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Member of Botswana Stock Exchange

MS ECONOMIC BULLETIN
Q3 2020

Contents

COVID-19 slows economic developments…

The entire globe has been greatly affected by the COVID -19 pandemic with the world's economy projected to decline by -4.5% in 2020 according to the latest report from the OECD. The effects of the lockdowns which were introduced in many countries across the globe had a significant impact on economic growth. Reports of further lockdowns and restrictions in the US and some countries in Europe are expected to further impact the global economy. Reports of a breakthrough in COVID-19 vaccine is a welcome development, although it shall take some time until the global economy can recover to pre-COVID era. Against this background, the global economic outlook remains uncertain and growth prospectus will depend on several factors such as availability of the vaccines to the larger global population, the extent of any new COVID-19 outbreaks as well as the duration and effectiveness of both fiscal and monetary policy interventions by various governments across the globe.

Most countries are projected to record a negative growth in GDP numbers in 2020 with the exception of only China which is the only country in the world projected to show a positive GDP growth. The IMF projects China's economy to grow by a modest +1.8% due to a quicker recovery than expected and a growth in exports.

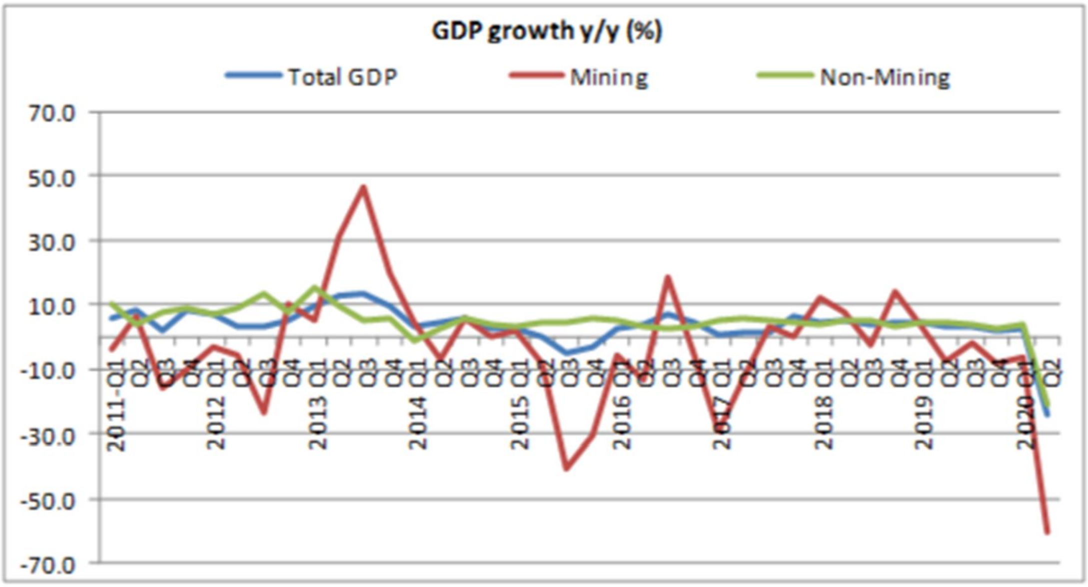
Closer to home, last week we saw South Africa's credit ratings being downgraded deep into the junk territory after Moody's Investors Service joined Fitch Ratings in lowering the country's credit ratings. S&P however, kept its assessment of South Africa's foreign-currency debt three levels below investment grade, with a stable outlook. The cut by Moody's takes South Africa two notches below investment grade status, while Fitch's brings it three levels below. Both also maintained negative outlooks, which means the next move would also likely be down. The downgrade will weaken further South Africa's economy which is still affected by the effects of the COVID-19 pandemic. The downgrade will not only push South Africa's borrowing cost up, but will also impact negatively on the SA fiscal framework. To cover the funding gap, the government might be forced to either cut expenditure through reduction on spending on social programmes or increase tax – a move which is unpopular and will further reduce disposable incomes. A slowdown in SA economy is not good news for Botswana and other members under SACU as this may result in a decline in SACU revenue, possibly further impacting on Botswana fiscal position.

Q2 2020 GDP Declines 24% y/y

GDP in the second quarter of 2020 nosedived y/y, contracting 24% y/y, versus the previous quarter's economic growth of 2.6% y/y, and the same quarters in the previous year's 3.0%. The steep decline in the quarter was resultant of a huge reduction in real value added of Mining & Quarrying and Trade, Hotels & Restaurants industries by 60.2% and 40.3% respectively. These were two hardest hit sectors of the economy in the second quarter, weighed down by containment measures undertaken by the Government of Botswana, which included the suspension of air travel of which impacted the number of tourists coming into the country. The trade and hospitality sector is expected to take the longest time to recover, and has a dependency on the availability of a COVID19 vaccine — which is currently outstanding.

The deterioration of the mining sector was in line with expectations given the unfavourable operating environment. The diamond industry weakened given the reduced global demand for rough diamonds, which was already slowing amidst the US/China trade war. In the second quarter of 2020, diamond production in carats declined 67% in tonnes. Coal production decreased 41% in the same period, underpinned by the temporary closure of Morupule B for remedial works, which had a negative impact on uptake. Confidence in the mining and quarrying sector is expected to swing into recovery in the third quarter of 2020, and lead economic recovery in the 12 months to June 2021.
The non-mining sector declined by 20.7% in the second quarter of 2020; with most of the underlying sectors noting double digit losses. The Trade, Hotels & Restaurants, Construction and Manufacturing led the losses at –40.3%, -36%, and –31.3 respectively versus the growth noted in the same period in 2019's 5.1%, 3% and 3.5%. The General Government industry expanded by 2.1% in real value added compared to 4.2% during the corresponding quarter of 2019. The industry was a major contributor to GDP for the first time in years.

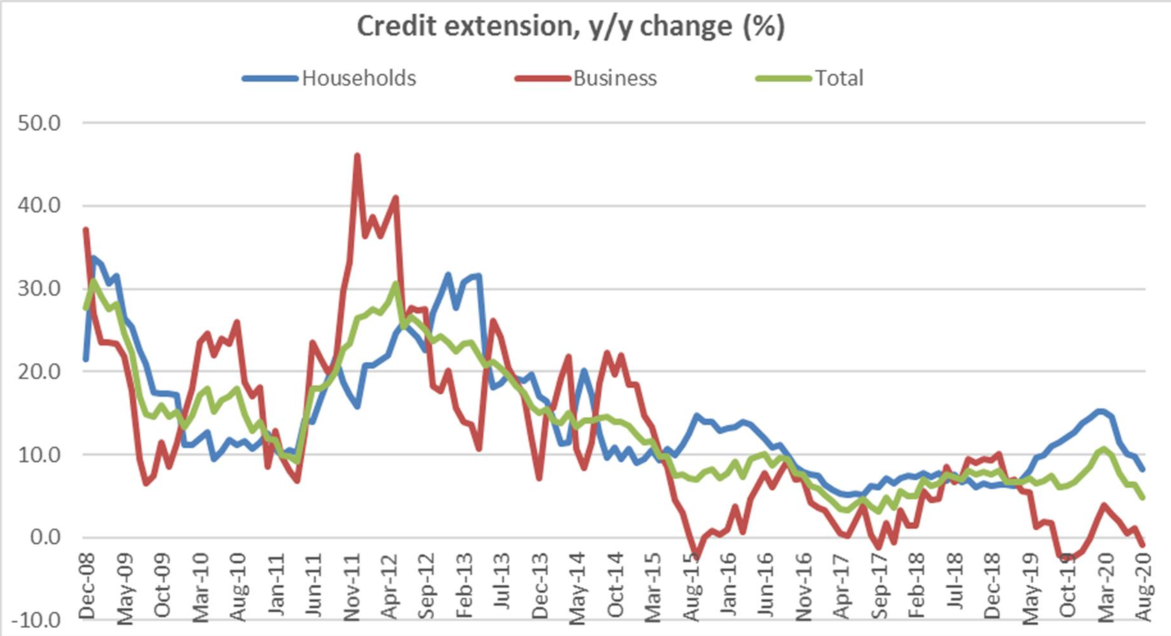
The annual inflation rate at the end of Q3 of 2020 remained well below the target range of 3% - 6%, at 1.8% y/y— up 0.8% y/y/ from the prior month. This increase in headline inflation came as no surprise given the increase in Minibus and Taxi fares as well as long distance bus fare. These changes were effected on 01 September 2020. Annual inflation at this time is expected to remain below the target range, as the economy expected to operate below full capacity in both the short and medium term.



Source: Statistics Botswana

Credit growth extension shrinks y/y

Credit growth by commercial banks in Botswana in the year was significantly hampered by the outbreak of the coronavirus pandemic. The latest statistics published by the Bank of Botswana show that the growth in credit extension in Q2 2020 back-trailed in July 2020 and August 2020. Overall credit growth by Commercial Banks in August 2020 declined to 4.8% y/y, from 7.4% y/y recorded in the same period last year. The decline in credit growth in August 2020 y/y was underpinned by a drop in both the business and household sectors, with the respective changes standing at -0.9% y/y and 8.2% y/y. The low interest rate environment, is however, not having the desired effect of boosting credit growth by, this can chalked down to prudency by lenders. They are weary of the possible deterioration of their loan book, spurred by the uncertainty stemming from the coronavirus pandemic.



Source: Bank of Botswana

The Bank of Botswana's Monetary Policy Committee maintained its accommodative monetary policy stance during its last meeting on the 8th October 2020; wherein the MPC cut the bank rate by 50bps, from 4.25% to 3.75%. This was the second rate cut implemented by the Bank of Botswana, the first having been implemented on the 30th April 2020. The Bank of Botswana has thus far cut the bank rate by 100 bps in 2020. This may well be the last rate cut the MPC implements for the year, as we believe there is now very little room for another downwards adjustment. Supporting this is also improved optimism for domestic market– oriented firms, according to the Business Expectations Survey (BES) published for Q3 2020. Business conditions are expected to improve in Q3 2020 and the next 12 months after that.

The business sector has noted a steady decline in credit extension since the beginning of April 2020, which is understandable, given that this was the beginning of the lockdown period when economic activity came to a near standstill. As such, the decline is not altogether surprising, given that mining was down to a growth of 13% y/y growth in August 2020, from 135.9% in the same period in the prior year.; agriculture declined to –14.8% y/y from 30.3% y/y; and manufacturing reducing to –48.6% from –11.2%.

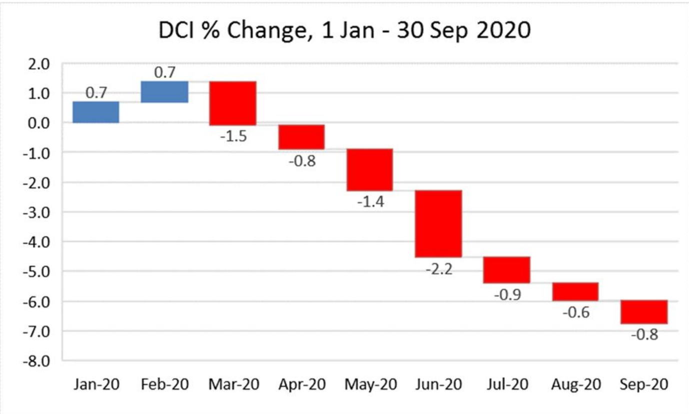
On the other hand, the Trade and Hospitality sector and the Finance sector improved from –16.1% and –23.4% y/y to 10.4% and 21.6% y/y . This is not surprising as the Trade and Hospitality sector likely required the funding to stay afloat. Credit growth for the business sector as at August 2020, stood at -0.9% y/y from 1.7% in the same period last year. Household credit declined to 8.2% y/y in August 2020, from 11.0% from the same period in 2019. This is also owing to the coronavirus pandemic, which has destabilised disposable incomes and slowed down the local economy.

The Domestic Equity Market feels the pinch of the COVID-19 outbreak

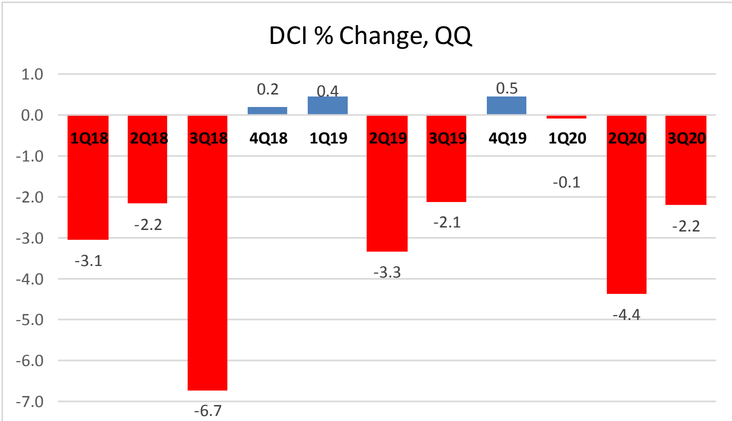
The third quarter of 2020 was plagued by a series of losses on the domestic equity board. Fifteen stocks sunk in value, putting some surmountable pressure on the domestic indexes, which dropped for the second consecutive quarter. The losses were relatively contained by the two stocks which gained during the quarter.

The impact of the COVID-19 pandemic on the market comes out clearly in the cascading DCI m/m changes as seen by the graphs below, led by the value loss in BTCL. This was more a reflection of the stock's shareholding structure, more than the company's performance, which is largely retail-inclined. As has become a notable outcome, the retail environment was hit by a decline in disposable income, resulting in the general slowdown of the local economy.

A number of the domestic companies, including Absa, BTCL, and StanChart, have taken to preserving their cash reserves, by not declaring dividends/distributions. While the move is prudent, and quite understandable, the Total Returns index, i.e. DCTRI, is reaping the outcomes of non-existent declarations. This was the second consecutive q/q loss, although less than the prior at negative 1.1% (Q2 2020: negative 2.0%); comparatively in line with the negative 2.0% in Q3 2019.



Source: Botswana Stock Exchange DMR; Motswedi Securities Calculations



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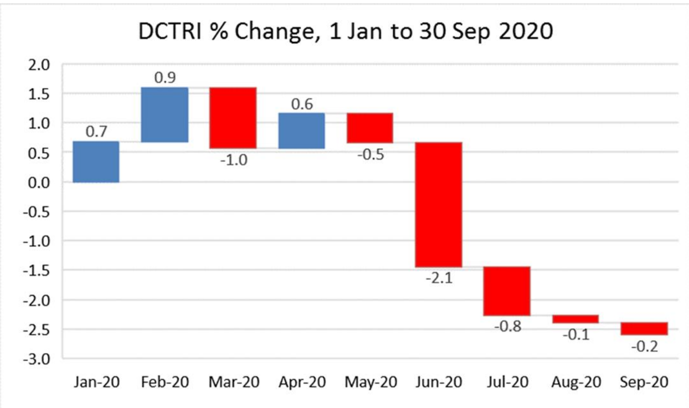

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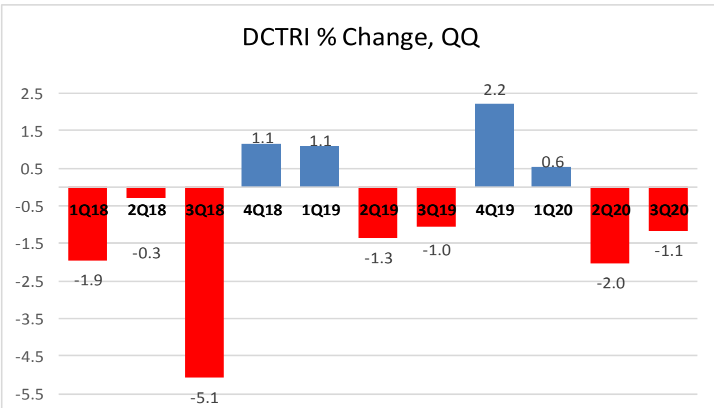
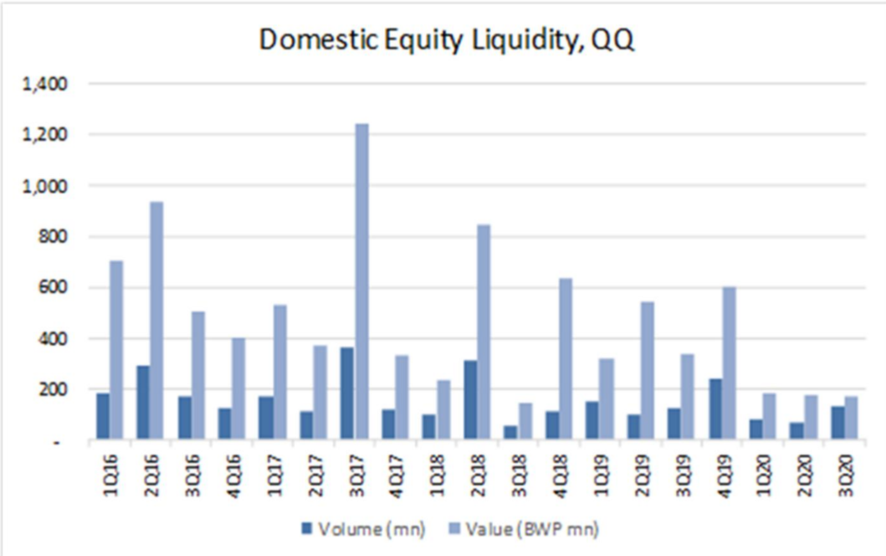


Source: Botswana Stock Exchange DMR; Motswedi Securities Calculations

Liquidity remained fairly depressed in the third quarter of 2020, in line with the previous quarters of the year. Volume and value traded in Q3 2020 was at 136mn and P173mn. Volumes increased by almost double from the previous quarter, but given that value was more or less unchanged, it indicates a somewhat undervalued market.

The low liquidity in the market was under-toned by the near disappearance of equity demand from investors. Sentiment also shows an inclined preference for the safer investments on the BSE as shown by increased activity in NewGold Exchange Traded Fund (which tracks the performance of gold) as well as government bonds. Government bonds are usually considered a safe bet given that the investment is essentially backed by the State.

It is evident that the year 2020 has been a bit of a challenge in as far as liquidity and capital appreciation is concerned, and we expect this trend to continue, at least until the year ends. These levels of illiquidity are at all their lowest in over 10 years.



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BSE Equity Market: Company Highlights

Banking

Most of the banking stocks made losses in the quarter, pressured by the low interest rate environment (bank rate now at 3.75%), impacting on margins coupled with a decline in transaction volumes. As the economic environment does not seem to be responding to the accommodative monetary policy, we expect the bank rate to remain at these low levels at least for the short to medium term. Key to survival in the market includes finding innovative platforms to tap in to support revenue. With this in mind, we largely expect to see the introduction of new products and corporate deals to support the low interest rate environment.

FNBB switched from being the best gainer in Q3 2019 to one of the biggest loser in Q3 2020, with a year to date loss of negative 17.9%. The bank's financial performance was fairly stable for full year 2020, with PBT at P695.8mn (2019: P732.5mn) despite an increased impairment ratio (of which was revised to provide for the uncertainty of COVID-19). Loans and advances to customers declined 8% in the year to P14.7bn, while deposits from customers increased 18% to P23.2bn. This ominous performance reflected somewhat in the stock's performance, which declined a slight 2.5% in the third quarter, closing at P2.34/share.

Absa's interim financial results for the period ended 30 June 2020 highlighted a modest 4% increase in net interest income on the back of a growth in the loan book. Net fee and commission income, was down 4% due to overall reduced activity and a decline in margins. Total income for the period was down marginally at P803.9mn for the period, from the prior comparative period's P809.7mn. Impairments increased to P178.5mn due to bank restructuring about P1bn of their loan book as a result COVID-19's impact. Impairments are now 1.3% of the overall loan book, and are expected to increase for the full year. Profit after tax for the period was down 70% to P9.7mn (2019: P298.8mn). Loans and advances to customers grew 7% year-on-year while customer deposits grew 8% -- both driven by the retail and business banking portfolio growth. Prudency was at the forefront of thinking, as they withheld dividends for the period. The company share price was unchanged qq, at P5.45/share, but still dragged with a ytd loss of negative 0.9%.

Banc ABC's unaudited interim financial results noted an increase of 19% in net interest income to P229mn from the prior comparative period. Interest income increased by 3% while interest expense shrank 15%. Primary to the improved interest income is improved traffic through the Bank's technological advances, including the use of the Banks online platform. Impairment provisions for the period increased to P2mn, from the previous comparative period's impairment release of P4.8mn. The impairment rise being on the back of deterioration of the Bank's SME lending book. Net trading income improved 278% to P8.8mn. This is encouraging, as it signifies an element of recovery for the segment, from the previously reported figures in the last comparative figure (2019: H1 P2.3mn). Net fee and commission income on the other hand dropped by 33% to P33.1mn, from P49.5mn, as a result of an overall reduction in transaction volumes and discount measures, according to the management of the Bank. This led to an improved PBT of P72.9mn (2019: P66.3mn). The loan book increased 3.6% y/y to P6.2mn, likely as a result of the current accommodative monetary policy which saw the bank rate decline 50bps to 4.25% in April 2020. The stock's price remained unchanged at P2.00/share, stuck at its 2018 IPO price, which is quite in line with expectations given the illiquidity of the stock.

Financial Services

BIHL's first half financial results were relatively flat, boosted by a significant increase in the share of profits from associates and joint ventures, although the other business lines also saw a marginal increase in H1 2020, compared to the H1 2019. The stock's trading levels were on the low end for the quarter, while the price was stuck at P17.50/share.

Letshego's share price performance was on the back end for yet another quarter, down 5.7% from the previous quarter. This came as a result of sombre financial numbers for the half year. As a microlender, the operating environment is similar to that of a bank, with risk being slightly higher, although the salary deduction code and exposure to government employees gives Letshego some comfort. Again the second leg of the Botswana civil servants salary increments maybe be positive for the group. The stock was the picture of liquidity in the quarter, trading well over P62mn.

Telecommunications

BTCL is experiencing a shortage in demand for the stock, which has decidedly put some selling pressure on the shares. The share price continued to cascade lower and breach historic lows. Liquidity for the stock continues to shrink q/q as 0.92mn shares worth P0.78mn traded during Q3 2020 from 1.73mn shares worth P1.50mn in Q2 2020. The demand/supply dynamics for the stock remain unbalanced, with the supply pulling heavier.

Tourism

Chobe lost ground in the first two months of the third quarter, losing in overall 9.5% - a fairly highly q/q loss when compared to the 8.7% noted in Q2 2020. Sentiment for the stock is generally on the low end during this era of COVID-19, as cases globally continue to increase, and cross border restrictions remain intact. The tourism and hospitality sector, together with all the other sectors that feed from it, were some of the hardest hit in Botswana's economy during the COVID-19 pandemic and will probably take quite some time to recover.

Cresta lost ground as well in the third quarter, understandably so, as the stock entered the negative territory in terms of price movements with a loss thus far of negative 2.2%. The company's half year financial results showed a reflection of the impact of the COVID19 outbreak in the tourism and hospitality sector. The Group's revenue declined 50% in the period to P93mn, compared to the previous comparative period's revenue figure of P188mn. Majority of the revenue figure was likely garnered in the Q1 2020 as the Group's hotels in Botswana were closed for normal operations from 1 April 2020 to 4 June 2020.

Retail & Wholesale

Choppies, lost 13% in value in the first two weeks after the trading suspension was lifted on the BSE, and stayed to the end of the third quarter. Choppies' 20 month trading suspension was lifted by the Botswana Stock Exchange (BSE) with effect from the 27th of July 2020. This is after the retail giant finally released its long awaited audited financial results on the 24th July 2020. The JSE suspension, on the other hand, was lifted much later in November 2020.

Sefalana was the only stock that has gained throughout all three quarters of the year, with the gains in the third quarter marginally improving the stocks year to date performance to +3.7%. Sefalana was the second most actively traded stock in the third quarter, driven by a host of profit taking exercise from its investors, more especially since they received their dividends in the last week of August 2020.

Sechaba's performance for the half year period was severely impacted by the containment measures implemented by the Botswana Government, which included the restrictions and/or regulations on the sale of alcoholic beverages, as well as movement restrictions. The holding company, as such, did not declare an interim dividend for the half year period. The stock had lost 2.3% of its value by the end of Q3 2020. Sechaba is a holding company that owns 49.9% in two associates, namely Kgalagadi Breweries (KBL) and Coca Cola Beverages Botswana (CCBB). As such their performance relates directly from both companies. Share of results from associates for the half year ended 30 June 2020 were slashed by 58% to P40.2mn, as compared to the previous comparative period, 30 June 2019 (P96.6mn). This came about as a result of declined volumes from both associates. KBL's volumes declined 40%, impacted directly by the Government ban on the sale of alcohol; while CCBB's volumes dropped a much smaller 7.1% - with sharp declines experienced in the second quarter of the year.

Property Sector

Letlole is one of the handful of stocks that retain a year to date that's positive for the year 2020, despite a retraction of 1.7% in the third quarter under review. The Company's financials were by and large supported by the disposal of the hotels to Cresta back in June 2019, as can be noted by a 17% increase in profit after tax. The company's name also made a number of appearances in the local headlines. According to the local newspapers and a number of company announcements, there is ongoing spat between the former Chief Executive Officer (whose contract was terminated in the Q3 2020) and the Company's Board of Directors relating to the Company's Long-term Incentive Plan. Nonetheless, the matter was referred to law enforcement agencies for criminal investigations.

NAP's performance for the financial year 2020 proved the company's resilience in the environment. Although, it could be said that better part of the company's performance came from the first nine months of the year, which happen to have been before the coronavirus became a pandemic. The stock was the most traded in the property sector in the quarter, clocking a marginal share value loss of negative 0.9%. A lot of the stock's appeal stems from the near zero gearing position and generally stable distribution yield (as at 30 Sept. 2020: 7.4%).

Primetime's share price was down 4.5% for the quarter, to become the highest loser in the sector after Turnstar. The Groups half year performance was impressive, and the full year numbers are likely to be severely hampered by its second half performance. Primetime's gearing is relatively high at about 50%, which may likely increase, given the uncertainty of the business environment, among others, rent deferrals. On a year to date basis, the stock is carrying a slightly higher loss of negative 4.8%

Energy

Engen published their interim financial results for the half year ended 30 June 2020. The company noted a 15% decline in revenue for the period to P1.15bn (2019: P1.35bn), due to movement restrictions in Botswana, as well as decline in global crude oil prices. In the period, the Group disclosed that the oil industry received a margin increase from the Government. The slate payable to Government was P172.6mn as at 30 June 2020, versus the under recovery position of PP29.4mn as at 31 December 2019. Cost of sales were contained in the period, declining by 11%; gross profit declined 47% to P77.2bn (2019: P145.8bn), with the GP margin down to 6.7%. Expenses were marginally contained as well, resulting in an operating profit of P33.2bn (2019: P89bn). PBT at P29.7mn (2019: P87.2), EPS down to 10 thebe (2019: 38.3 thebe), and a net dividend yield of 10%. Engen declared an interim gross dividend of 18 thebe per share for the period, which will become payable to shareholders registered in the company's books on the 16th October 2020.

Minergy saw demand for coal plunge, which forced the Group's production levels to decline as well, more especially as coal prices remain supressed. The financial impact of having to cover fixed overhead costs, has eaten away at the little funds the Group managed to raise earlier in the year, which unfortunately arm twists them into seeking additional capital. Despite all the above, in the quarter, the stock only lost 2.4% of its value in the quarter, declining to P0.83/share.

Agrobusiness

SeedCo published stellar financial results for the year ended 31 March 2020. As it seems, SeedCo experienced a surge in sales in the second half of the year, as would be expected. The Group's revenue climbed 19%, propped up by an increase in maize-seed sales volumes that improved due to maize commodity prices. This, further supported by improved rainfall in a number of regions the company operates. However, the improvement was capped by an unfavourable currency translation of the Zambian Kwacha to the reporting currency. The GP margin was relatively unchanged, hovering at around 48.9%; while the PE stood at 7.7x, and the EPS increased to 2.86 thebe from 1.75 thebe. Finance costs increased by a large margin of about 58% - the Group citing delayed settlement of receivables from major Government customers as the cause. As such, the Group relied on their bank's facilities that added to the increased debt to operational income ratio to 3.27x. The Group expects the full impact of the COVID-19 pandemic to reflect in its current ongoing financial year, given the restrictions of movement in various countries of operation. The stock spent the entire quarter with its fungibility between the BSE and the ZSE suspended by the Ministry of Finance and Economic Development (MFED) of the Republic of Zimbabwe. As a solution, the MFED established a subsidiary, the Victoria Falls Stock Exchange Limited ("VFEX") where dual-listed companies including Seed Co International Limited, would be allowed to list their shares for trading in United States Dollars. This was established in the first week of November 2020. Nonetheless, the stock's price was not spared in the quarter and lost 4.6%, arguably lower than would have been expected, given the lesser liquidity.

Research

Garry Juma

Salome Makgatlhe

Sales

Tshepo Setlhare

Refilwe Lesolle

Keyshia Tebogo

Plot 113, Unit 30, Kgale Mews Gaborone

P/Bag 00223, Gaborone, Botswana

Phone: +267 318 8627

Fax: +267 318 8629

Website: www@motswedi.co.bw

Email: motswedi@motswedi.co.bw

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