Cytonn Monthly - July 2021

Fixed Income

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

During the month of July, T-bill auctions remained oversubscribed, with the overall subscription rate coming in at 106.6%, down from 120.5% recorded in June. Investor demand shifted to the 91-day paper which had the highest subscription rate of 213.4%, up from 143.4% recorded the previous month. Investors' continued interest in the 91-day paper during the month is mainly attributable to the paper's higher return on a risk adjusted basis. The subscription rate for the 182-day papers also increased to 119.7%, up from 75.6%, while the subscription rate for the 364-day declined to 50.8%, from 156.4% recorded in June. The yields on the 364-day, 182-day and 91-day papers declined by 29.7 bps, 36.2 bps and 38.3 bps to 7.4%, 7.0% and 6.5%, respectively. For the month of July, the government accepted a total of Kshs 88.6 bn, out of the Kshs 102.3 bn worth of bids received as they sought to contain the rates.

During the week, T-bills remained undersubscribed, with the overall subscription rate coming in at 74.2%, an increase from the 69.6% recorded the previous week. The 91-day paper recorded the highest subscription rate, receiving bids worth Kshs 8.5 bn against the offered amount of Kshs 4.0 bn, translating to a subscription rate of 212.4%, a decline from the 252.1% recorded the previous week. The subscription rate for the 182-day paper increased to 65.0%, from 32.1% recorded the previous week, while the subscription rate for the 364-day paper declined to 28.1%, from 34.0% recorded the previous week. The yields on the 91-day and 182-day papers increased by 0.9 bps and 1.1 bps to 6.5% and 7.0%, respectively, while the yields on the 364-day paper declined by 0.6 bps to 7.4%. The government continued to take advantage of the low yields and the high liquidity in the market by accepting Kshs 17.7 bn out of the Kshs 17.8 bn worth of bids received, translating to an acceptance rate of 99.7%.

In the Primary Bond Market, the three bonds reopened by the government for the month of July recorded a subscription of 194.9%, attributable to the high liquidity in the market. The government sought to raise Kshs 60.0 bn in the three bonds and accepted Kshs 79.9 bn out of the Kshs 116.9 bn worth of bids received, translating to an acceptance rate of 68.4%. Investors preferred the shorter dated paper, FXD1/2012/15, with an effective tenor of 6.2 years, which received bids worth Kshs 48.8 bn, FXD1/2021/25 received bids worth Kshs 39.9 bn while FXD1/2018/15 received bids worth Kshs 28.2 bn. The three bonds had coupon rates of 11.0%, 12.7% and 13.9%, and the weighted average yields were 11.6%, 12.6% and 13.9% for FXD1/2012/15, FXD1/2018/15 and FXD1/2021/25, respectively.

During the week, the government reopened two bonds, FXD3/2019/10 and FXD1/2018/20 and a primary issue on FXD1/2021/20, with effective tenors of 7.5 years, 14.6 years and 20.0 years, respectively, whose offer period ends on 10th August 2021. The coupon rates are 11.5% for FXD3/2019/10 and 13.2% for FXD1/2018/20, while the coupon on FXD1/2021/20 will be market determined. We expect investors to prefer the longer dated papers, FXD1/2018/20 and FXD1/2021/20, as they search for higher yields given the low yields in the currently in the market. Our recommended bidding range for the three bonds are: 11.9%-12.2% for FXD3/2019/10, 12.8%-13.2% for FXD1/2018/20 and 13.1%-13.4% for FXD1/2021/20.

In the money markets, 3-month bank placements ended at 7.7% (based on what we have been offered by various banks), while the 91-day T-bill increased by 0.9 bps to 6.5%. The average yield of the Top 5 Money Market Funds remained unchanged at 9.8% as was recorded the previous week. Additionally, the yield on the Cytonn Money Market (CMMF) also remained unchanged at 10.6% as was recorded the previous week.

The table below shows the Money Market Fund Yields for Kenyan Fund Managers as published on 30th July 2021:

Money Market Fund Yield for Fund Managers as published on 30th July 2021

Rank	Fund Manager	Daily Yield	Effective Annual Rate
1	Cytonn Money Market Fund	10.06%	10.58%
2	Nabo Africa Money Market Fund	9.52%	9.95%
3	Zimele Money Market Fund	9.56%	9.91%
4	CIC Money Market Fund	9.02%	9.35%
5	Sanlam Money Market Fund	8.85%	9.25%
6	Madison Money Market Fund	8.84%	9.24%
7	Orient Kasha Money Market Fund	8.70%	9.06%
8	Co-op Money Market Fund	8.34%	8.70%
9	Dry Associates Money Market Fund	8.36%	8.69%
10	GenCap Hela Imara Money Market Fund	8.20%	8.55%
11	British-American Money Market Fund	8.19%	8.50%
12	ICEA Lion Money Market Fund	8.05%	8.39%
13	NCBA Money Market Fund	8.04%	8.34%
14	Apollo Money Market Fund	8.40%	8.27%
15	Old Mutual Money Market Fund	7.11%	7.35%
16	AA Kenya Shillings Fund	6.63%	6.83%

Source: Business Daily

Secondary Bond Market:

In the month of July, the yields on government securities in the secondary market remained relatively stable with the FTSE NSE bond index declining by 0.3%, to close the month at 96.5, bringing the YTD performance to a decline of 1.6%. The bond turnover declined by 0.5% to Kshs 91.4 bn, from Kshs 91.8 bn recorded in June. The total amounts of bonds transacted on a year to date basis stands at Kshs 542.4 bn compared to Kshs 355.9 bn transacted over a similar period last year. The chart below is the yield curve movement during the period;

Liquidity:

The money markets remained liquid in the month of July, with the average interbank rate declining to 4.0%, from 4.6% recorded in June supported by government payments. During the week, liquidity in the money market eased, with the average interbank rate declining to 3.2%, from 3.5% recorded the previous week, due to government payments, Term Auction Deposits (TADs) maturities worth Kshs 154.3 bn which offset the settlements of government securities and tax remittances. The average interbank volumes traded declined by 11.2% to Kshs 4.1 bn, from Kshs 4.6 bn recorded the previous week.

Kenya Eurobonds:

During the month, the yields on the Eurobonds recorded mixed performance with the 10-year Eurobond issued in 2014, 30-year issued in 2018 and 12-year issued in 2021 all declining marginally by 0.1% points to 3.2%, 7.3% and 6.2%, respectively. On the other hand, the 7-year and 12-year Eurobonds issued in 2019 and the 10-year Eurobond issued in 2018, remained unchanged at 4.8%, 6.2% and 5.4%, respectively.

During the week, the yields on the Eurobonds recorded mixed performance with the yields on the 10-year Eurobond issued in 2018 increasing marginally by 0.1% points to 5.4%. On the other hand, the yields on the 10-year Eurobond issued in 2014, 30-year Eurobond issued in 2018, 7- year Eurobond issued in 2019, 12- year Eurobond issued in 2019 and the 12- year Eurobond issued in 2021 remained unchanged at 3.2%, 7.3%, 4.8%, 6.2% and 6.2%, respectively. Below is a summary of the performance:

Kenya Eurobond Performance

	2014	2018		2019		2021
Date	**10-year issue**	**10-year issue**	**30-year issue**	**7-year issue**	**12-year issue**	**12-year issue**
31-Dec-20	3.9%	5.2%	7.0%	4.9%	5.9%	-
30-Jun-21	3.3%	5.4%	7.4%	4.8%	6.3%	6.3%
23-Jul-21	3.2%	5.3%	7.3%	4.8%	6.2%	6.2%
26-Jul-21	3.2%	5.3%	7.3%	4.8%	6.2%	6.2%
27-Jul-21	3.2%	5.4%	7.3%	4.8%	6.2%	6.2%
28-Jul-21	3.2%	5.4%	7.3%	4.8%	6.2%	6.2%
29-Jul-21	3.2%	5.3%	7.3%	4.8%	6.2%	6.2%
30-Jul-21	3.2%	5.4%	7.3%	4.8%	6.2%	6.2%
Weekly Change	**0.0%**	**0.1%**	**0.0%**	**0.0%**	**0.0%**	**0.0%**
MTD Change	**(0.1%)**	**0.0%**	**(0.1%)**	**0.0%**	**0.0%**	**(0.1%)**
YTD Change	**(0.7%)**	**0.2%**	**0.3%**	**(0.1%)**	**0.3%**	**-**

Source: Reuters

Kenya Shilling:

During the month, the Kenya Shilling depreciated by 0.7% against the US Dollar to close the month at Kshs 108.6, from Kshs 107.9 recorded at the end of June 2021, mostly attributable to increased dollar demand from general importers.

During the week, the Kenyan shilling depreciated by 0.4% against the US dollar to close the week at

Kshs 108.6, from Kshs 108.2 recorded the previous week partly attributable to the build-up of dollar demand from energy importers as they meet their end of the month hard currency obligations. On a YTD basis, the shilling has appreciated by 0.5% against the dollar, in comparison to the 7.7% depreciation recorded in 2020. Despite the recent appreciation of the shilling, we expect the shilling to remain under pressure in 2021 as a result of:

a. Rising uncertainties in the global market due to the Coronavirus pandemic, which has seen investors continue to prefer holding their investments in dollars and other hard currencies and commodities,
b. The widened current account position which increased by 0.2% points to 5.4% of GDP in the 12 months to June 2021 from 5.2% of GDP for a similar period in 2020, and,
c. Demand from merchandise traders as they beef up their hard currency positions in anticipation for more trading partners reopening their economies globally.

The shilling is however expected to be supported by:

i. The Forex reserves, currently at USD 9.3 bn (equivalent to 5.7 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. Improving diaspora remittances evidenced by a 6.0% y/y increase to USD 305.9 mn in June 2021, from USD 288.5 mn recorded over the same period in 2020, which has continued to cushion the shilling against further depreciation.

Weekly Highlights:

I. **July MPC Meeting**

The Monetary Policy Committee (MPC) met on Wednesday, 28th July 2021 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). The MPC retained the CBR at 7.00%, in line with our expectations, for the ninth consecutive time. Below are some of the key highlights from the meeting:

i. Inflation remains well anchored and within the Government’s target range of 2.5%-7.5%. The overall inflation stood at 6.3% in June 2021 compared to 5.9% in May, mainly attributable to increase in food and fuel prices,
ii. Private sector credit growth has been recovering having grown by 7.7% in June 2021 as compared to 6.8% in April 2021. The key sectors supporting this growth include manufacturing (8.1%), transport and communications (11.8%), and consumer durables (23.4%), and,
iii. The current account deficit to GDP is estimated at 5.4% in the 12-months to June 2021, a 0.2% points increase, from 5.2% recorded over a similar period in 2020. Exports of goods remained strong, growing by 11.1% in H1’2021 compared to a similar period in 2020. Receipts from exports of horticulture and manufactured goods increased by 29.4% and 45.2%, respectively, in H1’2021 compared to a similar period in 2020. However, receipts from tea exports declined by 5.5 %, partly attributable to the impact of accelerated purchases in 2020.

The MPC concluded that the current accommodative monetary policy stance remains appropriate and therefore decided to retain the Central Bank Rate (CBR) at 7.00%. The Committee will meet again in September 2021, but remains ready to re-convene earlier if necessary.

II. **July Inflation**

The y/y inflation for the month of July increased to 6.4%, from the 6.3% recorded in June, in line with our expectations. Key to note, this is the highest reading since a similar reading of 6.4% was recorded in February, 2020. The increase was mainly attributable to the increase in the y/y food and non-alcoholic beverages, housing, utilities and other fuels and transport inflation prices.

Notably, the information and communication inflation increased the most on an m/m basis, mainly attributable to the introduction of additional taxes on mobile phone airtime, which were effective from 1st July, 2021. However, the increase was mitigated by a decline in the food inflation. The table below shows a summary of both the year on year and month on month commodity groups' performance;

Major Inflation Changes – July 2021

Broad Commodity Group	Price change m/m (July- 21/June -21)	Price change y/y (July-21/June-20)	Reason
Food & Non-Alcoholic Beverages	(0.5%)	8.8%	The m/m decline was mainly contributed by decline in prices of tomatoes, white bread and oranges among other food items
Housing, Water, Electricity, Gas and other Fuel	1.3%	6.3%	The m/m increase was as a result of increase in the price of cooking Gas (LPG) and electricity
Transport Cost	0.0%	10.3%	There was no m/m change due to the pump prices of petrol remaining unchanged between June and July
Overall Inflation	**0.2%**	**6.4%**	**The m/m increase was due to a 1.8% increase in the information and communication cost, mainly driven by the increase in prices of mobile phone airtime**

Source: KNBS

Going forward, we expect the inflation to remain within the government's set range of 2.5% - 7.5%. However, we also anticipate the inflation pressures to remain elevated in the short term mainly driven by increases in food and fuel prices, and the impact of the recently implemented tax measures. The rising inflation remains a concern as the IMF has already cautioned the government against exceeding the set target rate as this will increase the risk of an inability to access further credit facilities from the international lender. The increasing inflation is also eroding the real rate of return to investors given the declining yields in government securities, for example; an investor's real return in a 364-day paper has been reduced to only 1.0% given the yield is currently at 7.4% against an inflation rate of 6.4%.

Monthly Highlights:

i. The Energy and Petroleum Regulatory Authority (EPRA) released their monthly statement on themaximum wholesale and retail prices for fuel prices in Kenya effective 15th July 2021 to 14th August 2021. The prices of Super Petrol, Diesel and Kerosene remained unchanged at Kshs 127.1 per litre, Kshs 107.7 per litre, and Kshs 97.9 per litre, respectively, despite increased landed cost of imported crude. For more information, see our Cytonn Weekly #28/2021.
ii. The Kenya Revenue Authority (KRA) released the FY'2020/2021 revenue performance, highlighting that the total revenue collected was Kshs 1.67 tn, against the revised target of Kshs 1.65 tn, representing an out-performance rate of 101.0%. This is despite the challenges posed by the COVID-19 pandemic on business conditions and people's income. For more information, see our Cytonn Weekly #27/2021,
iii. The headline Purchasing Managers' Index (PMI)for the month of June 2021 decreased to 51.0 from the 52.5 recorded in May 2021, indicating that the business conditions in the Kenyan private sector recorded an expansion but at a slower rate than that seen in May 2021. For more information, For more information, see our Cytonn Weekly #27/2021, and,

iv. The World Bank Board of Executive Directors approveda USD 130.0 mn (Kshs 14.0 bn) additional loan financing for the Kenya COVID-19 Health Emergency Response Project to facilitate affordable and equitable access to COVID-19 vaccines for Kenyans. The funding will enable Kenya to procure more vaccines through the African Vaccine Acquisition Task Team (Avatt) and the COVID-19 Vaccines Global Access (Covax) facilities in addition to supporting the deployment of the vaccines by boosting the country's cold-storage capacity. For more information, see our Cytonn Weekly #26/2021,

Rates in the fixed income market have remained relatively stable due the sufficient levels of liquidity in the money market, coupled with the discipline by the Central Bank to reject expensive bids. The government is 34.1% behind its prorated borrowing target of Kshs 63.3 bn having borrowed Kshs 41.7 bn in FY'2021/2022. We expect a gradual economic recovery going into FY'2021/2022 as evidenced by KRA collecting Kshs 1.7 tn in FY'2020/2021, a 3.9% increase from Kshs 1.6 tn collected in the prior fiscal year. However, despite the projected high budget deficit of 7.5% and the lower credit rating from S&P Global to 'B' from 'B+', we believe that the monetary support from the IMF and World Bank will mean that the interest rate environment may stabilize since the government will not be desperate for cash.