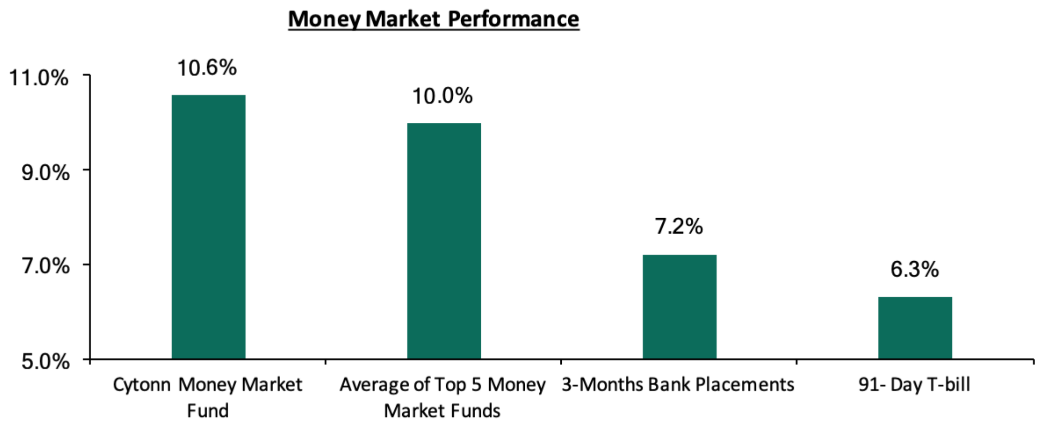
Kenya Real Estate Developers Regulatory Board, & Cytonn Weekly #38/2020

Fixed Income

Money Markets, T-Bills & T-Bonds Primary Auction:

During the week, T-bills remained undersubscribed, with the subscription rate coming in at 70.4%, down from 84.1% the previous week.The highest subscription rate was in the 91-day paper, which came in at 151.3%, down from 180.7% recorded the previous week as it remained attractive on a risk adjusted basis compared to the others. The subscription for the 182-day paper fell to 19.2%, from 76.0% recorded the previous week, while that of the 364-day paper increased to 89.2% from 53.5% recorded the previous week. The yields on all three papers remained unchanged at 6.3%, 6.7% and 7.6%, respectively, The acceptance rate increased to 100.0%, from 92.6% recorded the previous week, with the government accepting Kshs 16.9 bn worth of bids received.

There was high demand for the months bond offers as the overall subscription rate for the three bonds was at 163.5%, government received bids worth Kshs 81.7 bn, higher than the Kshs 50.0 bn offered. The three re-opened auctions were, FXD2/2010/15, FXD1/2020/15 and FXD1/2011/20 with fixed coupons of 9.0%, 12.8% & 10.0% and effective tenors of 5.3 years, 14.5 years and 10.7 years, respectively. It is clear that investors are happy with longer term bonds as FXD1/2020/15 had the highest subscription rate coming in at 99.6%, Kshs 49.8 bn, compared to the Kshs 50.0 bn offered. Yields on the bonds came in at 10.6%, 12.5% and 12.0%, for the FXD2/2010/15, FXD1/2020/15 and FXD1/2011/20, respectively. The government rejected high bids only accepting Kshs 64.2 bn out of the Kshs 81.7 bn worth of bids received, translating to an acceptance rate of 78.6%.



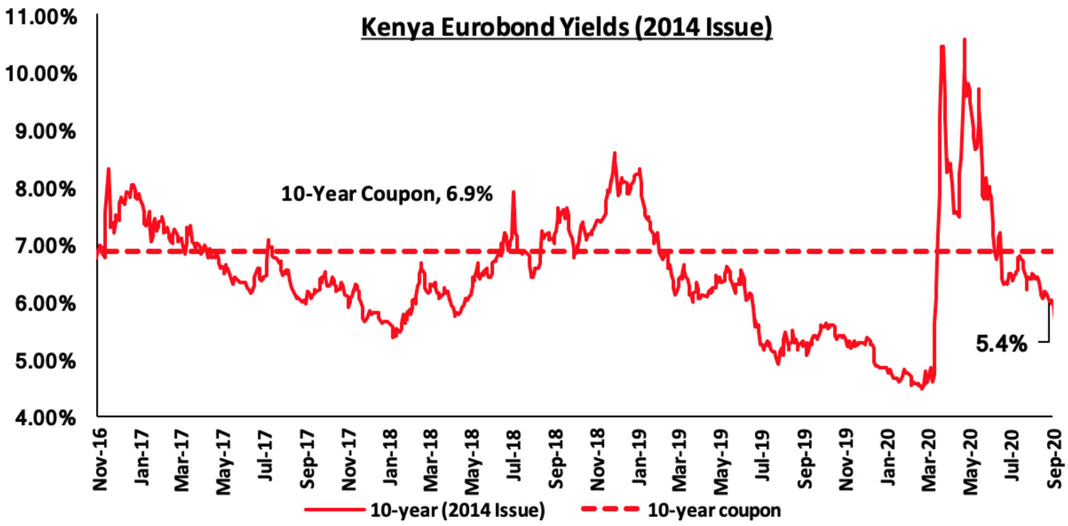
In the money markets, 3-month bank placements ended the week at 7.2% (based on what we have been offered by various banks), while the yield on the 91-day T-bill remained unchanged at 6.3%. The average yield of Top 5 Money Market Funds remained unchanged at 10.0%. The yield on the Cytonn Money Market remained unchanged at 10.6%, similar to what was recorded the previous week.

Liquidity:

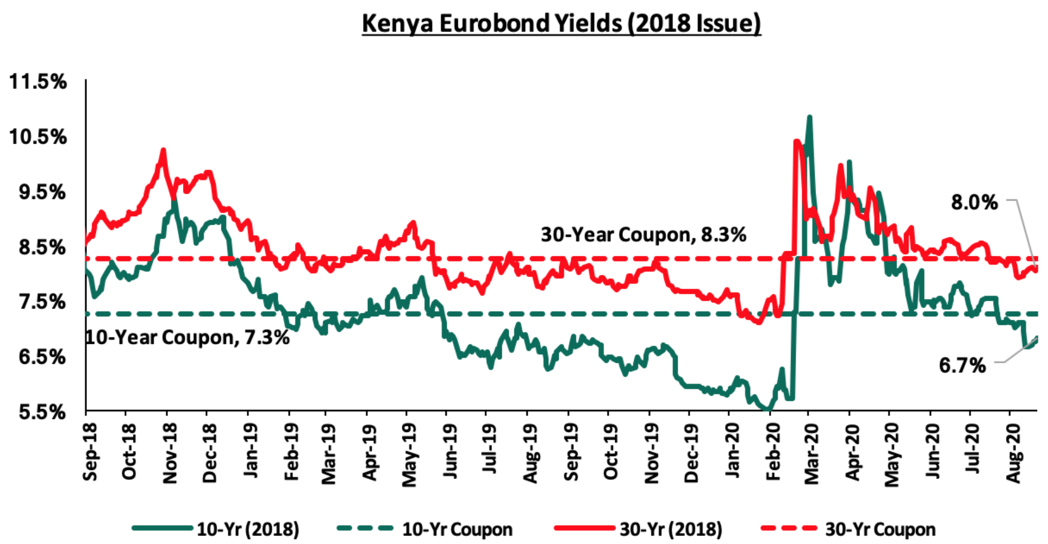
The money markets remained liquid during the week, with the average interbank rate increasing marginally to 2.7%, from 2.6% recorded the previous week, mainly supported by government payments. The average interbank volumes declined by 11.7% to Kshs 11.1 bn, from Kshs 12.6 bn recorded the previous week. According to the Central Bank of Kenya, commercial banks' excess reserves came in at Kshs 9.6 bn in relation to the 4.25% Cash Reserve Ratio.

Kenya Eurobonds:

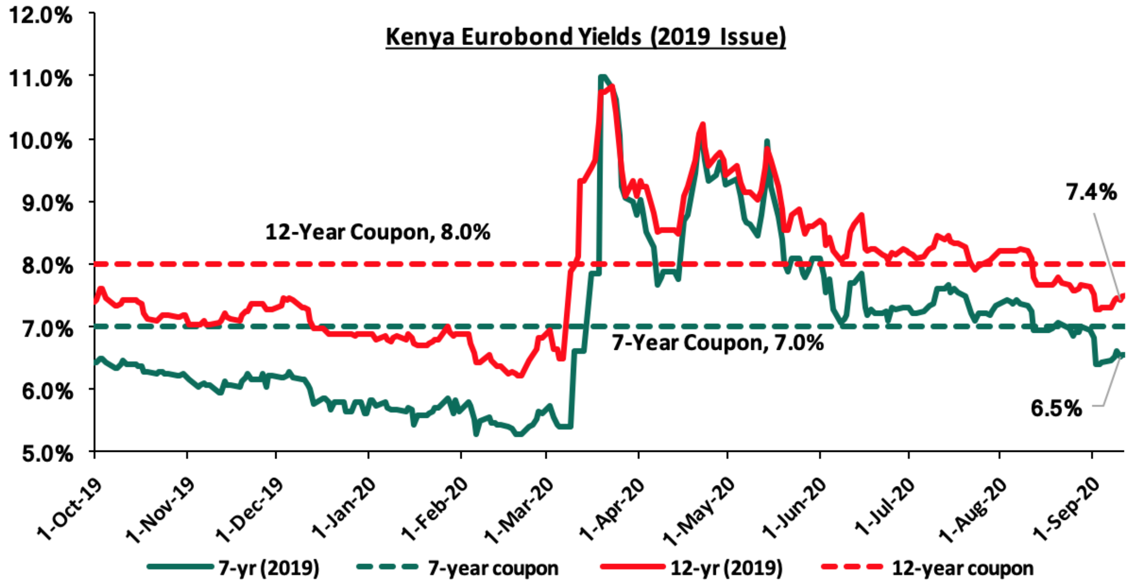
During the week, according to Reuters, the yield on the 10-year Eurobond issued in June 2014 declined marginally by 0.1% points to 5.4%, from 5.5% the previous week.



During the week, the yields on the 10-year and 30-year Eurobonds both remained unchanged at 6.7% and 8.0%, respectively, similar to what was recorded the previous week.



During the week, the yields on the 2019 dual-tranche Eurobond issue with 7-years decreased marginally by 0.1% points to 6.5%, from 6.6% the previous week. The 12-year Eurobond remained unchanged to close at 7.4%, similar to what was recorded the previous week.



Kenya Shilling:

During the week, the Kenyan shilling remained unchanged against the US dollar, to close at Kshs 108.4, mainly attributable to subdued dollar demand from importers. On an YTD basis, the shilling has depreciated by 7.0% against the dollar, in comparison to the 0.5% appreciation in 2019.

In the short term, the shilling is expected to be supported by:

i. Though has been decereasing, the high levels of forex reserves, currently at USD 8.9 mn (equivalent to 5.4-months of import cover), above the statutory requirement of maintaining at least 4.0-months of import cover, and the EAC region's convergence criteria of 4.5-months of import cover;
ii. Relatively strong Diaspora remittances that increased by 23.4% to USD 277.0 million in July compared to USD 225 million in July 2019, despite being 4.0% lower than the USD 288.5 million in June 2020, leading to the narrowing of the country's current account deficit to 4.7% of GDP in the 12 months to July 2020, compared to 5.0% of GDP in the 12 months to June.

However, in the longterm, the shilling in expected to be weighed down by:

i. Demand from merchandise and energy sector importers as they beef up their hard currency positions,
ii. A deteriorating current account position, with the current account deficit deteriorating by 10.2% during Q1'2020, to Kshs 110.9 bn, from Kshs 100.6 bn recorded in Q1'2019 attributable to;
   a. 0% decline in the secondary income (transfers recorded in the balance of payments whenever an economy provides or receives goods, services, income or financial items) balance, to Kshs 124.1 bn, from Kshs 128.0 bn in Q1'2019, and,
   b. A 67.0% decline in the services trade balance (the difference between the imports and exports of services) to Kshs 20.4 bn, from Kshs 61.9 bn.

Weekly Highlight:

During the week, the Energy and Petroleum Regulatory Authority (EPRA) released their monthly statement on the Maximum Retail Prices in Kenya for the period 15th September 2020 to 14th October 2020. Below are the key take-outs from the statement:

- Petrol prices have increased by 1.3% to Kshs 105.4 per litre from Kshs 104.0 per litre previously, while diesel prices have declined marginally by 0.1% to Kshs 94.5 per litre from Kshs 94.6 per litre. Kerosene prices also declined marginally by 0.6% to Kshs 83.2 per litre from 83.7 per litre, previously,

- The changes in prices have been attributed to:
  i. An increase in the average landing cost of imported of imported super petrol by 2.7% to USD 327.7 per cubic meter in August 2020 from USD 319.2 per cubic meter in July 2020,
  ii. Landing costs for diesel decreased by 1.0% to USD 329.9 per cubic meter from USD 333.3 in July 2020,
  iii. A 2.1% decrease in the landing costs for kerosene to USD 282.1 per cubic meter on August 2020, from USD 288.0 in July 2020,
  iv. A 3.3% increase in Free on Board (FOB) price of Murban crude oil lifted in August 2020 to USD 45.7 per barrel from USD 44.3 per barrel in July 2020, and,
  v. The Kenyan shilling depreciated by 0.4% against the dollar to close at Kshs 107.9 in August 2020, from Kshs 107.5 in July 2020.

The changes are a reflection of the crude oil prices in the global markets where the months of June and July saw significant gains which seem to have slowed down in the month of August. This was mostly attributable to the reopening of some economies. We expect the changes to have minimal impact on the total consumer price index (CPI) attributable to the netting effect on the kerosene and diesel prices.

Rates in the fixed income market have remained relatively stable due to the high liquidity in the money markets, coupled with the discipline by the Central Bank as they reject expensive bids. The government is 103.3% ahead of its prorated borrowing target of Kshs 112.2 bn having borrowed Kshs 228.1 bn. In our view, the government will struggle to meet their revenue collection targets of Kshs 1.9 tn for FY'2020/2021 because of the current subdued economic performance in the country brought about by the spread of COVID-19, and therefore leading to a larger budget deficit than the projected 7.5% of GDP, ultimately creating uncertainty in the interest rate environment as additional borrowing from the domestic market may be required to plug in the deficit. Owing to this uncertain environment, our view is that investors should be biased towards short-term to medium-term fixed income securities to reduce duration risk.
