AFRICAN LIONS FUND

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Masaki
Dar es Salaam

27 March, 2024

Dear Investor,

Last month I announced I would go back to writing a monthly letter, because I find it difficult to talk about things that happened as long as 3 ½ months ago by the time I sit down to write a quarterly letter. Well, this month I am feeling like even last month was a long time ago, because we've seen a very sudden positive shift in sentiment in Kenya. The Nairobi bourse is up 40.7% (in USD terms) for the month of March alone.

Back in February, just before my latest research trip to Nairobi and Addis Ababa, for the Safaricom Investor Day, which I'll talk more about in a second, the mood in the Kenyan economy and stock market was still decidedly gloomy. Volumes on the Nairobi exchange had all but dried up. A few hundred thousand dollars' worth of shares trading in a session was not unusual.

The Kenyan Shilling was plumbing depths below 160 to the US Dollar, and there was still real concern about whether Kenya would be able to raise the money to refinance or pay off its maturing $2 billion Eurobond this May.

Fast forward a month, and things have changed DRAMATICALLY. The Kenyan government secured a new US$1.5 billion Eurobond issue. Investors actually bid for over US$5 billion worth. Some of the money not accepted for the Eurobond, reportedly several hundred million dollars, found its way into the concurrent Kenyan-shilling denominated "Infrastructure Bond" the government was issuing.

As a result, confidence was restored and the Kenyan shilling has rallied by more than 20% since. Not surprisingly, the Nairobi bourse has risen strongly as a result, led by bellwether stocks, Equity Bank Group, KCB Group, and Safaricom.

I positioned the fund for exactly this. **March to date, African Lions Fund is up by more than 7.5%.** But that is really a story for NEXT MONTH'S letter.

In February, the Fund already started to recover from a very tough period, during which it had 3 down months in a row. For February, the Fund gained 0.83%. Since inception, the Fund was up 41.89% at the end of February. That number will have risen dramatically by the end of March. But this is not a surprise to me…

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Signs of a bottom in Africa's Frontier markets are everywhere

Those of you who know me well understand that I am wired a bit differently to most. I don't follow the herd. I march to the beat of my own drum. As such, I always pay attention to "contrary indicators."

To me, the first sign of a bottom was when our broker, EFG Hermes, decided to dismiss its entire Africa Frontier research team at the end of January.

Next, at the annual EFG One on One investment conference in Dubai earlier this month, less than a dozen African Frontier companies were present. I had 11 meetings over three days, with ALL of them. This was by far the lowest turnout in the 3 years that I have been physically attending these conferences.

EFG senior executive Ali Khalpey, who used to run EFG's Frontier Equities business, but now runs Equity Capital Markets (ECM), told me the firm was busy preparing and marketing 14 different Saudi IPOs at multiples of up to 25x 2024 earnings. I sighed and wondered to myself why no one was interested in our universe of quality African Frontier companies on P/E multiples as low as 1.2x.

But, on the bright side, with near-zero interest, and an ever-shrinking number of analysts covering our region, the opportunity to get an outsized return on the fundamental research we do should continue to get better.

According to one of the few surviving Frontier market research providers, Tellimer, brokers and investment banks cut frontier markets research coverage by 40% in the last year alone: for every frontier market stock recommendation, there are nine in developed markets and seven in large emerging markets. And this tide shows no sign of turning.

Then, a third significant contrary indicator emerged.

On March 18, index provider, S&P, REMOVED all Nigerian Domiciled companies from its Africa Frontier indices.

Among other things, this saw the S&P Africa Frontier BMI USD (Total Return) Index, to which we compare our performance for performance fee calculation purposes, fall 30% in one day!

S&P cited the problems for investors repatriating money from Nigeria among the reasons for its decision. In actual fact, S&P is about two years behind the curve. Nigeria has now liberalized its foreign exchange market, and the Bank of Nigeria claims to have cleared all the legitimate FX "backlogs" that existed, meaning there is no longer an FX repatriation queue.

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I suspect the "bottom" is now in for Nigerian stocks (in USD terms). S&P may as well have rung the bell to signify it.

S&P Dow Jones Indices
A Division of S&P Global

INDEX ANNOUNCEMENT

S&P Dow Jones Indices' 2023 Country Classification Consultation for Nigeria – Results

NEW YORK, NOVEMBER 22, 2023: S&P Dow Jones Indices ("S&P DJI") today announces the results of the 2023 country classification consultation covering Nigeria.

Following an in-depth assessment, including a review of the consultation feedback received from market participants, S&P DJI will make the following country reclassification.

Country	Previous Classification	Updated Classification
Nigeria	Frontier	Standalone

S&P DJI recognizes that although the Nigerian authorities have taken some measures to address the liquidity issues in the foreign exchange market and the significant delays in capital repatriation, these challenges persist for market participants.

For this reason, S&P DJI will reclassify Nigeria from a Frontier market to a Standalone market, and consequently remove all Nigeria-domiciled constituents from the S&P Frontier BMI and related sub-indices. The S&P Nigeria BMI index will be maintained as a standalone index once the reclassification becomes effective.

As a result of the change in classification, S&P DJI will remove Nigeria-domiciled constituents from the impacted indices at a zero-price, given the distortion between the parallel and official exchange rates for the Naira, and in order to facilitate index replicability.

The list of indices impacted by this change will be published on the S&P DJI's Client Resource Center by end of November.

IMPLEMENTATION TIMING

S&P DJI will implement the previously described change in conjunction with the upcoming March 2024 Frontier Reconstitution which takes effect prior to the market open on **Monday, March 18, 2024**. The changes will first be visible to clients in pro-forma files beginning on **Friday, March 1, 2024**.

For more information about S&P Dow Jones Indices, please visit www.spglobal.com/spdji.

That said, dire economic conditions persist in Nigeria, as the country implements difficult macroeconomic reforms. For example, following last year's removal of longstanding subsidies,

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The National Bureau of Statistics (NBS) has reported a surge in the average retail price of petrol, from N263.76 per litre in February 2023 to N679.36 per litre in February 2024.

Meanwhile, in part due to the **70%-odd devaluation of the official exchange rate**, food inflation is running at 37.9%, making it a challenge for ordinary Nigerians to even feed themselves. This has led to fears of social unrest and insecurity as people get more and more desperate.

But there are some rays of sunshine, too. Nigeria's National Petroleum Company (NNPC), a key state-owned enterprise, is doing much better under the management of the new administration. The company is now profitable and paying taxes. NNPC's transformation from a loss-making entity to a profit-oriented company capable of providing dividends to shareholders and creating value for all Nigerians is hugely significant. There are reportedly plans underway to partly privatize the firm and list it on the NGX, too.

The highlight of my meetings in Dubai was with Nigerian Exchanges Group (NGX)

The NGX has been a listed company for several years now and its CEO, Temi Popoola, was the only Nigerian executive who came and presented his company's investment case at the EFG conference in Dubai. Apparently, the UAE still has strict visa restrictions on Nigerian passport holders, after a diplomatic spat about two years ago, and that partly explains why more Nigerian corporates did not show up.

In any event, my meeting with Temi Popoola was the highlight of the conference for me. It is abundantly clear that he is a man on a mission to drag the company into the 21st century and implement several new growth initiatives. And things are moving ahead constructively.

Along with Uganda, NGX is one of the few African stock markets to have seen new listings in the past year. Two highly successful Nigerian power company IPOs, Geregu Power and Transcorp Power, have helped boost turnover in the past 12 months.

More IPOs are hopefully in the pipeline. Temi is especially keen to get some of the high-flying Nigerian tech "unicorns" to at least consider dual listings at home in Lagos, if they decide to list in the USA or London. He was also keen to point out that President Tinubu's anti-corruption drive dovetails well with a push to partially list state owned enterprises, so as to force greater transparency. Watch this space.

But Dubai was not the only place I had meetings over the past 6 weeks. I also had an extensive round of meetings in Nairobi and Addis Ababa, including with four of the five companies we have been building positions in in Kenya.

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Among our Kenyan investments, I think Jubilee Holdings and KCB Group are the most undervalued

Even with the strong rally in Kenya that began with the currency in mid-February, and has continued throughout March, there is still some excellent value to be found in the Kenyan market.

Bellwether stocks, Safaricom and Equity Group have rallied strongly so far this year, by 38% and 46%, respectively in local currency terms, and even more in US dollar terms. The days when we were accumulating Safaricom for as little as KES 13.50 per share are long gone, with the stock now trading above KES 19.

Attending the Safaricom investor event in Addis Ababa and seeing first-hand the quality of the company's operation there gave me further conviction in my assessment that the Safaricom Ethiopia business is most definitely not worth less than zero, which is what the market was valuing it at until recently. The growth driver is the state-of-the-art-network, and superior data service the company delivers, when compared to its only competitor, Ethiotel.

Ethiopia is a poor country and average revenues per user (ARPUs) are still very low at about $0.85 per month. Safaricom is working hard to get this number closer to the $2 per user, where it will begin making a decent return on investment. From what I observed, CEO of the Ethiopian business, Wim Vanhelleputte, is a highly experienced and inspiring manager, and he is leading an excellent team in Addis Ababa. Execution of the business model is first rate.

I value Safaricom Ethiopia at cost (i.e. what the group has spent on equipment and licenses getting to this point), and in that scenario, Safaricom was never worth only KES 11.50 per share, which was the recent low. The stock has now re-rated considerably. But, for a business of this quality, with the latent growth potential it has, a multiple of 12 to 13 times likely 2024 earnings is not expensive.

Given the rally in its shares, Safaricom is now neck and neck with NMB Tanzania as African Lions Fund's largest holding, at about 14.5% of our portfolio.

KCB Group on the other hand is up 36% year to date. But it had been so heavily sold off, it still trades at only 1.5x our estimate of 2024 earnings, on a price to book value of 0.3x, and with a return on average equity of 24.7%.

Compared to its closest comparable, Equity Bank, **KCB Group is trading at half the market value, half the P/E and half the P/B**. This does not make sense to us, even if Equity's DR Congo growth story has captured some investors' imaginations.

KCB's 2023 results were somewhat disappointing, but this had been discounted in the price and then some. The omission of a dividend for 2023, however was a bit of a surprise to the market. Nonetheless the stock has bounced back strongly in recent days.

KCB management has already signalled that after holding back the 2023 dividend to boost its capital ratio well back above regulatory minimums, the bank will almost certainly be paying interim dividends this year. We estimate a 13.1% dividend yield in 2024.

The other catalyst for KCB's recent rally came when KCB Group management announced they would off-load the troubled NBK subsidiary, which has been giving the bank grief more or less ever since they were strong-armed by the government into acquiring it, and tasked with cleaning up its loan book. Access Bank of Nigeria will pay 1.25 net book value for NBK upon closing, should regulators approve the binding deal which the two banks have already agreed, in the coming months.

KCB will collect nearly US$100 million from this sale and also be rid of a significant portion (about 1/8th) of its total bad loans, including some of the most stubborn ones. About 1/8th of the staff costs of the whole group also sit in NBK, with its long-tenured employees. So, one of the key drivers of our 2024 earnings forecast is a drop in the Group's cost-to-income ratio to 45%, from 50.3% in 2023.

The other stock we own in Kenya that looks far too cheap is Jubilee Holdings, East Africa's largest homegrown insurance firm, and part of the Aga Khan Development Network (AKDN) group of companies. African Lions Fund, represented by Senior Analyst, Muammar Ismaily, Director, Peter Tan, and I had a fruitful meeting with Jubilee's senior management in Nairobi in late February.

We are fortunate to have built strong relationships in Kenya with several investment industry heavyweights, including one who sits on the board of Jubilee's Life Insurance subsidiary. We leveraged this relationship to be able to get corporate access at Jubilee, a firm that is otherwise notoriously difficult to get a meeting with and not very good at communicating with outsiders. We made the point to management that they really need to change this. Thankfully, they were responsive to the idea.

Jubilee is old-fashioned, and conservative, but a leader in its industry. To the board's credit they have made several new key management hires in the last two years. It is our assessment that this is now beginning to truly bear fruit. The company is being dragged into the 21st century and applying modern management practices common in the insurance industry in other parts of the world.

It is still very much a work in progress, and there has been no real reflection of this in the group's share price. It continues to trade at extremely depressed valuations of 0.2 times book value and a P/E of 2.2x. We continue accumulating the stock. But it is difficult to build a large position, as it is tightly held.

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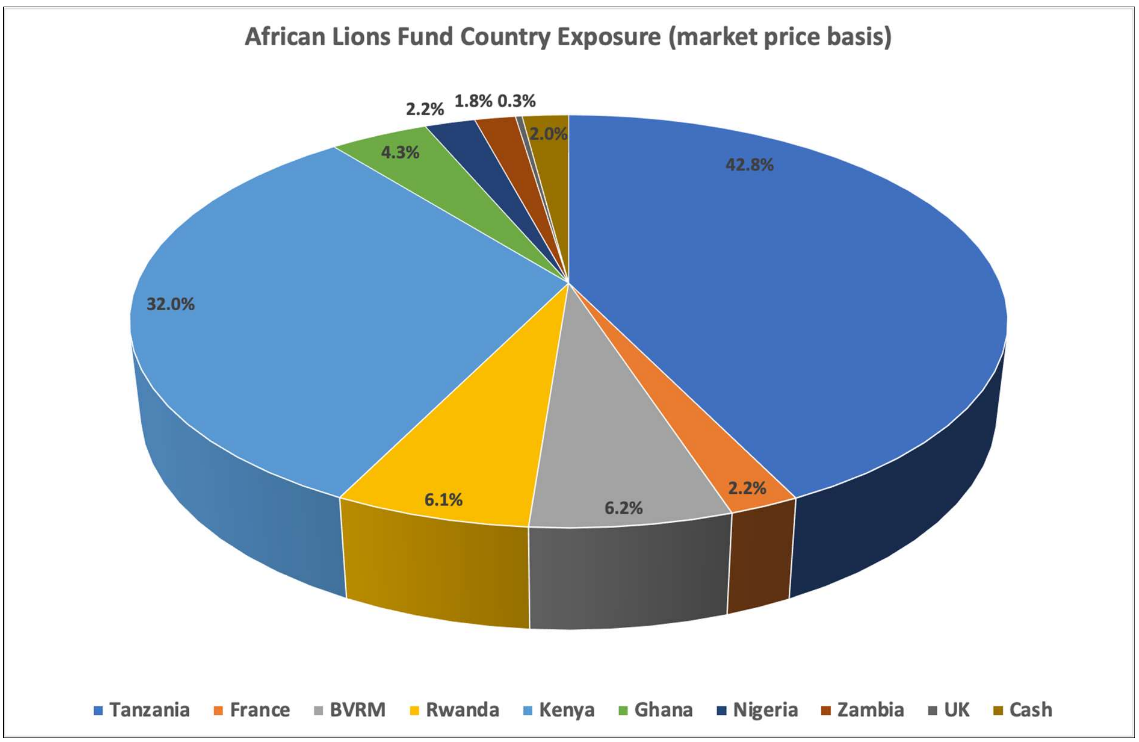
<u>Our portfolio now more evenly spread between Tanzania, and Kenya</u>

Given the strong recent recovery in the value of our Kenyan companies, their total share of the African Lions Fund portfolio has increased significantly. On recent numbers, Tanzania still accounts for 43%, but Kenya is up to 32%.
I expect this to continue. Although with dividend season fast approaching, we are going to be paid some handsome sums in Tanzania between now and June.

After the rally in Kenya, which I positioned the fund for, by buying aggressively there over the past 9 months or so, I believe the next big portfolio allocation shift needs to be towards Nigeria. But that is a story for next time…



*The company listed in France operates in Gabon.

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Housekeeping, and travel schedule

After a busy four or five weeks traveling to three different countries for company visits and conferences, I have been in Dar es Salaam the past 2 1/2 weeks, and I am staying put here for the time being, aside from taking the opportunity to go to the beach with my family over Easter.

My next planned trip is to New York City the week of May 6 for a series of meetings with potential new investors in the Fund. If anyone is in the northeast of the USA and wants to catch up, please reach out. It would be great to meet face to face.

Prior to then, I may visit Zambia again for the Zambia Breweries AGM, but the date has not been finalized yet.

A plan to visit West Africa in the early part of the second half of the year, or even in June, is also in the works. Nigeria, Ghana and Senegal are all on the list.

Quarterly investor call

The call is being held TODAY at 12 noon Dar es Salaam / Nairobi time.

Join Zoom Meeting:
https://us06web.zoom.us/j/86501221425?pwd=5kbbh3EkIvy8asn95VqOsBC78yvjYB.1

If you cannot make it, a recording will be available at the newly revamped African Lions Fund website, which I urge you to check out.

All previous Investor Zoom calls, and letters to investors are archived at website. If you want to refer anyone to the Fund, this is a good place to point them.

As always, your questions and feedback are welcome at tim@africanlionsfund.com

Until next time…

Good investing!

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