	3,440,527	3,834,530	4,173,233
Total Revenue	4,848,554	3,850,784	7,880,631	8,542,354	9,044,161	9,644,575
Net benefits and claims	(2,999,399)	(1,876,475)	(5,521,395)	(5,274,338)	(5,414,335)	(5,795,025)
Fee and commission expense	(890,043)	(690,346)	(669,678)	(724,477)	(767,735)	(807,850)
Other operating and administrative expenses	(603,311)	(733,046)	(856,582)	(960,408)	(1,053,943)	(1,117,378)
Cost of sales	-	-	-	(68,775)	(70,838)	(74,540)
Total benefits, claims and other expenses	(4,492,753)	(3,299,867)	(7,047,655)	(7,027,998)	(7,306,851)	(7,794,792)
Profit before income tax	**661,700**	**552,435**	**834,646**	**1,516,444**	**1,739,763**	**1,852,667**
Income tax charge	(75,942)	(109,030)	(136,375)	(266,012)	(310,938)	(441,990)
Profit for the year	585,758	443,405	698,271	1,250,432	1,428,825	1,410,676

Growth driven by both individual and group business

Strong Growth in Gross Premium Income: Gross Premium Income recorded a Compounded Annual Growth Rate (CAGR) of 11.6% over the past four years from KES 3.8 billion in FY2010 to KES 5.3 billion in FY2013 on the back of steady premium growth from individual life and premium growth from group business. FY2013 recorded a slight drop (2.1% decline) in gross premium income that could be attributed to the loss of income in the highly competitive group business. Going forward, we forecast a 3.0% gain in gross premium income to KES 5.5 billion for FY2014 driven by new acquisitions in group business and increased premium from individual life.

Interest Income from government securities and cash and cash equivalents were the main drivers of investment income growth

Interest Income Supports Investment Income Growth: Investment Income grew at a CAGR of 54.0% from KES 420 million in FY2010 to KES 1.5 billion in FY2013. Interest Income from government securities and cash and cash equivalents were the main drivers of investment income growth during the past four years.

Equities Boost Fair Value Gains: Fair value gains grew at a four-year CAGR of 19.2% to KES 1.2 billion (FY2013) from KES 689 million (FY2010). Notably, a fair value loss of KES 896 million occurred in FY2011. This was in line with the general downward trend of the stock market that posted a 27.7% decline during the year. Confidence has since returned to the market with unrealized gains and losses for the company posting positive returns and the stock market posting gains of 29.0% and 18.2% in 2012 and 2013 respectively. We expect a stable macroeconomic environment for the remainder part of the year characterized by relatively lower inflation and interest rates. We forecast a 12.6% growth to KES 1.3 billion on the back of realized and unrealized gains in both equities and debt securities.

Sale of plots is being facilitated by Mae Properties Limited

Sale of Plots Augments other Operating Revenue: Other operating revenue has grown at a four-year CAGR of 74.6% to KES 685 million (FY2013) from KES 129 million (FY2008) mainly driven by sale of plots. The sale of plots is being facilitated by Mae Properties Limited that owns half acre plots within the up-market Runda suburb. Management indicated its intention to increase these properties in the medium term. We forecast a 4.7% growth in other operating revenue to KES 715 million for FY2014.

New life administration system expected to increase efficiency

Investment in IT: Pan Africa invested in a new life administration system that should be operational by the end of 1Q2014. The system is expected to increase efficiency and save on staff costs going forward. We forecast operating expenses to stand at KES 1.0 billion (slower growth rate of 9.7%) for FY2014 informed by the planned implementation of the new Life Administration system during 1Q2014 that is expected to reduce staff costs going forward.

We project staff costs to stand at KES 404 million in FY2014 representing 38.4% of total operating and administrative expenses as opposed to 40.7% in FY2012.

Steady Increase in Benefits and Claims: Net benefits and claims have grown at a four-year CAGR of 20.7% to KES 5.3 billion (FY2013) from KES 3.0 billion (FY2010). We forecast a 2.7% growth to KES 5.4 billion for FY2014 on the back of increasing death and disability claims, maturity and survival benefits and annuities.

Alternative distribution channels set to ease pressure on free and commission costs

Marginal Growth in Fee and Commission Expense: Fee and commission expense recorded a negative four-year CAGR of 6.6% to KES 724 million (FY2013) from KES 890 million (FY2010). Notably, an 8.2% year-on-year growth was recorded in FY2013. We forecast a lower growth rate of 6.0% to KES 768 million informed by the company's intention to acquire more business from both the individual and group business lines. We expect alternative distribution channels such as bancassurance and Bima Mkononi to substantially ease pressure on fee and commission costs in the medium term.

Balance Sheet	FY2010	FY2011	FY2012	FY2013	FY2014F	FY2015F
Assets						
Investment properties	435,600	766,618	820,000	922,282	1,037,322	1,314,377
Loans	613,443	793,082	964,427	1,006,619	1,224,099	1,571,622
Held to maturity financial assets	2,056,052	2,453,528	4,078,995	5,536,053	7,701,742	8,568,958
Fair value through profit and loss	3,900,292	3,449,297	5,038,609	8,181,718	9,542,885	11,155,186
Deposits with financial institutions	-	2,807,818	4,169,370	4,505,266	4,280,003	4,066,003
Total Assets	**10,671,621**	**11,499,229**	**16,473,522**	**21,157,507**	**24,546,640**	**27,920,595**
Liabilities						
Insurance contract liabilities	3,178,811	3,469,504	5,221,365	6,868,452	7,674,609	8,305,271
Investment contract liabilities	4,022,147	4,390,298	6,680,701	8,069,684	9,631,237	11,335,860
Deposit administration contracts	706,181	681,547	1,071,633	1,335,921	1,766,473	2,013,854
Total liabilities	**8,839,100**	**9,376,589**	**14,100,258**	**17,799,064**	**20,736,168**	**22,898,081**
Shareholders' Funds	**1,832,521**	**2,122,640**	**2,628,911**	**3,338,443**	**4,036,590**	**4,844,180**

VALUATION

We used the P/B Multiple valuation approach to obtain our target price. The target price was obtained using our forecasted 2014 BVPS and a sample Sub-Sahara Africa P/B multiple that comprises Enterprise Ghana and the parent company (Sanlam South Africa).

Our valuation methodology was informed by the fact that insurance companies, as is the case with other financial institutions, mark to market a majority of their balance sheet.

P/B Multiple Valuation	
Current Market Price (7.05.14)	136.00
Trailing BVPS: 2013	34.98
Trailing P/B	3.89
Forecasted BVPS: 2014	42.05
Africa Insurance Comparable P/B	3.44
Target Price	**144.43**
Upside Potential	**6.2%**

RECOMMENDATION

We initiate coverage on Pan Africa with a NEUTRAL recommendation

We initiate coverage on Pan Africa with a **NEUTRAL recommendation.** Our price target of KES 144.43 represents a 6.2% upside potential from the current share price of KES 136.00 (07.05.2014).