MALAWI

Political and economic news

Government proposes a MWK 1.5trn 2018/19 national budget

Minister of finance, economic planning and development Goodall Gondwe presented the 2018/19 national budget to parliament on 18 May 2018 with total expenditure pegged at K1.5trn (USD 2bn) of which K391.7bn is set aside as development budget. Domestic revenues are projected at MWK 1.05trn while grants are expected to be K209bn. The growth in recurrent expenditure is said to be matched to growth in tax revenue making this a controlled budget. Budget deficit is expected to be 4.5% of GDP or K242bn however net domestic borrowing is expected to rise to K176bn. The highest allocations of expenditure budget have been made to education (K166bn) followed by agriculture and health at K151bn and K68.7bn respectively. In the development budget the allocations have been made to reflect the dictates of MGDSIII targeting agriculture sector (K78bn) road construction (K69bn) and education (K43bn). It is interesting to note that a total allocation of K9.8bn has been made for programmes that target the youth. A youth internship programme targeting 5,000 youths whereby they will be placed in various government departments as interns to equip them with skills and ethics for their future careers. A youth tree planting program targeting 10,000 youths has also been mooted to help with reforestation efforts.

Company news

FMBCH group leads the pack on its regional expansion

FMBcapital Holdings Plc (FMBCH) released its FY17 results after a very eventful year in which it acquired a controlling stake in Barclays Zimbabwe plc - a Zimbabwe stock exchange listed bank and 100% stake in Opportunity International Bank of Malawi as part of its complex restructuring process whose end game was the establishment of a bigger group registered in Mauritius. As part of the restructuring process; FMBCH acquired all the issued shares of FMB Plc group through a one-for-one share swap with shareholders of FMB Plc which was then listed on the Malawi Stock Exchange. The master stroke was the acquisition of a controlling interest in Barclays Zimbabwe which left some commentators in that country bemused with the development as they did not expect, in their wisdom, the river to flow upwards –so to speak. As it turned out, the timing of the acquisition could not have been better given the political developments that followed immediately after – a stroke of luck; but again, fortune favours the brave.

FMBCH delivered better FY17 results than its forecast in the prelisting statement issued during its listing on the MSE. Forecast earnings were USD 21.3m against USD 34.8m – representing 63% variance in favour. Over 50% of the value came from gains on bargain purchase of the acquisitions – the dominant one being the Barclays deal in which net assets valued at USD 36m, after adjusting for minority interests, were acquired at USD 17.4m resulting in a bargain gain of USD 18.6m; a great bargaining achievement. The market gave its vote of confidence to the restructuring process as FMB plc rose from its opening price of MWK 17.00 to MWK 45.00 by the date of listing of FMBCH plc on 18 September 2017. The price of FMBCH has since rallied to MWK 140.00 by 18 May 2018. –representing over 700% rise since January 2017. This makes FMBCH the biggest company by market capitalisation at MWK 327bn (USD445m) when compared to those companies on the domestic index.

Apart from Barclays Zimbabwe other territories net interest income grew 31% to USD 38m and group cost to income ratios improved from 65% to 62%. A further USD 6m capital injection was made to the Mozambican subsidiary to comply with minimum capital requirement dictated by the bank regulatory authorities. FMBCH has as a result raised its stake from 70% to 80%. In terms of performance this was the only loss making subsidiary with a loss of USD 2m while the holding company reported a loss of USD 1.7m. Mozambique is currently beset with challenges of debt default which has affected confidence levels from foreign cooperating partners and investors alike. The situation is expected to improve in the medium term when its extractive industries start in earnest. Other territories contributions to earnings were positive as follows; Malawi (USD 11.3m); Botswana (USD 2.7m); and Zambia (USD 2.3m). FMBCH balance sheet ballooned to USD 1.1bn of which USD 660m is in liquid assets.

The directors of FMBCH will be requesting shareholders at its forthcoming AGM to authorise them to raise capital through issue of shares to the extent of 10% of the company's issued capital – which can potentially be around USD 40m at current levels. The group is eventually planning to augument its capital through a capital raise and dual list on a regional stock exchange to enable it take advantage of opportunities in the region.

Should shareholders be worried about a one-off boost to earnings in form of USD 18m bargain gain? Ideally yes but we still see future value to come from the Zimbabwean subsidiary which was consolidated for about 2.5 months of the FY17 reflecting from 10 October 2017; the actual date the deal was closed. Barclays Zimbabwe FY17 earnings were just over USD 19m but only USD 4.1m is consolidated in FMBCH. We therefore see the current levels achieved as sustainable going forward. FMBCH has an option to acquire a further 19% of Afcarme Zimbabwe Holdings which will take its stake in Barclays Zimbabwe to 52%. As the group streamlines its operations over various geographical locations we expect some economies of scale to kick in and help with cost management. FMB plc has a history of maintaining lean costs and delivering attractive cost to income ratios, we see this attribute being replicated at FMBCH level. Although we believe most of the achievements of the group have been priced in at current levels, we still rate the stock as a BUY for long term holders on its exciting prospects.

FMBcapital Holdings Plc

FY 17 FMBCH ("USD")	2017	2016	% CHG
Interest income	63,707,350	47,008,665	35.5%
Interest expense	20,281,940	17,911,120	-13.2%
Net interest income	43,425,410	29,097,545	49.2%
Fees and commissions	22,115,286	12,982,780	70.3%
Gain on fx transactions	10,106,665	7,238,566	39.6%
Income from investments	3,227,697	-1,898,997	-
Total non-interest income	35,724,333	18,322,349	95.0%
Gains on bargain purchases	18,655,953	-	-
Total income	97,805,696	47,419,894	106.2%
Total expenses	55,453,025	31,678,053	-75.1%
Net earnings	34,858,163	10,591,597	229.1%

Source: Company filings

Illovo 1H18 results down 10% on finance costs

Illovo Sugar (Malawi) plc (Illovo) released its half year results for 2018 showing a 10% drop in earnings to MWK 6.9bn. There is a discrepancy in the comparative period as Illovo changed its financial year end to 31 Aug from previously 31 March. Thus the discrepancy is not only in the fact that six months is being compared to five in the previous period but also that the months being compared are totally different; September 2017 to February 2018 in current half versus April to August 2017 in the previous. In agriculture this is a typical case of comparing apples to oranges as the seasons are different.

Although turnover grew 34.6% to MWK 66bn, finance costs worsened 152% to MWK 4.3bn negatively impacting on earnings. What is interesting is that the 1H18 earnings are flat compared to 12 months ended 31 March 2017. Finance costs are said to be negatively impacted by foreign exchange losses a ZAR 345m loan which has since been reduced to ZAR 75m and is expected to be fully repaid by year end in August. Debt has been a major issue for Illovo in recent years making dividend payment a rarity.

Weather conditions at both estates are said to have been erratic in the period under review with the estates subjected to fluctuating periods of very wet weather and very dry conditions over the course of the period. This also impacted on the electricity generating capacity as low water levels impacted power production.

In terms of markets, the local market is said to have been somewhat affected by smuggling of sugar across the borders while exports into the region are said to have improved with sales into US markets producing positive gains.

Illovo's debt remains the huge elephant in the room as the company has continued to grapple with huge financial costs which erode earnings. Despite the predicament, the company needs to carry out capital intensive projects if it has to address its perennial concerns about power generation. We rate the stock as a SELL at current levels.

Illovo Sugar Malawi plc

1H18 ILLOVO ("MWK M")	2017	2016	% CHG
Revenue	66,210	49,099	34.8%
Operating profit	14,173	12,696	11.6%
Net finance cost	4,372	1,733	-152.3%
Net earnings	6,957	7,735	-10.1%

Source: Company filings and Cedar Capital

Corporate action

Dividends

COMPANY	YEAR	TYPE	AMOUNT	LAST CUM DATE
Standard Bank	2017	Final	MWK 4.26	TBA
BHL	2017	Final	MWK 0.15	TBA
SUNBIRD	2017	Final	MWK 0.63	TBA
TNM	2017	Final	MWK 0.25	TBA
NBM	2017	Final	MWK 8.33	TBA
PCL	2017	Final	MWK 20.00	TBA
NICO	2017	Final	MWK 1.00	TBA

Source: Company filings

Company announcements and our commentary – *(**this section is repeated**)*

- MPICO – expects its FY17 results to be at least 100% higher than FY16. Towards the end FY16, MPICO raised MWK 9bn in a renounceable rights issue which effectively converted its loans to equity. The effect of this transaction was a reduction in finance charges on loans which was reported at MWK4.1bn in FY16. We believe this is the main driver of earnings for FY17. On the other hand, we think the reduction in debt burden should help unlock value in rental income, especially from the Gate Way Mall whose occupancy rates were reported to be on the rise. We therefore forecast a minimum of 25% growth in 2018 barring any setbacks, especially on the long outstanding government debt. Source: Company filings and Cedar Capital

Market activity and colour

The market traded 12.1m shares in all 13 counters in 25 trades recording a market turnover of MWK 660.7m (USD 900K) during the week. This is to be compared to 21.1m shares worth MWK 2.1bn (USD 2.9m) in 33 trades registered in the previous week.

FMBCH and NICO traded the most value worth K285.9m and K210m respectively.

Risers during the week were FMBCH up 10% to K140; BHL up 8.5% to K35; and Sunbird edging up 5t to K141.05. There were no decliners. BHL closed for its corporate action of share split and bonus issue on 18 May 2017.

The market has demand for BHL, PCL, STANDARD, OML and NBM. Sellers are available in MPICO, NICO, FMBCH, NBS, TNM and ILLOVO. (Source: *MSE and Cedar Capital*)

Cedar Capital Limited
4th Floor, Livingstone Towers
Sir Glyn Jones Road
P O Box 3340
Blantyre, Malawi
+265 1 831 995
Feedback: nzimar@cedarcapital.mw

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