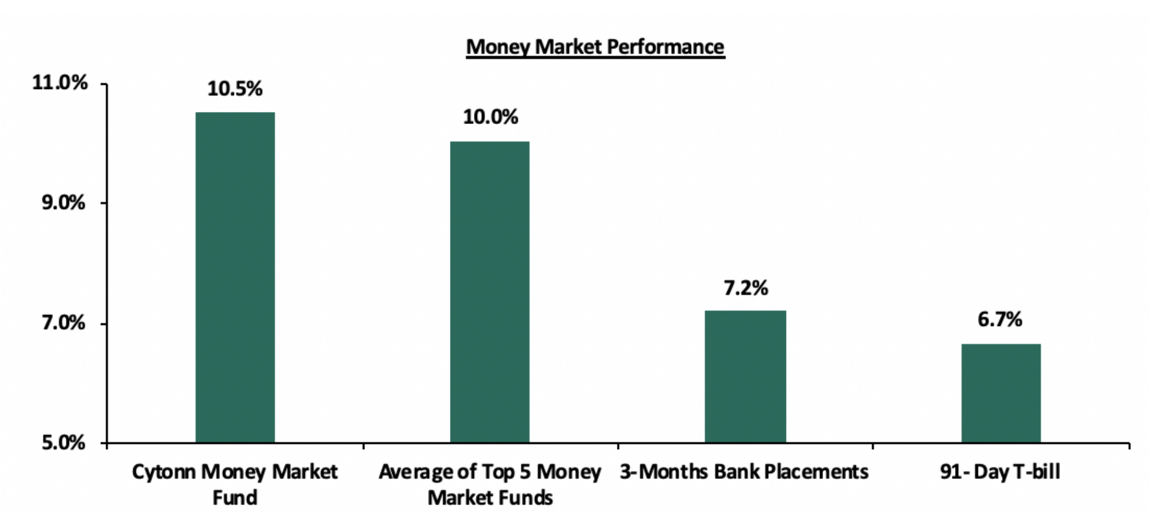
# Kenya Mortgage Refinance Company (KMRC) Recap, & Cytonn Weekly #45/2020

## Fixed Income

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

During the week, T-bills were oversubscribed, with the overall subscription rate coming in at 115.9%, up from 72.1% the previous week driven by high liquidity in the money markets. The highest subscription rate was in the 364-day paper, which came in at 210.0%, up from 110.1% recorded the previous week. The subscription for the 182-day paper increased to 45.5% from 33.1%, while that of the 91-day paper dropped to 56.9% from 74.9% recorded the previous week. The yields on the 182-day and 364-day both increased by 0.1% points to 7.1% and 8.0%, respectively, from 7.0% and 7.9% while the 91-day paper remained unchanged at 6.7%. The acceptance rate increased to 99.2%, from 95.5% recorded the previous week, with the government accepting bids worth Kshs 27.6 bn out of the Kshs 27.8 bn worth of bids received.

The Treasury plans to re-open two bonds, a 15-year and 20-year bond, FXD2/2013/15 and FXD2/2018/20, with effective tenors of 7.5 and 17.4 years, respectively for a total value of Kshs 40.0 bn. The bonds have fixed coupon rates of 12.0% for the 15-year, and 13.2% for the 20-year. The period of sale runs from 4th November 2020 to 17th November 2020 and our recommended bidding ranges are 12.5% - 12.7% for FXD2/2013/15 and 12.9% - 13.1% for FXD2/2018/20, given that bonds with a similar tenor are currently trading at 12.6% and 13.0%, respectively. Additionally, the treasury has offered a tap sale for a 25-year bond, FXD1/2018/25, with a fixed coupon rate of 13.4%, and an effective tenor of 23 years, for a total amount of Kshs 20.0 bn. The period of sale starts from 4th November 2020 to 10th November 2020, or upon attainment of the amount offered.



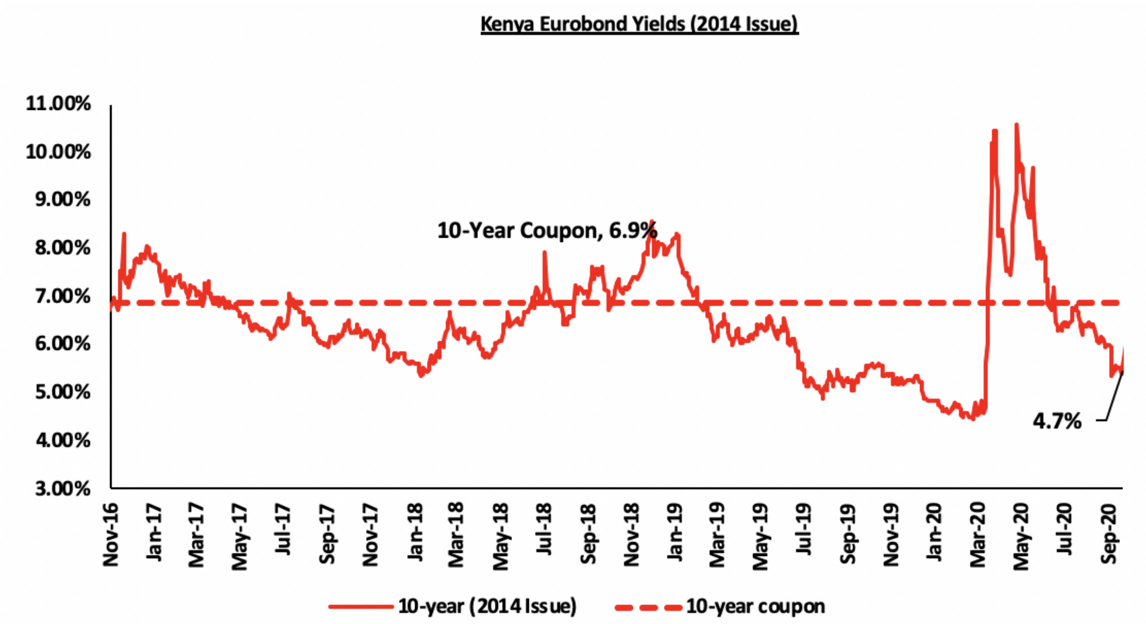

In the money markets, 3-month bank placements ended the week at 7.2% (based on what we have been offered by various banks), while the yield on the 91-day remained unchanged at 6.7% recorded the previous week. The average yield of the Top 5 Money Market Funds declined by 0.1% points to 10.0% from 10.1% as recorded the previous week. The yield on the Cytonn Money Market declined by 0.1% points to 10.5% from 10.6% as recorded the previous week.

Liquidity:

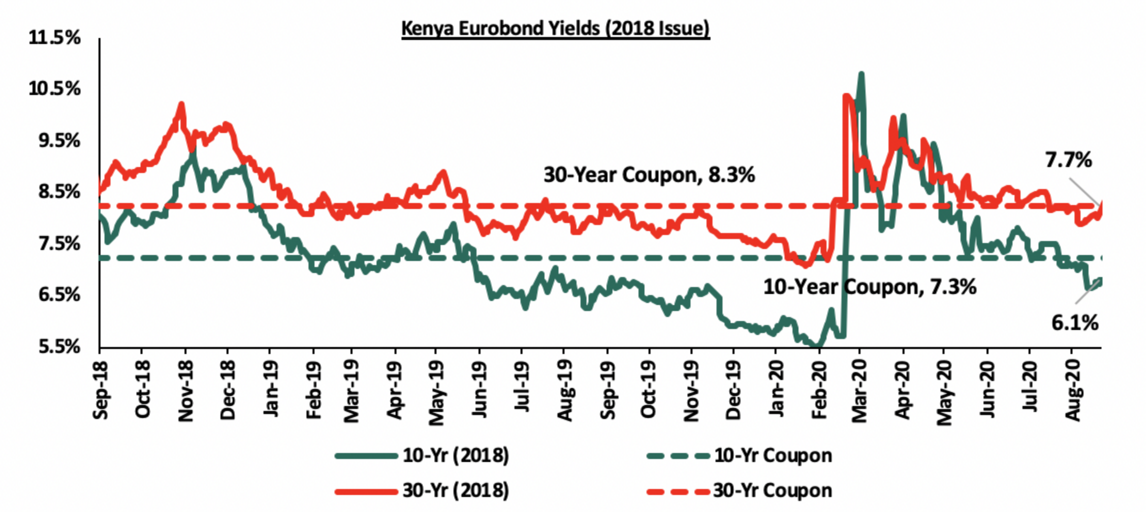
The money markets were relatively liquid during the week, supported by government payments, which partly offset tax receipts. However, the average interbank rate increasing to 3.3%, from the 3.0% and the interbank volumes decreased to Kshs 7.0 bn from Kshs 13.1 bn recorded the previous week. According to the Central Bank of Kenya's weekly bulletin, commercial banks' excess reserves came in at Kshs 10.5 bn in relation to the 4.25% Cash Reserve Ratio.

Kenya Eurobonds:

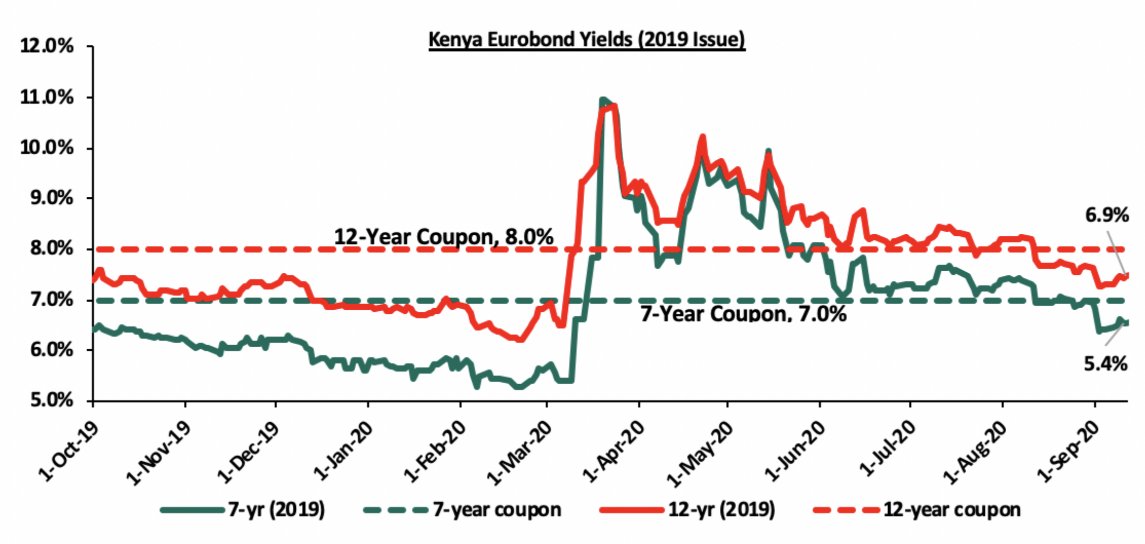
During the week, the yields on all Eurobonds declined pointing to improved investor sentiment and perception of decreased risk on the country's outlook driven by the improvement in the PMI ratings which increased to 59.1 from 56.3, pointing out to an improving business environment. According to Reuters, the yield on the 10-year Eurobond issued in June 2014 declined by 0.4% points to 4.7%, from 5.1% recorded the previous week.




During the week, the yields on the 10-year and 30-year Eurobonds both declined by 0.4% points and 0.3% points to close at 6.1% and 7.7%, respectively.




During the week, the yields on the 2019 dual-tranche Eurobonds issue declined. The 7-years Eurobond declined to 5.4%, from 6.1% the previous week, while the 12-year Eurobond declined to close at 6.9%, from the 7.3% recorded the previous week.




Kenya Shilling:

During the week, the Kenyan shilling marginally depreciated against the US dollar by 0.1% to Kshs 108.9 from Kshs 108.8, mainly attributable to the dollar importer demand being matched by supply. On an YTD basis, the shilling has depreciated by 7.4% 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. The Forex reserves which are currently at USD 8.1 bn (equivalent to 4.9-months of import cover), which is 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. The improving current account position which has seen a 39.9% decline during Q2'2020, coming in at Kshs 82.2 bn, from Kshs 136.9 bn in Q2'2019, equivalent to 7.0% of GDP from the 10.9% of GDP recorded in Q2'2019.

October PMI:

During the week Stanbic Bank released the Monthly Purchasing Managers' Index (PMI) for October 2020, which came in at 59.1, up from the 56.3 recorded in September 2020. Key to note, a reading of above 50 indicates improvements in the business environment, while a reading below 50 indicates a worsening outlook. Notably, Kenya recorded the sharpest improvement in business conditions during the month since the beginning of the survey in January 2014. This points towards robust improvements in the private sector, production and demand in the month of October. This comes after the government eased further lockdown restrictions related to the coronavirus pandemic. Rising output and demand saw firms levelling up their staff numbers, ending a seven-month sequence of job cuts. This was noted as the highest employment growth rate in 11 months. As such, selling prices rose as firms passed higher cost burdens to customers backing on staff cost inflation although the rise was minimal. Pre-production inventories increased remarkably as a result of increased input buying by companies. Consequently, purchase costs rose at a considerable rate attributable to higher raw material prices. A sequential increase in stocks with improved investor perception in future demand was also noted. The record increase is an indication of business confidence and improved business conditions. Lockdown restrictions re-imposed by international trading partners could however hinder growth witnessed in the recent months. We have a cautious outlook in the short term owing to the increase in COVID-19 infections, which has also seen the government extend the curfew hours by one hour and for a further two months. We expect this to lead to a subdued economic performance.

*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 63.5 % ahead of its prorated borrowing target of Kshs 130.9 bn having borrowed Kshs 214.0 bn. In our view, due to the current subdued economic performance brought about by the effects of the COVID-19 pandemic, the government will record a shortfall in revenue collection with the target having been set at Kshs 1.9 tn for FY'2020/2021 thus 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 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.*

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