Cytonn Monthly – August 2021

Fixed Income

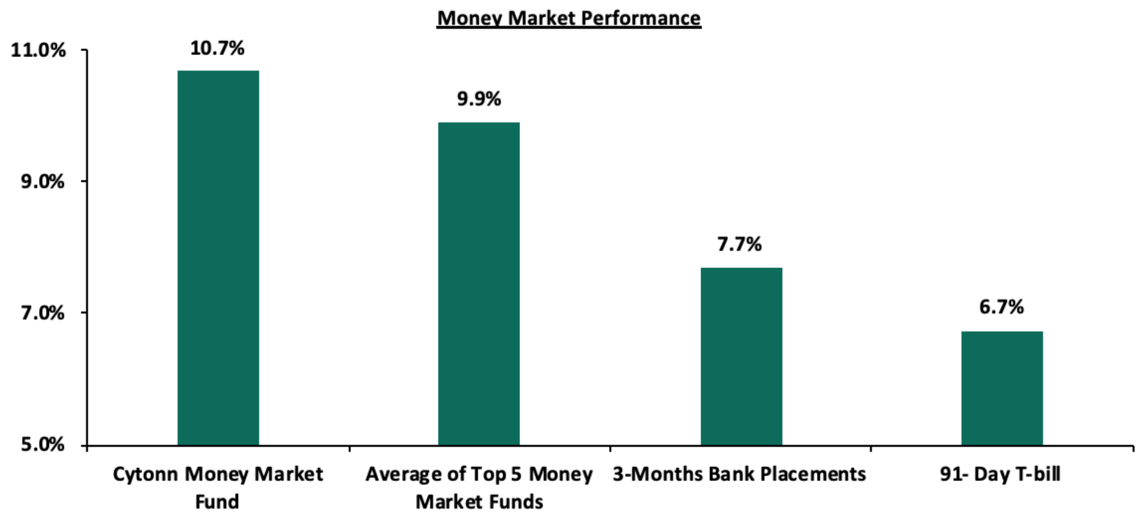
Money Markets, T-Bills & T-Bonds Primary Auction:

During the month of August, T-bills recorded an undersubscription, with the overall subscription rate coming in at 36.5%, down from 106.6% recorded in July, as investors shifted their interest to the bonds market in search of higher returns. Investors' demand shifted to the 364-day paper which recorded the highest subscription rate of 49.6%, down from 50.8% recorded the previous month. On the other hand, the subscription rate for the 91-day and 182-day papers declined to 20.2% and 44.2%, from 213.4% and 119.7% recorded the previous month, respectively. The yields on the 91-day, 182-day and 364-day papers increased by 26.4 bps, 24.0 bps and 6.0 bps to 6.7%, 7.2% and 7.6%, respectively. For the month of August, the government accepted a total of Kshs 83.9 bn, out of the Kshs 85.9 bn worth of bids received as they sought to contain the rates. This translated to a 97.7% acceptance rate.

During the week, T-bills were slightly undersubscribed, with the overall subscription rate coming in at 99.5%, up from the 36.5% recorded the previous week attributable to the eased liquidity in the market as evidenced by the 0.1% points decline in the interbank rates. The 91-day paper recorded the highest subscription rate of 100.8% an increase from the 20.2% recorded the previous week, receiving bids worth Kshs 4.03 bn against the offered Kshs 4.00 bn. The subscription rate for the 182-day and the 364-day papers increased to 99.5% and 98.9%, from 44.2% and 49.6% recorded the previous week, respectively. The yields on the 91-day, 182-day and 364-day papers increased by 3.3 bps, 3.1 bps and 2.5 bps to 6.8%, 7.2% and 7.5%, respectively. The government accepted all Kshs 23.9 bn bids received, translating to an acceptance rate of 100.0%.

In the Primary Bond Market, the government offered three bonds namely; FXD3/2019/10, FXD1/2018/20 and FXD1/2021/20 for the month of August, which recorded a subscription rate of 174.4% attributable to the high liquidity in the market and the investors' appetite for higher yields. The government sought to raise Kshs 60.0 bn in the three bonds and accepted Kshs 80.3 bn out of the Kshs 104.6 bn worth of bids received, translating to an acceptance rate of 76.7%. Investors preferred the longer dated paper, FXD1/2021/20 which received bids worth Kshs 43.5 bn. FXD3/2019/10 received bids worth Kshs 38.3 bn while FXD1/2018/20 received bids worth Kshs 22.8 bn. The coupons for the three bonds were 11.5%, 13.2% and 13.4%, and the weighted average yield rates during the issues were 12.3%, 13.3% and 13.5% for FXD3/2019/10, FXD1/2018/20 and FXD1/2021/20, respectively.

For the month of September, the government is seeking to raise Kshs 75.0 bn for infrastructure projects by opening an infrastructure bond, IFB1/2021/21, with a tenor of 21 years whose offer period ends on 7th September 2021. Key to note, the bond's coupon rate will be market determined. Given the eased liquidity in the market coupled with the government's increased appetite for domestic borrowing as well as the attractive tax-free nature of the infrastructure bond, we anticipate an oversubscription and a higher acceptance rate. Our recommended bidding range for the bond is: 11.8%-12.0% within which bonds of a similar tenor are trading and given that this is a tax free bond it translates to a return of around 14.0%.



In the money markets, 3-month bank placements ended the week at 7.7% (based on what we have been offered by various banks), while the yield on the 91-day T-bill increased by 3.3 bps to 6.8%. The average yield of the Top 5 Money Market Funds declined by 0.8% points to 9.9% from 10.7% recorded the previous week. The yield on the Cytonn Money Market Fund increased by 0.1% points to 10.7%, from 10.6% recorded last week.

The table below shows the Money Market Fund Yields for Kenyan Fund Managers as published on 3rd September 2021:

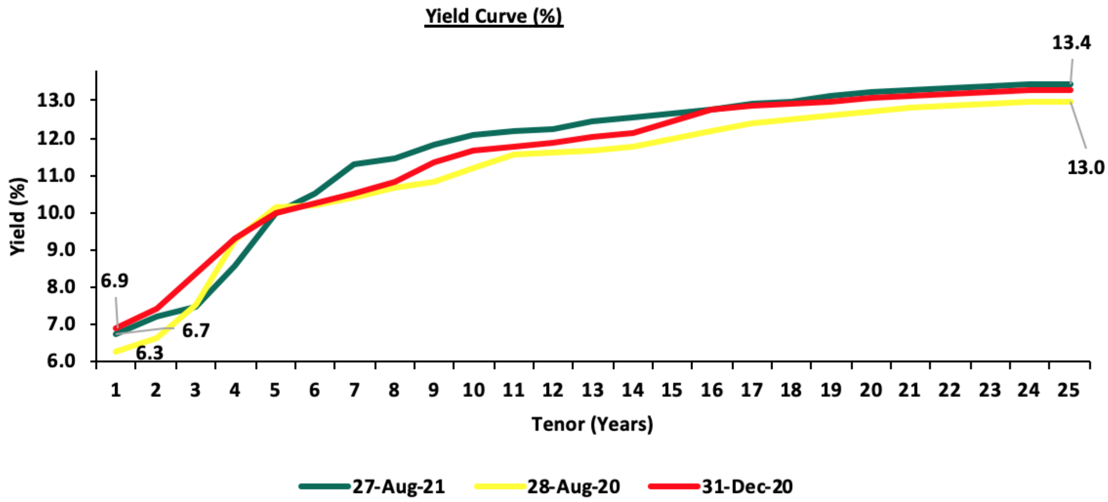
Money Market Fund Yield for Fund Managers as published on 3rd September 2021

Rank	Fund Manager	Daily Yield	Effective Annual Rate
1	Cytonn Money Market Fund	10.15%	10.68%
2	Nabo Africa Money Market Fund	9.70%	10.18%
3	Zimele Money Market Fund	9.56%	9.91%
4	Madison Money Market Fund	9.06%	9.48%
5	Sanlam Money Market Fund	8.87%	9.28%
6	CIC Money Market Fund	8.70%	9.01%
7	Apollo Money Market Fund	9.10%	8.95%
8	Dry Associates Money Market Fund	8.44%	8.77%
9	Co-op Money Market Fund	8.32%	8.68%
10	Orient Kasha Money Market Fund	8.16%	8.50%
11	British-American Money Market Fund	8.12%	8.43%
12	ICEA Lion Money Market Fund	8.05%	8.38%
13	NCBA Money Market Fund	8.03%	8.34%
14	GenCapHela Imara Money Market Fund	8.00%	8.33%
15	Old Mutual Money Market Fund	7.43%	7.19%
16	AA Kenya Shillings Fund	6.53%	6.73%

Source: Business Daily

Secondary Bond Market:

In the month of August, the yields on government securities in the secondary market remained relatively stable with the FTSE NSE bond index increasing marginally by 0.1%, to close the month at Kshs 96.6, bringing the YTD performance to a decline of 1.4%. The secondary bond turnover declined by 9.1% to Kshs 83.1 bn, from Kshs 91.4 bn recorded in July. On a year on year basis, bonds turnover increased by 47.8% to Kshs 625.5 bn from Kshs 423.3 bn worth of T-bonds 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 August, with the average interbank rate declining to 3.2%, from 3.9% recorded in July mainly supported by government payments inclusive of Kshs 305.9 bn Term Auction deposits maturities (TADs). During the week, liquidity in the money market eased, with the average interbank rate declining marginally to 3.4%, from 3.5% recorded the previous week, due to government payments, TADs maturities worth Kshs 43.0 bn which offset the settlements of government securities and tax remittances. The average interbank volumes traded increased by 45.7% to Kshs 11.2 bn, from Kshs 7.7 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, 10-year and 30-year issued in 2018 and 12-year bonds issued in 2019 and 2021 all declining by 0.2% points to 3.1%, 5.0%, 7.1%, and 6.0%, respectively. On the other hand, the 7-year Eurobond issued in 2019 remained unchanged at 4.6%.

During the week, the yields on the Eurobonds were on a downward trajectory with the yields on the 10-year Eurobond issued in 2014 and 2018 decreasing by 0.1% and 0.4% points to 3.1% and 4.9%, respectively while the yields on the 30-year Eurobond issued in 2018, 7-year and 12-year Eurobonds issued in 2019 all declined by 0.2% to 7.1%, 4.6% and 6.0%, respectively. The 12- year Eurobond issued in 2021 declined by 0.3% to 5.9%. 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%	-
31-Jul-21	3.3%	5.2%	7.3%	4.6%	6.2%	6.2%
27-Aug-21	3.2%	5.3%	7.3%	4.8%	6.2%	6.2%
30-Aug-21	3.0%	5.1%	7.2%	4.8%	6.2%	6.0%

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-Aug-21	3.1%	5.0%	7.1%	4.6%	6.0%	5.9%
01-Se[-21	3.1%	4.9%	7.1%	4.6%	6.0%	5.9%
02-Sep-21	3.0%	4.9%	7.1%	4.6%	6.0%	5.9%
03-Sep-21	3.1%	4.9%	7.1%	4.6%	6.0%	5.9%
Weekly Change	(0.1%)	(0.4%)	(0.2%)	(0.2%)	(0.2%)	(0.3%)
MTD Change	0.0%	(0.1%)	0.0%	0.0%	0.0%	0.0%
YTD Change	(0.8%)	(0.3%)	0.1%	(0.3%)	0.1%	-

Source: Reuters

Kenya Shilling:

During the month, the Kenya Shilling depreciated by 1.2% against the US Dollar to close the month at Kshs 109.9, from Kshs 108.6 recorded at the end of July 2021, mostly attributable to increased dollar demand from general importers outweighing the supply of dollars from importers.

During the week, the Kenyan shilling depreciated by 0.2% against the US dollar to close the week at Kshs 109.9, from Kshs 109.8 recorded the previous week, mainly attributable to increased dollar demand from general importers. On a YTD basis, the shilling has depreciated by 0.7% against the dollar, in comparison to the 7.7% depreciation recorded in 2020. We expect the shilling to remain under pressure for the remainder of 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 0.5% points to 5.4% of GDP in the 12 months to July 2021 from 4.9% of GDP for a similar period in 2020, and,
c. Demand from energy importers as they beef up their hard currency positions in the prevailing elevated global oil prices.

The shilling is however expected to be supported by:

i. The Forex reserves, currently at USD 8.9 bn (equivalent to 5.4 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 21.6% y/y increase to USD 336.7 mn in July 2021, from USD 277.0 mn recorded over the same period in 2020, which has continued to cushion the shilling against further depreciation.

Weekly Highlights:

I. August Inflation

The y/y inflation for the month of August increased marginally to 6.57%, from the 6.55% recorded in July, in line with our expectations. This is the highest reading since the pandemic begun. The increase was mainly attributable to the increase in the y/y food and non-alcoholic beverages, transport, Housing, water, electricity, gas and other Fuels inflation prices which increased by 10.7%, 7.9 and 5.1% respectively . Food and non-alcoholic beverages index has had the greatest increase year on year as well as on a month on month basis due to the increased food prices as food supply is lower given the erratic weather.

However, the increase was mitigated by a decline in the transport inflation. The table below shows a summary of both the year on year and month on month commodity groups' performance;

Major Inflation Changes – August 2021

Broad Commodity Group	Price change m/m (August-21/July-21)	Price change y/y (August-21/August-20)	Reason
Food & Non-Alcoholic Beverages	0.5%	10.7%	The m/m increase was mainly contributed by increase in prices of cabbages, spinach and oranges among other food items. The increase was however mitigated by a decline in prices of potatoes and onions
Housing, Water, Electricity, Gas and other Fuel	0.3%	5.1%	The m/m increase was as a result of increase in the price cooking fuel and house rent despite the slight decrease in the price of electricity
Transport Cost	(0.3%)	7.9%	The m/m decrease in bus fare of country and city public service vehicles following the return to carrying of full capacity for public service vehicles in the month of August 2021
Overall Inflation	0.1%	6.6%	The m/m increase was due to a 0.5% increase in the food and non-alcoholic beverages as compared to the 0.5% decline in the month of June

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 Inflation pressures to remain elevated in the short term mainly driven by increases in food prices, and the impact of the increase in tariffs and taxes as we foresee a concurrent contribution to the increase in the headline inflation, despite the government's interventions through unchanged fuel prices. 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. We anticipate continued pressure on the government to keep the inflation under control before the next IMF evaluation test date which is in December 2021. Additionally, the recently issued communication by KRA on inflation adjustment on Specific Rates of Excise Duty effective from 1st October 2021 will cause an upward pressure on the inflation rate in the coming months, as the burden will be passed to the consumers.

Monthly Highlights:

i. The National Treasury gazetted the revenue and net expenditures for the first month of FY'2021/2022, ending 31st July 2021, highlighting that the total revenue collected as at the end of July 2021 amounted to Kshs 267.1 bn, equivalent to 8.4% of the FY'2021/2022 target of Kshs 3.2 tn while the total expenditure amounted to Kshs 170.4 bn, equivalent to 5.3% of the budget of Kshs 3.2 tn. For more information, see our Cytonn Weekly #33/2021, and,
ii. The headline Purchasing Managers' Index (PMI) for the month of July 2021 decreased to 50.6 from the 51.0 recorded in June 2021, which was a second decline in a row, indicating that the business conditions in the Kenyan private sector recorded an expansion but at a slower rate than that seen in June 2021. For more information, see our Cytonn Weekly #31/2021.

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 33.8% ahead of its prorated borrowing target of Kshs 126.6 bn having borrowed Kshs 169.5 bn of the Kshs 658.5 bn borrowing for the FY'2021/2022. We expect a gradual economic recovery going into FY'2021/2022 as evidenced by the KRA July collections of Kshs 267.1 bn compared to the monthly prorated amount of Kshs 266.0 bn. 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.
