DRY ASSOCIATES

INVESTMENT BANK

Investment Newsletter May 2024

Photo Courtesy: Dry Associates Marketing Department

Dear Investor,

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Global Outlook

The Word Bank estimates the global economy will expand 2.4% in 2024. That is the slowest in the past three years. In 2021, as Covid faded, the global economy expanded 6%! Pent up demand and government stimulus spending – excess spending as it turns out - however, led to inflation.

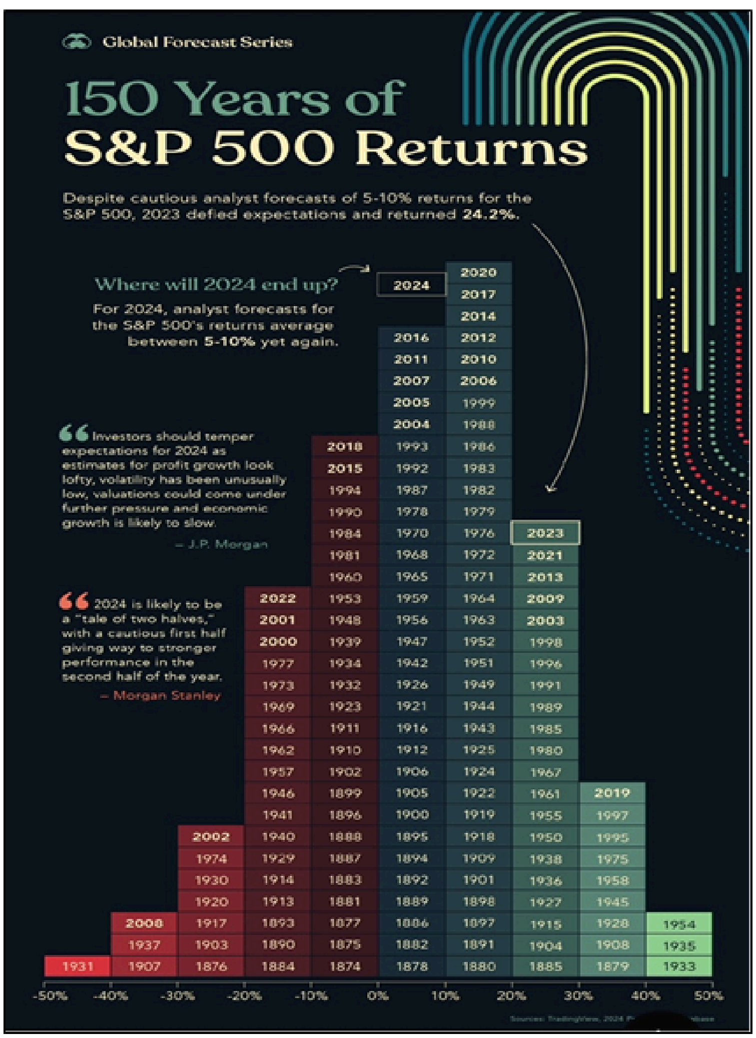
Central banks' efforts to control inflation around the globe led to interest rate hikes and that is what is constraining economic activity now. Fortunately, inflation worldwide is slowing but not rapidly enough, and the World Bank's global growth projections for 2025 are the same as 2024, that is, 2.4%. The growth figures are below:

Year	Global Growth
2021	6.02%
2022	3.08%
2023	3.00%
2024 (estimate)	2.40%
2025 (estimate)	2.40%

Source: World Bank

US Economy

The US economy, the largest in the world at 25 trillion dollars, is expected to grow at 2.5% in 2024. Earlier projections of a recession (two consecutive quarters of negative growth) have faded to a "soft landing" scenario. The Federal Reserve Bank has held interest rates at a relatively high 5.5% since mid-2023. The Fed's actions have succeeded in bringing inflation down from a high of 7.0% to 3.5% today. The target, however, is 2.0%. We expect the Fed will hold rates steady at its June meeting but may cut rates a quarter or half a point by year end. Any cut in interest rates will be a boost to the US stock market.



The US has presidential elections in November 2024 which introduce some uncertainty in the market. But while the US electorate is split down the middle between Democrats and Republicans, we expect that whoever takes the White House would not negatively impact the securities market. Of more concern, however, are current geopolitical events getting out of hand. But in investing, historically it is best to be a rational optimist. By that we mean, recognize short term obstacles for what they are but remain confident of long-term outcomes.

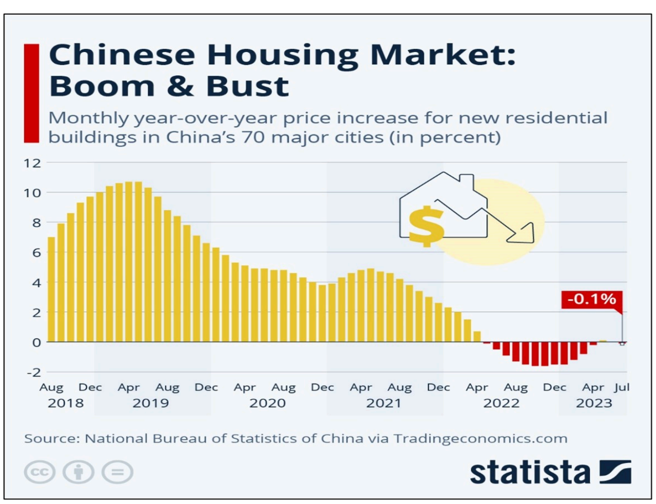
As investors, we need to be focused on the longer term – even the next 25 years. The world is changing fast and there are major themes shaping our future in dramatic ways. Perhaps the most dramatic is technological innovation and the emerging potential of AI. We think the US will continue to be a leader in this technological transformation and investors ought to have exposure to it through the US market. In fact, out model investment portfolio (see our "Weekly") for individuals 35 – 55 years old pencils in a 50% exposure to US securities, although this drops to 20% for older clients.

<u>China – Special Mention</u>

China deserves special attention here for its recent turn inward and increasing rejection of free market capitalism. The World Bank estimates China's economy will expand 4.5% in 2024, down 5.4% from the previous year. This is significantly less than the blistering 10%+ growth rates of prior years. President's Xi and the Communist Party of China have clearly cracked down on free market enterprise. There has always been an underlying conflict between capitalism, that is, private ownership of the means of production and communism which is state ownership. It is now in the open. President Xi's explanation for this new policy is that capitalism has led to income inequality and vast disparity in wealth. It has but why not simply tax excessive wealth rather than kill off innovation and entrepreneurship? We're reminded of Charlie Munger's (Warren Buffet business partner) quip, describing free market capitalism "I believe in equal opportunity, but unequal outcomes". In any event, state control is not the answer. Goldman Sachs estimates China lost over a trillion dollars in the market value of traded securities last year.

The Australian economist Peter Saunders argues, 'Nobody planned the global capitalist system, nobody runs it, and nobody really comprehends it. This particularly offends intellectuals, for capitalism renders them redundant. It gets on perfectly well without them.'

The Chinese economy has other problems, not the least of which is a real estate sector in crisis. Real estate prices ballooned in value caused by speculation and too much debt. It's variously estimated that as much as 50% of private individual wealth in China is tied to real estate. There are estimates of 50 to 100 million empty apartments owed by individuals who are underwater in terms of mortgages. The crisis begs a comparison to Japan in the late 1980's when its real estate bubble led to a drop of 60% in equity prices in 1992. That was followed by Japan's so-called "lost decade" of slow and negative economic growth.

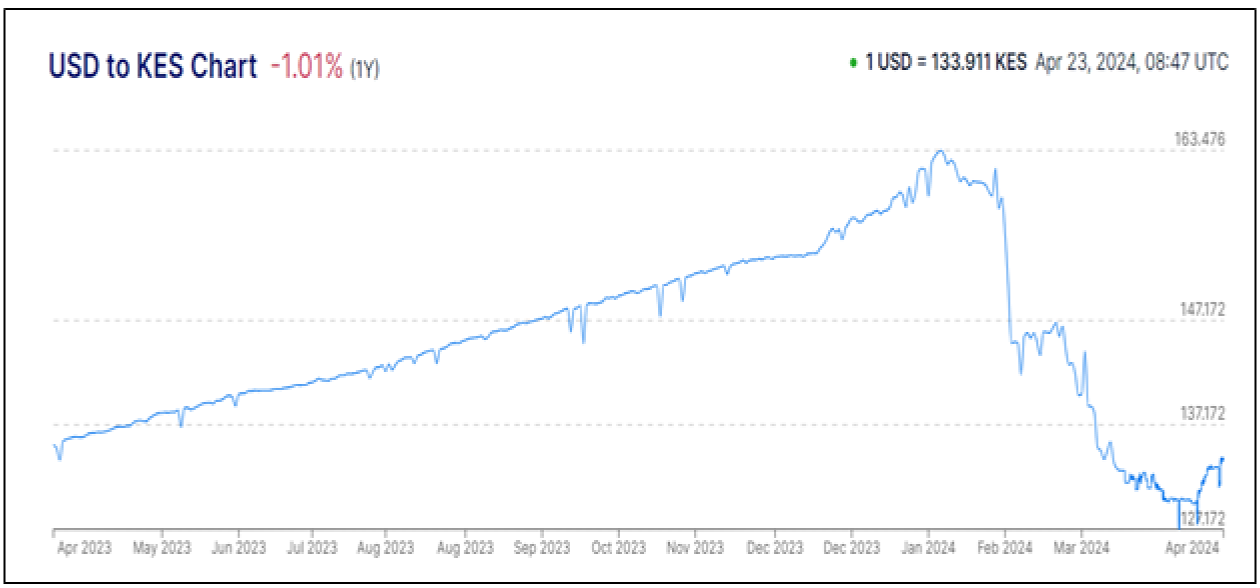


China has other concerns including an aging population and low birth rates. China fertility rate – meaning number of births per woman is 1.71. A fertility rate of 2.1 is the generally accepted as the minimum to maintain a country's population. As it is, China's population is expected to shrink by 110 million by 2050. Kenya's fertility rate by comparison is a robust 3.2!

That said, China's economy is still enormous. With a GDP of $17.5 trillion and a population of 1.4 billion, it remains the biggest trading partner of many countries. The US is China's biggest export market exporting over a half a trillion dollars of goods to the US in 2023. So, as long as it does not kill off capitalism completely, China will be an economic power – just not a recommended investor destination for the indefinite future.

Kenyan Shilling – Remarkable Rebound!

The Kenyan Shilling made an historic rebound over the past two months. The shilling appreciated from KES 163.47 to the US dollar on January 26 to KES 134.50 today (29-Apr-24). The shilling went from the worlds' worst performing currency to the best in a matter of weeks per the following graph:



Source: XE.com

The shilling fell in value almost daily – particularly in December 2023 - as fear mounted that Kenya would not be able to pay off a $2 billion Eurobond maturing in June 1024. The high interest rates in the Eurobond market were so unattractive that Kenya felt it could not refinance at those rates. In the end, Kenya bit the bullet and did place a $1.5 billion Eurobond into the market at an interest rate yield of 10.375%.

While it was the right thing to do to stop the depreciation of the shilling, the 10.375% yield is significantly higher than the 6.80% coupon on the bond it replaced. The balance of $500 million to be paid in June will be financed mainly by the World Bank. So, it is evident that the can has only been kicked down the road. This new bond is to be paid back in three equal installments in 2029, 2030 and 2031. In the meantime, the government continues to ply up debt to the tune of $82 billion (equivalent) today at killer interest rates.

If the Kenyan government continues to borrow and spend as it has in the past, we expect the shilling will continue to weaken against other major currencies. Without major reforms, we would expect the shilling to trend toward KES 150/$ over the next 6-12 months.

Estate Planning

There is an important subject that requires attention as one gets older. That is the orderly and efficient transfer of wealth from one generation to another. Assuming one has created wealth over a lifetime, passing that wealth to loved ones is a lifetime act of caring to those we leave behind. It should not be left until one is feeble or incapacitated. For the record, it has no bearing on the timing of one's passing to a better world.

Wealth transfer, however, requires some preparation. If not done properly, your wealth will be tied up in probate court for 6 months (or more). Your progeny may well squabble over what seems rightfully theirs and, in the end, what is eventually conveyed will probably be much less than it should have been because of court and legal fees, taxes not avoided, and lost income.

"When it comes to divide an estate, the politest men quarrel."
Ralph Waldo Emerson

Succession Planning

This exercise is particularly important to families that own businesses. Succession planning is a special form of estate planning for families that own businesses. To quote from the manual of the US Certified Financial Planning College "Most closely held businesses fail to survive their founder because no succession planning is done". This is a shame and ought not to happen.

There are ways of preserving wealth in family-owned businesses. One way is to on-board strategic investors with Board of Director and/or management representation. Another is "Listing by Introduction" on the Nairobi Securities Exchange where new capital is not raised but shares are listed. This provides a market value for company shares through "price discovery" and provides liquidity for shareholders. It allows shares to be conveyed to any number of beneficiaries. Listing by Introduction is less onerous than an "IPO" or Initial Public Offering which involves raising new capital while obtaining price discovery for a company's shares. These and other ways of preparing a company for eventual ownership changes are at your disposal through Dry Associates Investment Bank.

Using a Trust to Transfer Wealth

Wills and trusts are typically not necessary for married couples if all you own is a bank account and that account is in joint name. The Doctrine of Survivorship typically applies to bank accounts in joint names, but it is wise to review bank account opening forms to ensure that joint tenancy is established. Other assets like life insurance policies are created with beneficiaries as the objective so payouts are automatically conveyed to designated persons.

Nevertheless, most people own more than a bank account or an insurance policy. Most people own automobiles, jewelry, land, home(s), securities, partnership interests, and many other assets. These assets can all be conveyed to beneficiaries through a will. The problem with a will is that it must be probated meaning a court must be involved to review, approve, and see to its distribution. This is a public process and involves lawyers and time - typically six months or more in Kenya.

A better approach is to create a trust. This is because it avoids the probate process and is not a matter of public record. Basically, a settlor (owner of the assets) sets up a trust and designates a trustee(s) to manage and disburse the settlor's assets for the benefit of others upon death of the settlor.

There are various types of trusts – Family Trusts, Charitable Trusts, Testamentary Trusts – but the most common trust we prepare at Dry Associates are Family Trusts. Family trusts can be "living" or "testamentary". A testamentary trust is established through a will so it must go through probate which is what most people want to avoid. Living trusts, on the other hand, are not probated and can be amended by the settlor during the settlor's lifetime. This type of trust also allows for the appointment of an "enforcer" who can watch over the performance of the trustee(s). The settlor can even designate himself as enforcer during his lifetime.

Trusts can be created for any number of purposes, for example, to provide for long term household staff, to transfer ownership directly to children, to fund specific organizations and so on. For more information on estate planning, please contact your Investment Executive at Dry Associates who will arrange a meeting with our internal legal counsel to prepare and register these private trusts. Note that these services are only available to Private Wealth Clients.

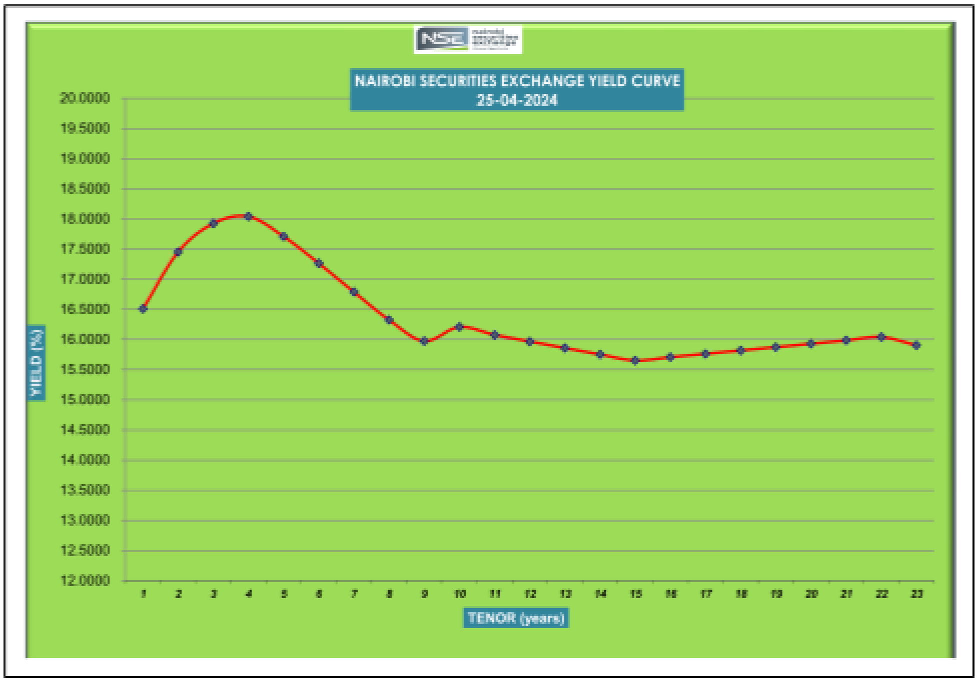
New Corporate Debt Issues

4G CAPITAL

4G Capital offers working capital and literacy training to thousands of Kenyan and Ugandan Small and Medium Sized Enterprises. In business since 2013, the company has some 450,000 clients offering short term loans via mobile phone and face-to-face outreach. Dry Associates is the Arranger and Placement Agent of the 6- and 12-month KES 500 million note programme.

Kenyan Fixed Income Yields Today

The yields available on Kenya Shilling denominated debt securities typically use the GOK Treasury Bill and Bond yield curve as a guide in pricing debt securities. Normally short-term yields are lower than long term yields as it is riskier to lend money long term than short term. But this is currently not the case in Kenya. Short term yields are higher than long term yields! This anomaly reflects the fact that the Central Bank has hiked its CBK Base Rate to dampen inflation and hold the value of the shilling, but also indicates that investors are currently demanding higher yields because of short-term uncertainty.



Whatever the reason, the following yields are currently available on KES and US$ fixed income securities today:

Issue	Interest Rate Yield
3-year Corporate Note (BBB rated) (KES)	20.89%
1-year Commercial Paper (BBB rated) (KES)	18.33%
2-year re-opened Treasury Bill	17.00%
1-year Government of Kenya Treasury Bill	16.49%
6-month Government of Kenya Treasury Bill	16.46%
Dry Associates Money Market Fund (KES)	13.82%
Annual Average Inflation in Kenya	***6.97%***
Dry Associates Money Market Fund (US$)	6.34%

Dry Associates 30th Anniversary

Dry Associates turned 30 years old on February 24, 2024. The company celebrated with a team building and white-water rafting day on the Tana River.

Photo Courtesy: Rapids Camp

New Directors for Dry Associates

Dry Associates has welcomed the following two new Directors to the Board of Directors. We look forward to working with each of them and gaining from their skills and experience.

Hamish Keith is a Kenyan advocate of the High Court of Kenya, Solicitor of the Supreme Court of England, and Certified Public Secretary with over 50 years of experience in legal practice. He is a member of the Law Society of Kenya, Law Society of England, and the Institute of Certified Public Secretaries (Kenya). He has served as a Senior Partner, Managing Partner, and Leader of the Corporate and Commercial Section at CMS Daly Inamdar Advocates. He has worked on a wide variety of Kenyan legal projects, including banking, corporate and commercial transactions. He has substantial experience in privatization e.g. of Kenya Airways, Safaricom, Tourism Promotion Services (Serena Hotels), and other capital markets transactions. He is a director of several companies and a trustee of various trusts.

Davinder Sikand is one of the private equity pioneers in this region with over 30 years' experience in Africa, Europe, and USA. He co-established Aureos Capital, a mid-market private equity firm, where he served as Deputy CEO and Head of Sub-Saharan African Operations. He later initiated the sale of Aureos to Abraaj group. He has also advised Catalyst Principal Partners and Admaius Capital on their East Africa private equity operations. Davinder has extensive experience in Environmental Conservation through board positions. He holds an MBA from Kellogg.

Ms. Susan Hinson recently retired from the Board of Directors after 12 years of service to Dry Associates. Her expertise, particularly in accounting and finance, helped guide the company over these many years and we will miss her very much.

We end this Newsletter once again by reiterating that our sole purpose and mission is to help our clients achieve financial independence through wealth creation and preservation. We do this by participating in the growth and prosperity of growing companies operating in Kenya and abroad. We look forward to working with each of our clients on an individual basis for many years to come.

Sincerely,
Dry Associates Investment Bank

We Know … Investment Matters

DRY ASSOCIATES

INVESTMENT BANK

Dry Associates Investment Bank offers a wide range of products and services:

Private Wealth Management | Unit Trusts | Commercial Paper | Investment Advisory Services | Pension Fund Management | Offshore Funds | Consulting | Corporate Finance | Treasury Management | Portfolio Management

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