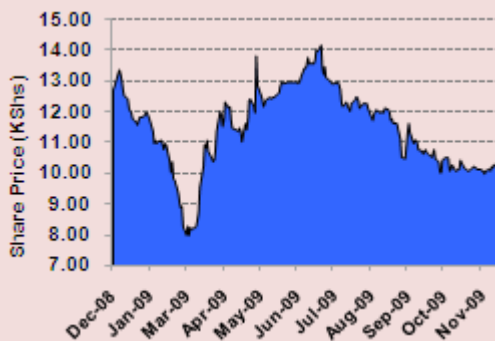


## Selected Financial Ratios

Year End (Dec.)	07A	08A	09E	10E
Gross Premium (mn)	3,222	3,428	3,986	4,368
Net Premium (mn)	2,975	3,109	3,634	3,999
EBITDA (mn)	1,044	1,739	1,730	1,960
Net Profit (mn)	838	1,481	1,606	2,339
EPS	1.40	2.47	2.68	3.29
Premium Growth	3.5	6.4	16.3	9.6
EBITDA Growth	28.4	66.5	(0.5)	13.3
EBITDA Margin	31.3	50.5	43.2	44.9
Return on Equity	12.4	19.4	17.5	-
Solvency Margin	243.0	257.0	252.6	-
EV/EBITDA	9.0x	3.8x	3.8x	3.4x
Mkt. Cap./Premium	3.2x	2.2x	1.6x	3.2x
PE Ratio	12.1x	5.2x	3.9x	3.2x

Source: Company data, FIB Research estimates



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## General Disclaimer:

The information contained herein is obtained from sources, which to the best of our knowledge are 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.

## Kenya Reinsurance Corporation Limited

Finance and Investment Sector | NSE | Reinsurance | Medium Cap  
(pricing in this report is based on 18<sup>th</sup> November, 2009 closing prices)

### Spirited growth in premium as the combined ratio contracts

Kenya Re's net profits rose 50% in the nine months ended September 2009 to Kshs1,058 mn from Kshs702 mn in the same period in 2008

The combined ratio declined significantly during the nine months as premium income growth offset the increase in combined costs and losses

Kenya Re's large investment portfolio valued at over Kshs10.3 bn is still being restructured with a view of prioritizing more liquid investments

Investment income from the portfolio grew marginally in 2008 mostly on account of equity market crashes, however, high returns from real estate investments cushioned the overall fall in investment income

Kenya Re was re-rated by A.M. Best in October 2009, who affirmed a financial strength rating of B+ (Stable) & an issuer credit rating of "bbb-" Red flags mentioned by rating agency include declining underwriting profitability, risky investment allocation and a weak ERM model

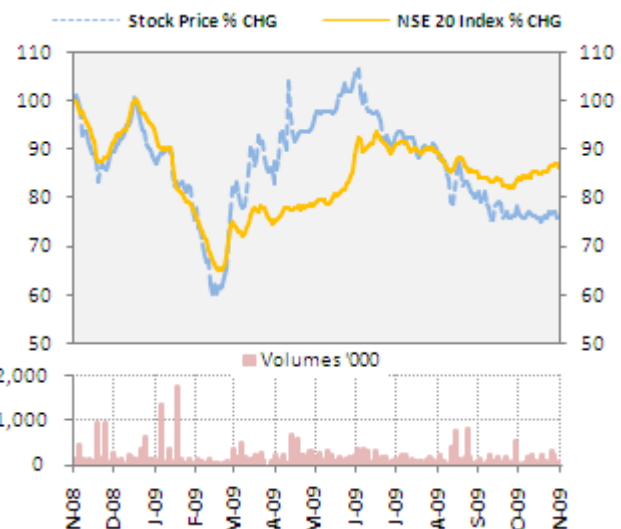
The long term strategies for Kenya Re include building capacity in key West African countries, improving its credit rating to 'A' as well as establishing public private partnerships to develop idle land

As a result of retaining more reserves Kenya Re has been able to expand its underwriting capacity particularly for life business

We project an EPS of Kshs 2.68 in 2009 and we believe the share price is significantly discounted at current prices for long term buyers

## Stock Data

Price	10.10
52 week range	20.75-9.15
Market Cap.	KSh6.1 bn
Market Cap.	US\$81 mn
Solvency Margin	257%
Free Float	40%
Issued Shares	600 mn
EPS (09E)	2.68
P/E (09E)	3.9x
EV/EBITDA (09E)	3.8x
Div Yield (09E)	5.9%



## Exhibit 1: Forecast and valuation

Year End (December)	Gross Premium (Kshs mn)	EBITDA (Kshs mn)	Pre-Tax Profit (Kshs mn)	EPS (Kshs)	EV/EBITDA (x)	Price to Sales (x)
2005	2,613	999	962	4.99	-	-
2006	3,114	813	796	3.59	-	-
2007	3,222	1,044	1,074	1.40	9.0x	3.2x
2008	3,428	1,739	1,759	2.47	3.8x	2.2x
2009E	3,986	1,730	1,932	2.68	3.8x	1.6x
2010E	4,368	1,960	2,335	3.29	3.4x	1.4x

Source: Company data, FIB Research estimates

### ***Brief valuation summary: Encouraging earnings growth but prudent dividend policy***

The listed insurance stocks still remain fairly undervalued based on the common valuation multiples and may be attributed to the fact that core business growth largely tracks the performance of the overall economy. We expect the company to accomplish its long term strategies such as expansion into the new markets in West, North and Central Africa and management's renewed focus on prudent real estate management should yield tangible investment returns in short term. The company will realize only limited success in improving its rating as international standards employed by rating agencies require high advanced risk management (currently unavailable to most developing economies). We anticipate a continued conservative dividend policy in '09 to facilitate high solvency margins and enlarge underwriting capacity. We recommend a buy and using our weighted valuation basket we set our price target to Kshs 21.00 for the next 24 months. This price moves the projected P/E and PBV to 7.8x and 1.5x in line with Jubilee Holdings' multiples today.

### ***Local insurance industry remains crowded while focus moves to building capacity***

Kenya Reinsurance Corporation was incorporated in 1970 and commenced underwriting in 1971. The Government of Kenya divested 40% of its shareholding in the company through an IPO in 2007 in an effort to enhance corporate governance. Following renewed economic growth in 2004 the insurance industry has recorded improved profitability and growth; however, since the start of 2008 the economic and political uncertainties have dampened growth prospects. Since 2004 Kenya's real GDP growth averaged 5.2% per annum and estimated growth in 2009 ranges between 2-3% (driven by the construction and hospitality sectors).

The insurance industry has about 42 licensed insurance companies (of which 20 write general insurance business only, 7 are life only and 15 are composite insurers). About two-thirds of industry gross premiums are short term where premium growth has averaged 13.7% since 2004 against 16.6% for long term business. The top 10 players in the general insurance space collect about 59% of premiums; however, this is different in the life and deposit administration businesses where top 10 players control about 89% and 90% respectively of business. Kenya Re is one of two locally registered reinsurers and operates in a highly competitive market that includes three other international reinsurers.

***Industry Hurdles and Performance***

In Kenya the insurance penetration is estimated at 2.63% (0.87% for life & 1.76% for non-life). The public's view of insurance is still fairly poor and penetration among Sub-Saharan countries remains low as the bulk of the working population operates in the informal sector. These people are usually uneducated, earn irregular incomes and don't have access to traditional financial services. Improving public perception through effective education programs has been suggested by industry experts to raise awareness by softening cultural impediments to insurance concepts.

Insurers have been called upon to embrace innovative methods of working around the high poverty levels in the country by advancing tailor-made solutions that boost the uptake of micro-insurance. Recent suggestions from the Association of Kenyan Insurers (AKI) regarding the provision of life, fire and theft insurance target micro-enterprises traders and small-scale rural farmers. The association is looking to piggy-back off the impressive technological advancements witnessed in the mobile phone market space. The recent success of the Kenyan microfinance model and telecom-run money transfer services gives the industry hope that most low-income members of society can enhance penetration level countrywide.

The industry has been criticized for accommodating too many insurers and regulation has been introduced over the years to improve capitalization in order to strengthen solvency margins. The industry is expecting major restructuring efforts to continue in 2010 as small insurers are merged or are acquired to enable them to conform to the changing regulatory environment. There may be lack of enthusiasm from investors to contribute more capital in light of the decline in returns in 2008.

The challenging insurance environment was reflected in the industry figures with premium income declining as a result of declined economic activity, discouraging economic forecasts and mounting losses owing to the election chaos witnessed in the country in 2008. Players across the board ceded more premiums and investment income took heavy damage from the downed equity markets. However, despite the harsh business conditions underwriting profits improved as costs were contained.

**Exhibit 2: Industry Combined Profit & Loss Statement and Balance Sheet**

**Combined Industry Profit and Loss Statement**

Shs billions	2006	2007	2008	% CHG
Gross Earned Premium	36.14	42.58	42.01	-1.3%
Reinsurance ceded	8.74	9.48	11.35	19.7%
Net Earned Premium	27.40	33.10	30.66	-7.4%
Investment & Other Income	14.42	12.19	8.49	-30.4%
Net Income	41.82	45.29	39.15	-13.6%
Net Incurred Claims	21.20	24.70	22.75	-7.9%
Commissions & Expenses	14.77	16.58	14.76	-11.0%
Profit Before Taxation	5.85	4.01	1.64	-59.1%
Provision for Taxation	0.87	0.99	1.08	9.1%
Profit After Taxation	4.97	3.02	0.56	-81.5%

Source: AKI Statistics 2008

**Combined Industry Balance Sheet**

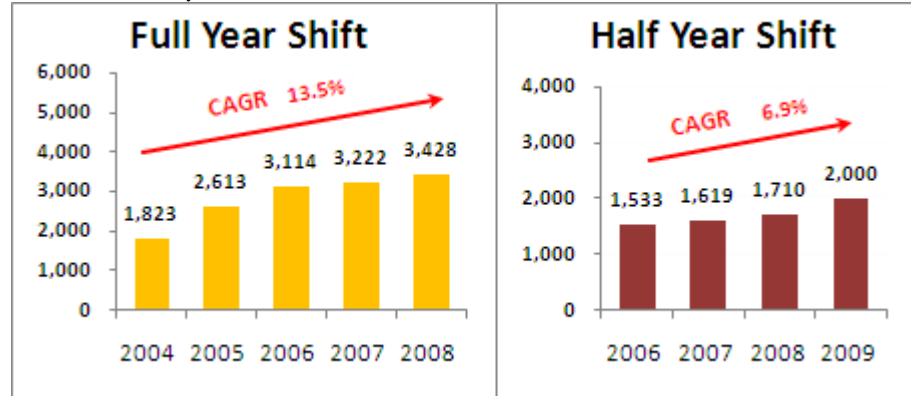
Shs billions	2006	2007	2008
Shareholders Capital			
Life Fund & Reserves	27.40	30.42	29.62
Total Assets	110.07	127.96	146.12
Total Liabilities	82.67	97.54	116.37
<b>Other Ratios</b>			
Return on Capital Employed	20.6%	10.4%	1.9%
Solvency Margin	100.0%	91.9%	96.6%
Retention Rate	75.8%	77.7%	73.0%
Loss Ratio	77.4%	74.6%	74.2%
Commission & Exp. Ratio	53.9%	50.1%	48.1%

Source: AKI Statistics 2008

**Industry growth**

Business within the local insurance sector is very volatile and large portion of the nature of business written by Kenya Re is on the short tail end (i.e., where the ratio of general to life business written was 83:17 in 2008). Global catastrophe losses from natural and man-made disasters were particularly high in 2008 and so the retention rate for the industry dipped considerably as insurers hedged potential losses. The persistence of these kinds of losses will continue to test local reinsurance capacity in '09 and challenge Kenya Re's exposure as a price-taker (i.e, rigid pricing capability).

**Exhibit 3: Kenya Re - Gross Premium Growth Trends**



Source: Company Published Statements

Kenya Re's registered a 17% growth in half year premiums from Kshs 1.7 bn to Kshs 2.0 bn for the period ended June 2009. Historic premium growth rates are not closely aligned to the Kenyan insurance market where gross industry premiums have risen by 15% during the 2006-08 periods against Kenya Re's 10% gain. Trends have seen growth in long term business being the influential driver in moving industry gross premiums and contributions from this line adds more equilibrium (less risk exposure) as it accounts for 33% of premiums (against Kenya's Re's 16.5%).

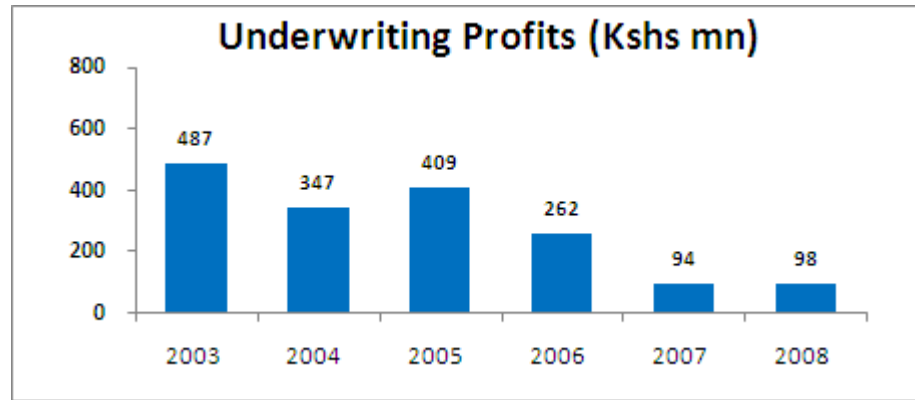
In Kenya Re's life division the ratio of the capital base to net premium rose in 2008 from 21% to 111% and we believe that these reserves are adequate to enable the corporation to comfortably grow its life premiums without setting off any flags with rating agencies. The regulation on insurance capital requirements stipulates that the company needs a minimum of Kshs500 mn (\$6.7 mn) in capital. Kenya Re is currently capitalized at Kshs1.5 bn (\$20 mn) and holds adequate excess reserves to expand its underwriting capacity throughout Kenya and beyond.

The company's gross premium growth in 2008 grew marginally at 6% largely attributed to the reduced contributions from life business and was outperformed by the broader industry that registered a 14% growth rate. Industry underwriting results recorded rapid growth of 120% as profits rose from Kshs365 m to Kshs805 m despite a weighty loss of Kshs1.2 bn from the private motor insurance class (that represents 16.5% of industry business). Non-life industry premiums registered slow growth in line with the growth in the economy, but, through careful cost containment it to post a 4% marginal growth in underwriting profits to Kshs 98 mn.

*Life business will be the key value driver in 2010*

*The loss ratio for the private motor insurance class rose 8% to 83.5% in 2008*

Exhibit 4: Kenya Re - Underwriting Performance



*The ratio of underwriting profits to net premiums earned remain unchanged in 2008 at 3.1%*

**Moderate risk from loss of lucrative treaty business**

Kenya Re currently sources 70% of its business from the Kenyan market and enjoys mandatory cessions in the form of 18% compulsory ceding of all treaty insurance business from all domestic insurance companies. The mandatory treaty agreements have contributed to about 12.2% of treaty business since 2004, thus, a majority of the business is negotiated. The company has made a big effort to develop marketing strategies that will enable it to survive without the mandatory cessions. These initiatives focus on raising market penetration, emphasizing on personal selling, improve customer service, and pursuing a competition oriented pricing strategy.

Optional treaty agreements form the bulk of the agreements written and the mentioned strategies can support long term business growth. The mandatory treaties cover a number of regional insurers as well such as Zep Re and Africa Re and for this reason any change in treaty agreements will have to provide a level playing field for all involved. Despite government’s majority holding, competition from international players (such as Swiss Re and Africa Re) and the unexploited premium classes (like marine and aviation), there is still a high probability that the mandatory cessions will be phased out by 2011. It is safer to bet on a comprehensive industry reform that assumes the complete elimination of compulsory cessions.

*The IRA and other industry stakeholders will have to access the threat from regional players that enjoy their own share of compulsory treaty cessions in other African markets*

Exhibit 5: Kenya Re - Gross Premium Growth Trends

Shs billions	General Business		Life Business		Total	
	2007	2008	2007	2008	2007	2008
Gross Premium	2,822.4	2,890.3	580.9	571.3	3,222.3	3,427.8
Reinsurance	205.1	188.4	42.6	130.3	247.8	318.7
Net Premium	2,436.2	2,668.1	538.3	441.0	2,974.5	3,109.1
Claims Incurred	1,147.8	1,336.2	317.6	229.4	1,465.4	1,407.9
Commissions	801.1	846.1	132.5	149.3	943.8	1,009.5
Other Expenses	468.3	397.1	29.8	-68.3	794.1	663.1
<b>Retention Rate</b>	<b>86.3%</b>	<b>92.3%</b>	<b>92.7%</b>	<b>77.2%</b>	<b>92.3%</b>	<b>90.7%</b>
<b>Loss Ratio</b>	<b>47.1%</b>	<b>50.1%</b>	<b>59.0%</b>	<b>52.0%</b>	<b>49.3%</b>	<b>45.3%</b>
<b>Commissions Ratio</b>	<b>32.9%</b>	<b>31.7%</b>	<b>24.6%</b>	<b>33.8%</b>	<b>31.7%</b>	<b>32.5%</b>
<b>Expense Ratio</b>	<b>19.2%</b>	<b>14.9%</b>	<b>5.5%</b>	<b>-15.5%</b>	<b>26.7%</b>	<b>21.3%</b>

\* Life and Non-Life A/Cs does not include changes in the unearned premium reserve

Source: Company Data

Kenya Re's positive underwriting performance was strengthened by a better combined ratio that dropped from 107% to 98%. The company's loss ratio reflected the industry trend where AKI statistics indicate that major premium classes recorded declines in their loss ratios apart from the private motor insurance class. Following the restructuring in 2007 the expense ratio dipped by over 5%.

The retention rate for the industry dipped from 77% to 73% at a time when economic growth weakened, growing by 1.6%. The company's retention rate declined marginally from 92% in '07 to 90% in '08 likely due the increased purchase of reinsurance to cover their risk exposure to post poll losses. The rate drop would also enable the company to reduce its net liability on individual risks as well as enable it to take on additional underwriting capacity.

The industry has about 141 licensed insurance brokers who are estimated to place over 65-70% of total premiums in the market. The company's commission ratio has continued to rise marginally from 28.9% in 2006 to 32.5% in 2008 as it makes use of brokerage coverage. The first half of 2009 saw the commission ratio decline from 31.6% in 2008 to 28.9% largely on account of higher premiums.

### Product Analysis

#### Exhibit 6: Kenya Re - Gross Premium Growth Trends

Kenya Re - Premium by Class (%)

Insurance Classes	GEP		NEP		Retention	
	2007	2008	2007	2008	2007	2008
Fire	35.8	36.9	33.4	35.3	81.7	85.9
Theft	11.7	9.5	11.8	11.2	88.3	105.7
Engineering	5.3	9.3	6.2	8.4	103.9	81.5
Marine	8.0	7.7	7.5	7.9	82.0	92.5
Motor	7.7	6.1	8.0	7.4	90.6	110.2
Personal Accident	4.5	3.8	4.2	4.5	82.1	105.6
Life	17.1	16.5	18.1	14.2	92.7	77.2
Others	9.9	10.3	10.6	11.1	93.3	96.9

\* Life and Non-Life A/Cs does not include changes in the unearned premium reserve

Source: Company Data

There is an extremely high concentration of premium business in motor and personal accident that account for 61% of gross industry premiums and the classes register high loss ratios ranging from 50-80%. Kenya Re's premium exposure has largely been concentrated on fire class and life business that account for 53% of premiums earned. The higher retention rates for classes such as theft, motor and personal accident arise as we take into account the changes in the unearned premium balances.

*From 1<sup>st</sup> of January 2009 all reinsurance treaties relating to life business were domesticated*

Despite the high prevalence of fires most people prefer to take chances and not protect their properties against fire. However, as GDP levels raise we expect this trend to reverse. Fire insurance growth has helped Kenya Re grow premiums over the last few years but has generated underwriting losses consistently due to high loss ratios. The level of unemployment and low disposable income levels have limited the growth of the life business and only recently has the company increased its underwriting capacity by retaining more reserves. Kenya Re has deliberately avoided expanding other classes such as aviation and marine where they perceive risks to be too high despite the influx of international players stealing market share.

### Combined ratio sending positive signals

In developed markets investors stick to those they consider safe and a key measure of safety is reflected in the combined ratio (that includes expenses and claims). Over the last few years Kenya Re has incurred high loss ratios; but, restructuring efforts in 2007 with regard to management expenses have borne fruit in 2008. By the ratio lowering to below 100% Kenya Re is sending a strong signal saying that is capable of disciplined underwriting while remaining flexible in mitigating risks.

### Exhibit 7: Kenya Re – Trends in Loss and Underwriting Expenses

as % of net premiums	2003	2004	2005	2006	2007	2008	Sep-09
Net Claims	31%	45%	44%	55%	49%	45%	37%
Management Expenses	13%	26%	14%	16%	27%	21%	16%
Commissions	31%	30%	33%	29%	31%	32%	28%
<b>Total</b>	<b>75%</b>	<b>101%</b>	<b>91%</b>	<b>100%</b>	<b>107%</b>	<b>99%</b>	<b>82%</b>

*Source: Company Data, FIB Research estimates*

In the nine months to September 2009 the combined ratio has dipped considerably from the 2008 largely offset by a 27% rise in net premium income to Kshs 2.5 billion. During the nine months ended September 2009 net claims incurred, net commissions paid and underwriting expenses rose 9%, 11% and 8% respectively; however, the combined ratio declined significantly by 13% from the '08 figure of 95% to 82%. The higher net premiums were also supported by an increase in the retention ratio (net premiums to gross premiums) from 87.4% to 91.8%.

### Kenya Re embraces technology

The management embarked on an ambitious program to enhance the sophistication of the insurers risk management, which has been a key criticism from rating agencies. Among the initiatives include investment and installation of a financial system to handle portfolio risk, a life system for their long term business and a document management system. The financial system was expected to yield benefits in the 2009 financial years, however, the remaining new systems are long term projects that would require substantial training and thus the full benefits will be extracted in future years. The initiatives will enhance internal efficiencies and boost customer service provision. The projects may sway rating agency opinions as to the sophistication of risk models; however, the impact on the credit rating is likely to be minimal as the standards used by the rating analysts generally do not favour African markets where complex IT-based risk models are hard to employ.

### **Bankassurance**

This insurance model can be described as a merger of insurance and banking services with a view of using a bank's existing sales and branch network to sell insurance products. The potential for this model to accelerate insurance penetration is high given that some banks are already showing signs that they are ready to exploit the potential synergies for interrelated financial services.

### **Benefits to industry players**

For banks venturing into the bankassurance space will help them diversify their revenue streams and grow their non funded income. For insurers this model can enable them to maintain a smaller sales team as their products are sold at banking halls to ordinary bank customers. The caveat implicit in this model relates to the fact that the bank would become the new middleman and insurers will be weary not to be saddled with higher commissions charged in return for the scale, infrastructural deployment and institutionalization of insurance sales the banks provide. Commission ratios are expressed as the ratio between (net) commissions paid to net premiums earned and are paid to brokers without whom the insurer would not be able to access a wide geographical client base.

The insurance sector caters for both corporate and retail clients and the commercial line (premiums from businesses) dominates the industry. An insurer's foray into bankassurance space will expand the capacity to service the retail line more effectively and Kenya Re will benefit directly from enhanced penetration. An insurer's efficiency is measured by the expense ratio, which is expressed as the ratio between management and administration expenses to net earned premiums. Some Kenyan banks are already experimenting with this model by acquiring insurance firms as well as by offering insurance covers with certain banking products.

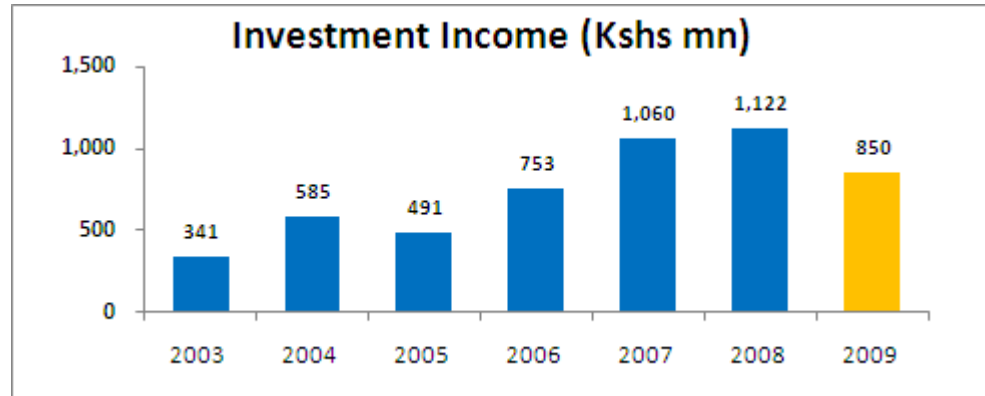
For example, if the banks make use of insurance covers at their asset financing divisions and some insist that if a customer does business with the bank it must insurer with an affiliated insurance provider (who in most cases is a subsidiary agent or broker of the bank). During the purchase of new equipment a customer may be looking to obtain a comprehensive cover, so it provides the customer a flexible avenue to do this.

There are other unexploited sectors of the economy such as real estate that banks can exploit through their mortgage divisions. In a bid to attract more business, mortgage providers have been encouraging home owners to apply for mortgage life insurance in the event that they die prematurely leaving the family with the financial burden. A mortgage life insurance policy runs for a fixed term and many people ensure that the policy remains consistent with the duration of their mortgages.

**Investment Income**

Kenya Re has a huge investment portfolio estimated to be valued at over Kshs10.3 billion as at 30<sup>th</sup> June 2009. The portfolio that represents 73% of assets has been the ‘Achilles Heel’ at least in terms of rating agency’s assessment of portfolio risk. The company has been restructuring its property portfolio to improve its liquidity and is substituting its property holdings with its mortgage loan business. Investment income has become crucial for Kenya Re’s business largely because underwriting profits have been unreliable due to a high combined ratio.

**Exhibit 8: Investment Income 2003-2008**



Source: Company Data

*In the nine months to September 2009 investment income rose 8.8% from Kshs 780 mn to Kshs 850 mn showing no signs of fear from depressed equity markets*

Insurers have been able to use their premium surpluses to build their “cash float” to counteract a combined ratio that’s in excess of 100%. Insurers earn investment income from these surplus premiums as they are collected until a claim arises that requires funding.

**Investment portfolio**

Although investment income has been volatile over the years the composition of the investment portfolio has witnessed subtle changes to correct the skewed focus on property holdings. The reduction of property holdings started a few years earlier with an increased focus on market securities (equity holdings) following the market upswing from 2003 to 2006. The equity portfolio is particularly exposed to one counter namely EABL and the management is simply considering diluting their exposure by piling into short term fixed income securities.

**Exhibit 9: Portfolio Composition 2004-2009**

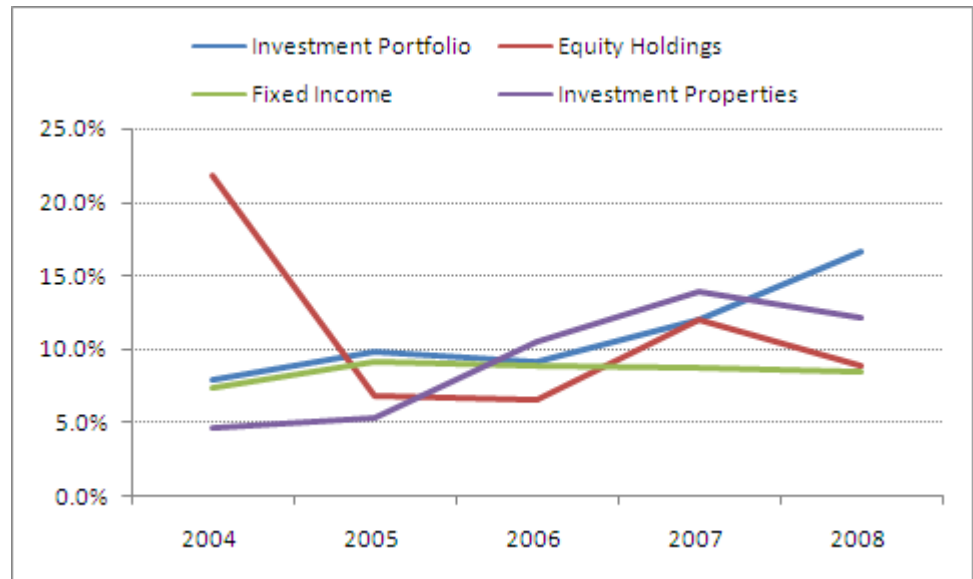
Investment Mix	Investment Mix					
	2004	2005	2006	2007	2008	HF 2009
Rental Properties	51.0%	42.7%	37.1%	33.6%	37.3%	37.1%
Fixed Deposits	6.2%	5.2%	6.3%	6.0%	9.0%	10.7%
Mortgage Loans	4.6%	5.1%	7.0%	7.2%	4.5%	4.6%
Marketable Securities	17.9%	22.9%	25.6%	27.6%	21.8%	21.6%
Government Securities	20.4%	24.0%	24.1%	25.7%	27.5%	26.1%
<b>Investment Portfolio</b>	<b>7,222.6</b>	<b>7,654.7</b>	<b>8,824.6</b>	<b>9,930.8</b>	<b>10,321.6</b>	<b>10,365.1</b>

Source: Company Data

*Investment mix is skewed toward investment properties of which a good portion comprise of non-performing assets*

However, during the nine months to September there was no significant increase in their fixed income earning assets. In fact there are indications that the premium float was being used to cover claims more effectively considering the ratio of cash to assets had rise from 1.0% to 3.7% in the nine months to September 2009. The ratio of cash to outstanding claims rose from 36.5% in 2007 to 46.6% in 2008 and that ratio has since improved to 59.8% as at September 2009. This means that the company’s liquidity is better suited to meet short term claims. Management plant to bolster the claims coverage ratio includes the disposal of non-performing property assets. Kenya Re holds properties valued at Kshs536 mn that it intends to sell (maybe in ‘10) on its balance sheet (categorised as non-current assets held for sale).

**Exhibit 10: Investment Returns from Key Investment Classes 2004-2008**



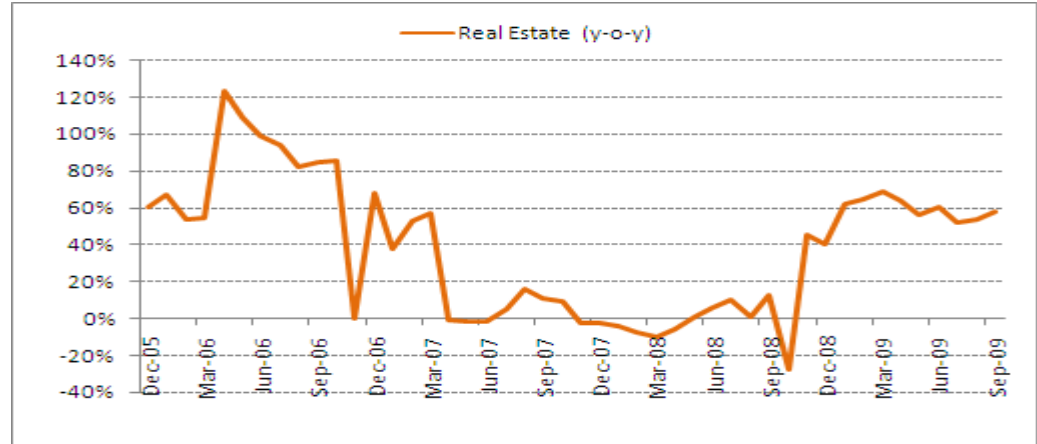
Source: Company Data

The management managed to yield a 7.6% growth in the life fund (up from 7.0% in ‘07) and we estimate an average growth of 12.6% in returns for Kenya Re’s investment portfolio between 2006 and 2008. The high growth was attributed largely to the investment property investments (including gains on sale of investment properties). Kenya Re is selling its properties and is no longer offering mortgage loans on properties it owns, but to finance independent property projects.

To show it’s commitment it launched a Kshs100 million commercial mortgage scheme earlier in the year to widen the firm’s revenue base in recognition of the dwindling returns from the equity markets. Although the scheme is a step in the right direction the size of the reserves may not be significant to drive growth of the bottom-line or make a dent on the balance sheet. Other key tests facing the scheme include high mortgage rates that could undermine the affordability of financing to customers as well as the fact that Kenya Re has no property arm that could deny it from accessing top quality mortgage assets. However, financing independent housing projects carries its own risk but the firm feels this risk can be managed effectively. During 2008 mortgage loans (largely for commercial properties) registered a marginal decline because of the property assets on its books being disposed during that year.

We estimate the returns on Kenya Re’s investment portfolio to be above 10% for the past three years, but, the risk on loans for properties it owns is considerably lower than for the mentioned scheme above. The property sector has continued to perform well in 2009 supported by robust lending from banks (up 60% y-o-y-).

**Exhibit 11: Domestic Credit to Real Estate Sector**



Source: CBK Monthly Economic Reviews

**Competitive Positioning**

The company operates in a highly competitive market with other regional players as well as international reinsurers. Regional players such as PTA Re and Africa Re enjoy regional compulsory cessions and have been rated by internationally recognized credit agencies such Standard & Poors. Many African countries are beginning to develop their own reinsurance firms such as Tanzania’s Tan Re and sign treaty agreements that favour the new entities. The region has witnessed the entry of new players such as Continental Re looking to steal market share and set-up shop using Kenya as the regional hub. Kenya Re has a strategic holding in PTA Re (that rose from 21.3% to 25.5%) and enables the latter to closely observe the performance of markets Zep Re operates in. In addition Kenya Re will likely post better margins as it pays a lower corporate tax rate of 20% as a result of listing 40% of its issued shares on the NSE in mid-2007. The downside to the 60% government holding is the fact that Kenya Re may be exposed to a high level of bureaucracy.

*PTA (Zep) Re is an associate company of Kenya Re and is exempt from all forms of taxation*

*The reduction of Kenya Re’s tax rate was for a limited time period of five years*

**Exhibit 12: Reinsurance Peer Comparison**

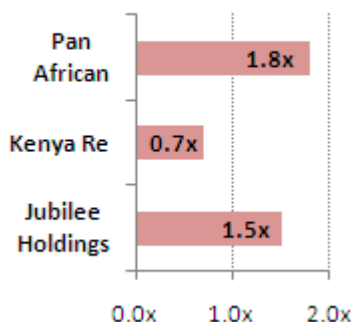
		Gross Premiums	Capital Base	ROA*	Solvency Margin
Kenya Re	2007	\$47.9 m	\$107.4 m	6.5%	243.0%
	2008	\$49.6 m	\$115.7 m	10.8%	257.4%
Africa Re	2007	\$366.4 m	\$230.8 m	5.1%	70.0%
	2008	\$393.4 m	\$223.7 m	3.0%	62.5%
Zep Re	2007	\$37.9 m	\$23.4 m	9.8%	79.2%
	2008	\$46.0 m	\$31.3 m	3.0%	84.5%
E. A. Re	2007	\$18.1 m	\$12.6 m	3.2%	120.2%
	2008	\$15.3 m	\$13.9 m	3.6%	122.1%

Source: Company Reports \* Figure based on year end balances

Profit Model	2004	2005	2006	2007	2008	2009E	2010E
<b>Gross Premium Earned</b>	<b>1,823</b>	<b>2,613</b>	<b>3,114</b>	<b>3,222</b>	<b>3,428</b>	<b>3,986</b>	<b>4,368</b>
<i>Growth</i>		43.3%	19.2%	3.5%	6.4%	16.3%	9.6%
<b>Net Earned Premium</b>	<b>1,718</b>	<b>2,111</b>	<b>2,791</b>	<b>2,975</b>	<b>3,109</b>	<b>3,634</b>	<b>3,999</b>
<b>EBITDA</b>	<b>614</b>	<b>999</b>	<b>813</b>	<b>1,044</b>	<b>1,739</b>	<b>1,730</b>	<b>1,960</b>
<i>EBITDA Growth</i>		62.7%	-18.6%	28.4%	66.5%	-0.5%	13.3%
<b>EBITA</b>	<b>566</b>	<b>948</b>	<b>764</b>	<b>1,009</b>	<b>1,730</b>	<b>1,720</b>	<b>1,959</b>
<i>EBITA Margin</i>	31.0%	36.3%	24.5%	31.3%	50.5%	43.2%	44.9%
- Taxes	397	59	312	258	205	191	172
<b>NOPLAT</b>	<b>169</b>	<b>889</b>	<b>453</b>	<b>751</b>	<b>1,525</b>	<b>1,530</b>	<b>1,787</b>
+ Depreciation	49	51	49	35	9	10	10
+/- Working Capital Change	528	(325)	155	62	(98)	98	141
- Expansionary Capex	(5)	6	(19)	(6)	(18)	(20)	(24)
<b>Free cash flow</b>	<b>751</b>	<b>609</b>	<b>675</b>	<b>855</b>	<b>1,453</b>	<b>1,657</b>	<b>1,962</b>
<i>% Change</i>		-18.9%	10.9%	26.5%	70.1%	14.0%	18.4%

**Valuation: Insurance sector retains low valuation multiples**

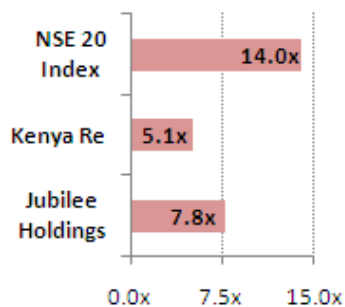
**Peer PBV Comparison**



Source: FIB Calculation

WACC Assumptions		Performance Indicators				
Debt Level	0.0%	2008	per annum change			
Equity Level	100.0%		2007	2008	2009E	2010E
Tax Rate	20.0%	<b>Growth Rates</b>				
Cost of Debt	0.0%	Sales	6.4%	9.7%	11.5%	10.0%
Risk Free Rate	7.2%	EBITA	71.5%	28.0%	8.5%	9.2%
Risk Premium	6.0%	EBITA Margin	50.5%	35.4%	44.8%	46.1%
Inflation Premium	5.0%	NOPLAT	102.9%	39.9%	10.5%	11.1%
Equity Beta	1.00	Free Cash Flow	70.1%	35.8%	15.6%	14.3%
Geared Beta	1.00	<b>Multiples</b>				
Cost of Equity	18.2%	EV/EBITDA	9.0x	3.8x	3.8x	3.4x
WACC	18.2%	Price/Sales	3.2x	2.2x	1.6x	1.4x
Long-term Growth	2.0%	PE Ratio	12.1x	5.2x	3.9x	3.2x

**Market PE Comparison**



Source: FIB Calculation

**Our recommendation**

We have valued Kenya Re at **Kshs21.00 per share** based on a weighted valuation basket namely: DCF, DDM and P/E. Insurance stocks at the NSE have low valuation multiples in comparison to their counterparts within the finance & investment sector and we believe there is a significant upside available in terms of capital appreciation. The downside risks are the hefty receivables balances accruing to reinsurance agreements stuck on their balance sheet of which the bulk of these receivables are owed by international companies. Other risks include properties pricing risk particularly for properties they will put on sale as well as risks from old/new competitors with better credit ratings. Given Kenya Re's objective to build underwriting capacity in French-speaking West African markets we anticipate the company will continue to plow back its earnings to boost reserves. The drawback to this may be a conservative dividend policy where the board is likely to payout 25-30% of profits to shareholders.

Financial Model	2002	2003	2004	2005	2006	2007	2008
<b>Profit &amp; Loss Statement</b>							
<i>KShs mn</i>							
Gross Earned Premium	1,339	1,680	1,823	2,613	3,114	3,222	3,428
Premium Ceded	109	142	195	324	323	248	319
<b>Net Earned Premium</b>	<b>1,212</b>	<b>1,487</b>	<b>1,718</b>	<b>2,111</b>	<b>2,791</b>	<b>2,975</b>	<b>3,109</b>
Investment Income	465	341	585	491	753	1,060	1,122
Other Income	0	0	0	264	0	175	579
<b>Net Income</b>	<b>1,678</b>	<b>1,828</b>	<b>2,303</b>	<b>2,867</b>	<b>3,544</b>	<b>4,209</b>	<b>4,810</b>
Management Expenses	200	196	193	290	453	597	665
Other Expenses	388	465	780	706	807	1,141	1,010
<b>Net Claims and Benefits</b>	<b>770</b>	<b>458</b>	<b>766</b>	<b>924</b>	<b>1,522</b>	<b>1,465</b>	<b>1,408</b>
<b>Underwriting Profit</b>	<b>N/A</b>	<b>487</b>	<b>347</b>	<b>409</b>	<b>262</b>	<b>94</b>	<b>98</b>
<b>Pre-Tax Profit</b>	<b>339</b>	<b>736</b>	<b>601</b>	<b>962</b>	<b>796</b>	<b>1,074</b>	<b>1,759</b>
Tax Charge/(Credit)	68	155	111	213	257	236	278
<b>Net Income</b>	<b>271</b>	<b>581</b>	<b>490</b>	<b>749</b>	<b>539</b>	<b>838</b>	<b>1,481</b>
EPS (Kshs)	2.71	5.81	3.26	4.99	3.59	1.40	2.47
DPS (Kshs)	1.20	1.20	1.00	1.00	1.00	0.35	0.50
Shares outstanding (mn)	100.0	100.0	150.0	150.0	150.0	600.0	600.0
<b>Balance Sheet</b>							
<i>KShs mn</i>							
Non Financial Assets	469	455	470	645	696	730	1,261
Financial Assets	7,576	8,543	8,494	9,733	12,288	12,232	12,404
<b>Total Assets</b>	<b>8,045</b>	<b>8,998</b>	<b>8,964</b>	<b>10,378</b>	<b>12,983</b>	<b>12,962</b>	<b>13,666</b>
Long Term Reinsurance Liabilities	1,363	1,534	1,658	1,816	2,123	2,084	1,926
Short Term Reinsurance Liabilities	2,634	2,694	2,345	2,449	2,414	3,062	3,368
Other Non Current Liabilities	1,366	697	508	563	2,111	590	367
<b>Shareholders' Funds</b>	<b>2,682</b>	<b>4,074</b>	<b>4,454</b>	<b>5,549</b>	<b>6,336</b>	<b>7,227</b>	<b>8,004</b>
<b>Other financial ratios</b>							
Reinsurance Retention Ratio	91%	89%	94%	81%	90%	92%	91%
Underwriting Profit / Net Earned Premium	N/A	33%	20%	19%	9%	3%	3%
Investment Income/Total Income	28%	19%	25%	17%	21%	25%	23%
<b>Return on Equity</b>	<b>N/A</b>	<b>17%</b>	<b>11%</b>	<b>15%</b>	<b>9%</b>	<b>12%</b>	<b>19%</b>
<b>Net Profit Margin</b>	<b>20%</b>	<b>35%</b>	<b>27%</b>	<b>29%</b>	<b>17%</b>	<b>26%</b>	<b>43%</b>
Claims Ratio	64%	31%	45%	44%	55%	49%	45%
Management Expense Ratio	16%	13%	26%	14%	16%	27%	21%
Commissions Ratio	32%	31%	30%	33%	29%	31%	32%
<b>Combined Ratio</b>	<b>112%</b>	<b>75%</b>	<b>101%</b>	<b>91%</b>	<b>100%</b>	<b>107%</b>	<b>99%</b>
<b>Available Solvency Margin (General)</b>	<b>N/A</b>	<b>N/A</b>	<b>N/A</b>	<b>N/A</b>	<b>N/A</b>	<b>292%</b>	<b>282%</b>
<b>Available Solvency Margin (Life)</b>	<b>N/A</b>	<b>N/A</b>	<b>N/A</b>	<b>N/A</b>	<b>N/A</b>	<b>21%</b>	<b>111%</b>
Cash Ratio	2.5%	3.2%	6.7%	4.7%	8.4%	5.7%	7.8%
Cash to Outstanding Claims	8.8%	12.9%	30.1%	25.5%	239.8%	36.5%	46.6%

Source: Company data

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