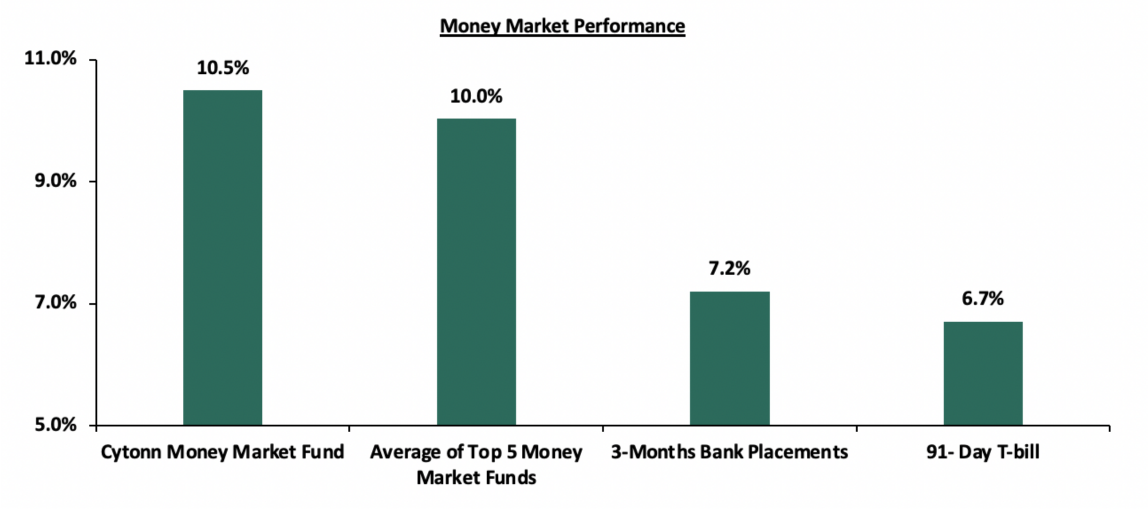
Kenya Retail Report 2020 & Cytonn Weekly #47/2020

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 104.2% down from 126.6%, the previous week, mainly attributable to focus on the primary bond auction, where there were two bonds re-opened namely, FXD2/2013/15 and FXD1/2018/20, which recorded a higher overall subscription rate of 140.0%. The highest subscription rate was in the 91-day paper, which came in at 139.6%, down from 220.3% recorded the previous week. The subscription rate for the 364-day and 182-day papers both dropped to 129.3% and 65.0%, respectively, from 135.4% and 80.3% recorded the previous week. The yields on all the three papers, 91-day, 182-day and 364-day increased marginally by 3.2 bps, 3.8 bps and 5.2 bps to 6.7%, 7.2% and 8.1%. The acceptance rate declined slightly to 96.6% from 97.7%, recorded the previous week, with the government accepting bids worth Kshs 24.2 bn out of the Kshs 25.0 bn worth of bids received.

On the Primary bond market there was high demand for this month's bond offers, with the overall subscription rate for the two bonds coming in at 140.0%, partly supported by the favorable liquidity in the market, and financial institutions bias towards the fixed income market in this period of economic uncertainty. The Central Bank of Kenya had re-opened 2 bonds the FXD2/2013/15 and FXD1/2018/20 with coupons of 12.0% and 13.2% and effective tenors of 7.5 years and 17.4 years, respectively. The government received bids worth Kshs 56.0 bn, higher than the Kshs 40.0 bn offered and accepted only Kshs 53.7 bn. Investors preferred the longer-term paper i.e. FXD1/2018/20, which received bids worth Kshs 28.9 bn, representing 51.2% of the total bids received. The weighted average rate of accepted bids for the two bonds came in at 11.4% and 13.3%, for FXD2/2013/15 and FXD1/2018/20, respectively. The government rejected high bids only accepting Kshs 53.7 bn out of the Kshs 56.0 bn worth of bids received, translating to an acceptance rate of 96.0%.



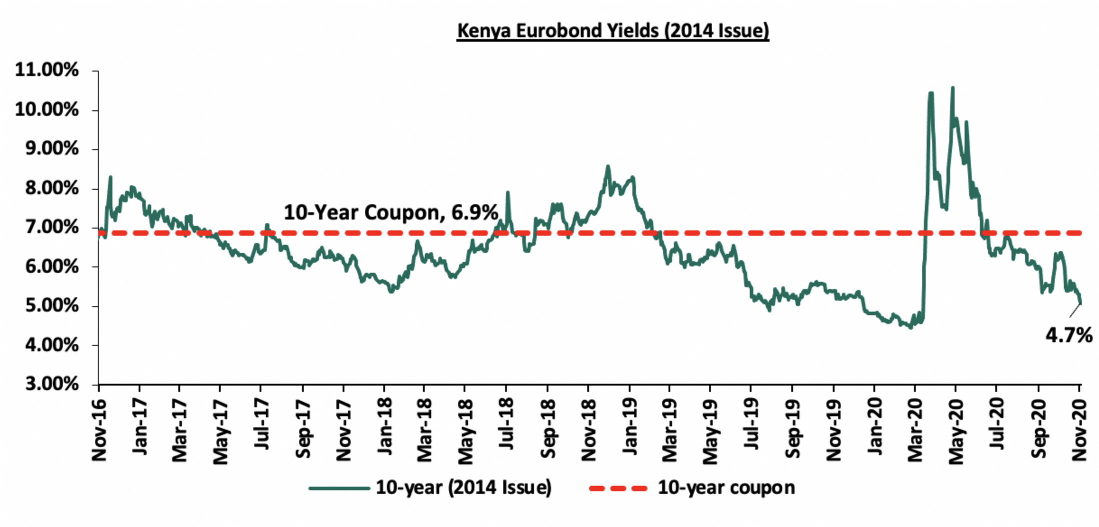
In the money markets, 3-month bank placements ended the week at 7.2% (based on what we have been offered by various banks), while the yield on the 91-day increased marginally by 3.2 bps to close at 6.7%. The average yield of the Top 5 Money Market Funds declined by 0.1% points to 10.0% from 10.1% recorded the previous week. The yield on the Cytonn Money Market Fund remained unchanged at 10.5%, similar to what was recorded the previous week.

Liquidity:

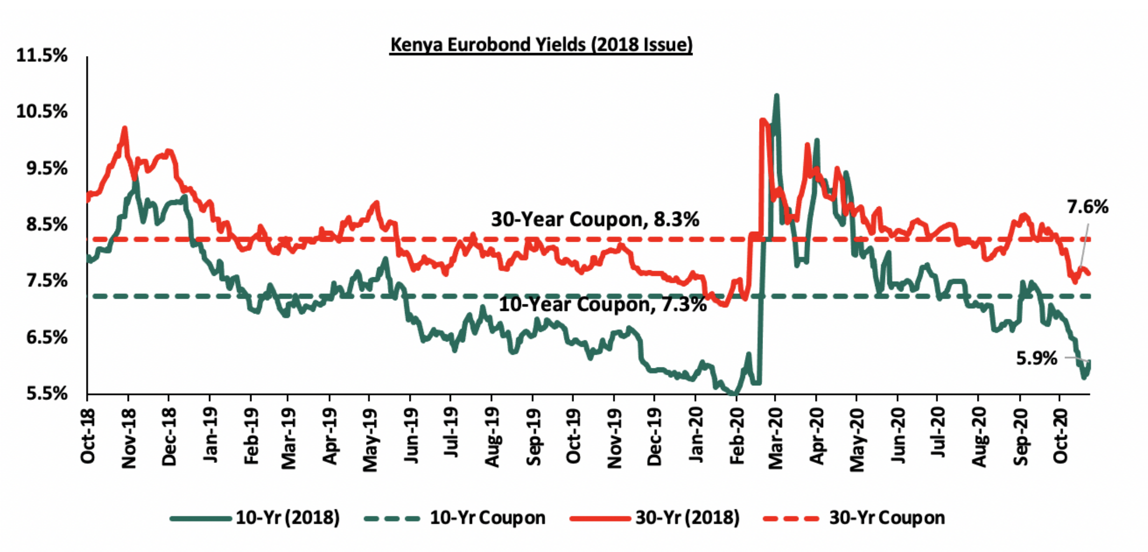
The money markets remained liquid during the week, with the average interbank rate increasing marginally by 0.2% points to 3.1%, from the 2.9% recorded the previous week. This was supported by government payments, which partly offset tax receipts. The average interbank volumes also declined by 42.0% to Kshs 4.7 bn from Kshs 8.2 bn, as recorded the previous week. According to the Central Bank of Kenya's weekly bulletin released on 20th November 2020, commercial banks' excess reserves came in at Kshs 8.2 bn in relation to the 4.3% Cash Reserve Ratio.

Kenya Eurobonds:

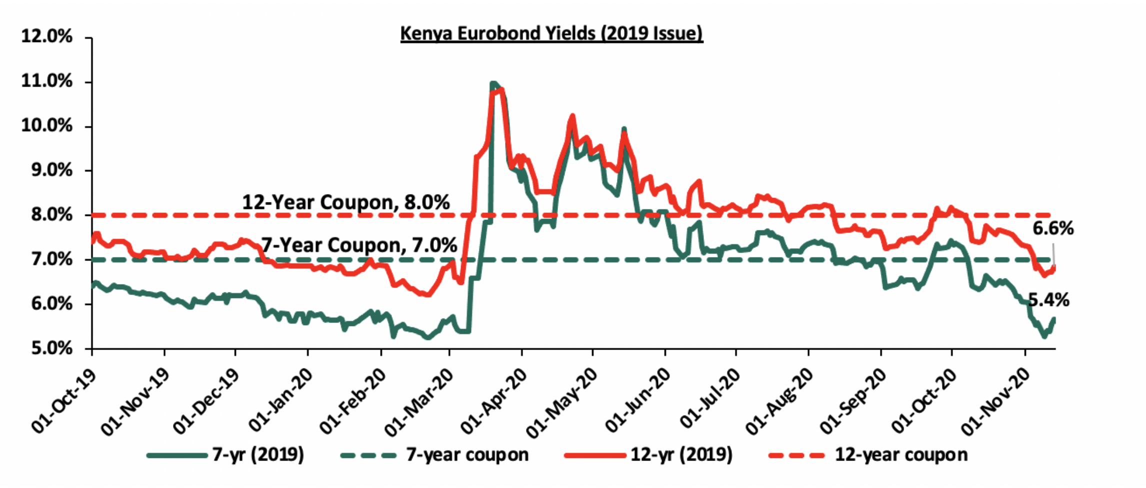
During the week, Kenyan Eurobonds recorded mixed performance with the yield on shorter-dated bond remaining unchanged, while the longer-dated bonds saw a declines in the yields. According to Reuters, the yield on the 10-year Eurobond issued in June 2014 remained unchanged closing the week at 4.7%, as was recorded the previous week.



During the week, the yields on the 10-year and 30-year Eurobonds issued in 2018, on the other hand, declined by 0.2% points and 0.1% points to 5.9% and 7.6%, respectively, from 6.1% and 7.7% recorded previous week.



During the week, the yields on the 2019 dual-tranche Eurobonds increased, with the 7-year Eurobond and the 12-year Eurobond increasing by 0.3% points each to 5.4% and 6.6%, from 5.7% and 6.9% recorded last week.



Kenya Shilling:

During the week, the Kenyan shilling marginally depreciated against the US dollar by 0.3% to Kshs 109.4 from Kshs 109.1, mainly attributable to the persistent dollar demand from general goods importers and low inflows from sectors like tourism. On a YTD basis, the shilling has depreciated by 7.9% against the dollar, in comparison to the 0.5% appreciation in 2019. We expect continued pressures on the Kenyan shilling due to:

i. Demand from merchandise and energy sector importers as they beef up their hard currency positions amid a slowdown in foreign dollar currency inflows, and,
ii. Continued uncertainty globally making people prefer holding dollars and other hard currencies.

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

i. The Forex reserves which are currently at USD 7.9 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, and,
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.
iii. Improving diaspora remittances evidenced by a 17.3% y/y increase to USD 263.1 mn in October 2020, from USD 224.3 mn recorded over the same period in 2019, has cushioned the shilling against further depreciation.

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 November 2020 to 14th December 2020. Below are the key take-outs from the statement:

- Petrol prices have declined by 1.3% to Kshs 105.9 per litre from Kshs 107.3 per litre previously, while diesel prices declined by 2.4% to Kshs 90.7 per litre from Kshs 92.9 per litre. Kerosene prices also declined by 2.5% to Kshs 81.6 per litre from Kshs 83.7 per litre.
- The changes in prices have been attributed to:
  i. A decline in the average landed cost of imported super petrol by 4.5% to USD 316.6 per cubic meter in October from USD 331.7 per cubic meter in September 2020 2020,
  ii. Average landed costs for diesel decreased by 7.4% to USD 288.0 per cubic meter from USD 312.0 per cubic meter in September 2020,

iii. Landed costs for kerosene also decreased by 7.4% to USD 261.2 per cubic meter from USD 282.1 Per cubic meter in September 2020,
iv. A 5.2% decrease in Free on Board (FOB) price of Murban crude oil lifted in October 2020 to USD 40.2 per barrel, from USD 42.4 per barrel in September 2020,
v. The Kenyan shilling depreciation by 0.5% against the dollar to close at Kshs 109.1 in October 2020, from Kshs 108.6 in September 2020.

We expect a slight decline, not only in the transport and fuel index, which carries a weighting of 8.7% in the total consumer price index (CPI), but also on the prices of other commodities such as food prices because of a trickle-down effect due to the lower cost of transport.

The Monetary Policy Committee (MPC) is set to meet on Thursday, 26th November 2020, to review the outcome of its previous policy decisions and recent economic developments, and to decide on the direction of the Central Bank Rate (CBR). In their previous meeting held on 29th September 2020, the committee decided to reconvene in November 2020, while highlighting that they would remain ready to reconvene earlier if necessary, as they continue to closely monitor the impact of the policy measures have had so far. Additionally, the MPC maintained the CBR at 7.0% citing that the accommodative policy stance adopted in March, April and May 2020 sittings was having the intended effects on the economy.

We expect the MPC to maintain the Central Bank Rate (CBR) at 7.0%, with their decision mainly being supported by:

i. Stable inflation within the government's target range of 2.5% -7.5% on account of the stable food prices being experienced in the country as a result of the favourable weather conditions,
ii. There is a lot of liquidity in the money market hence additional cuts are less likely to spur private sector growth given (a) the reduced economic activity in Kenya's key sectors and (b) elevated credit risk resulting to a cautious lending stance by banks, with the possibility of heightened Non Performing Loans if the pandemic is to continue, and,
iii. Additional rate cuts could lead to a further depreciation of the Shilling thus reducing Kenya's attractiveness as an investment destination.

For further analysis on the factors to be considered by the Monetary Policy Committee please see, MPC Note

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 52.0% ahead of its prorated borrowing target of Kshs 187.0 bn having borrowed Kshs 284.3 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.
