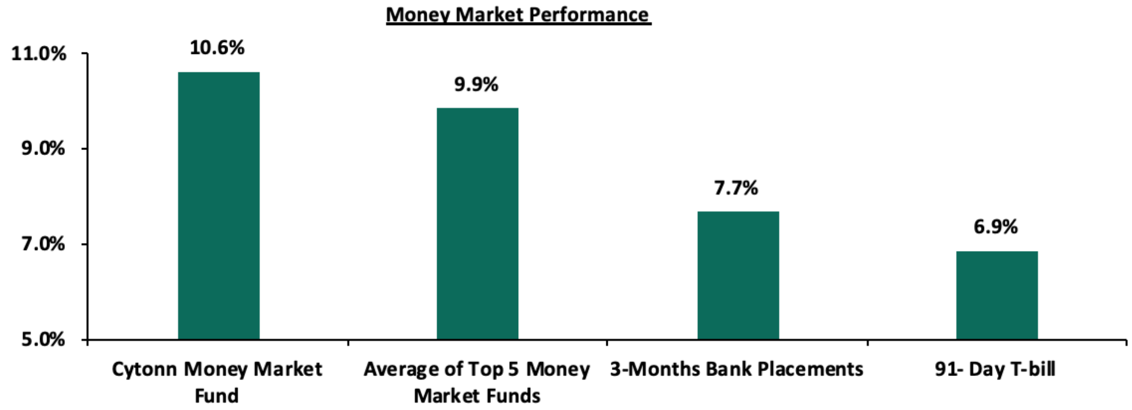
Kenya Retail Report 2021, & Cytonn Weekly #38/2021

Fixed Income

During the week, T-bills remained undersubscribed, with the overall subscription rate coming in at 42.3%, down from the 54.6% recorded the previous week. The 91-day paper recorded the highest subscription rate, receiving bids worth Kshs 4.9 bn against the offered Kshs 4.0 bn, translating to a subscription rate of 119.8%, an increase from the 83.8% recorded the previous week. The subscription rate for the 182-day paper declined to 46.7%, from 68.0%, while that of the 364-day paper declined significantly to 7.0%, from the 29.5% recorded the previous week. The yields on the 91-day, 182-day and 364-day papers increased by 2.6 bps, 3.2 bps and 4.5 bps to 6.9%, 7.3% and 7.9%, respectively. The government accepted all the Kshs 10.2 bn worth of bids received, translating to an acceptance rate of 100.0%.

In the Primary Market, the government reopened three bonds, FXD1/2013/15, FXD3/2019/15 and FXD1/2021/25, with effective tenors of 6.4 years, 12.9 years and 24.7 years, respectively, in a bid to raise Kshs 60.0 bn for budgetary support. The coupon rates are 11.3% for FXD1/2013/15, 12.3% for FXD3/2019/15 and 13.9% for FXD1/2021/25. We expect investors to prefer the longer dated papers, FXD3/2019/15 and FXD1/2021/25, as they search for higher yields. The bonds are currently trading in the secondary market at yields of 11.7%, 12.7% and 13.5%, for FXD1/2013/15, FXD3/2019/15 and FXD1/2021/25, respectively, and as such, our recommended bidding range for the three bonds are: 11.5%-11.8% for FXD1/2013/15, 12.3%-12.7% for FXD3/2019/15 and 13.2%-13.5% for FXD1/2021/25. The period of the sale runs until 5th October 2021.



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 2.6 bps to 6.9%. The average yield of the Top 5 Money Market Funds increased marginally by 0.1% points to 9.9%, from 9.8% recorded the previous week. The yield on the Cytonn Money Market Fund 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 24th September 2021:

Money Market Fund Yield for Fund Managers as published on 24th September 2021

Rank	Fund Manager	Daily Yield	Effective Annual Rate
1	Cytonn Money Market Fund	10.10%	10.63%
2	Nabo Africa Money Market Fund	9.70%	10.18%
3	Zimele Money Market Fund	9.56%	9.91%
4	Sanlam Money Market Fund	9.04%	9.46%
5	Madison Money Market Fund	8.72%	9.11%
6	CIC Money Market Fund	8.69%	8.99%
7	Apollo Money Market Fund	9.10%	8.95%
8	Dry Associates Money Market Fund	8.46%	8.80%
9	GenCapHela Imara Money Market Fund	8.38%	8.74%
10	Co-op Money Market Fund	8.31%	8.66%
11	Orient Kasha Money Market Fund	8.21%	8.55%
12	British-American Money Market Fund	8.16%	8.47%
13	ICEA Lion Money Market Fund	8.00%	8.33%
14	NCBA Money Market Fund	8.02%	8.33%
15	Old Mutual Money Market Fund	7.11%	7.35%
16	AA Kenya Shillings Fund	6.50%	6.70%

Source: Business Daily

Liquidity:

During the week, liquidity in the money markets tightened, with the average interbank rate increasing by 2.0% points to 6.1%, from 4.1% recorded the previous week, partly attributable to the tax remittances which offset government payments made during the week. The average interbank volumes declined by 2.0% to Kshs 16.9 bn, from Kshs 17.2 bn recorded the previous week.

Kenya Eurobonds:

During the week, yields on all the Eurobonds increased marginally, with the yields on the 10-year bond issued in 2018, 30-year issued in 2018, 7-year issued in 2019, and 12-year bond issued in 2019 all increasing by 0.2% points to 5.3%, 7.4%, 5.0%, and 6.4%,respectively. Yields on the 10-year bond issued in 2014 increased by 0.1% to 3.1% while yield on the 12-year bond issued to 6.4%. 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-Aug-21	3.1%	5.0%	7.1%	4.6%	6.0%	5.9%
17-Sep-21	3.0%	5.1%	7.2%	4.8%	6.2%	6.1%

Kenya Eurobond Performance

Date	2014 10-year issue	2018 10-year issue	2018 30-year issue	2019 7-year issue	2019 12-year issue	2021 12-year issue
20-Sep-21	3.0%	5.2%	7.3%	4.9%	6.3%	6.3%
21-Sep-21	3.0%	5.1%	7.3%	4.9%	6.3%	6.2%
22-Sep-21	3.1%	5.2%	7.3%	4.9%	6.3%	6.3%
23-Sep-21	3.1%	5.3%	7.4%	5.0%	6.4%	6.4%
Weekly Change	**0.1%**	**0.2%**	**0.2%**	**0.2%**	**0.2%**	**0.3%**
MTD Change	**0.0%**	**0.3%**	**0.3%**	**0.4%**	**0.4%**	**0.5%**
YTD Change	**(0.8%)**	**0.2%**	**0.4%**	**0.1%**	**0.4%**	**-**

Source: CBK Weekly Bulletin

Kenya Shilling:

During the week, the Kenyan shilling depreciated marginally by 0.3% against the US dollar to close the week at Kshs 110.4, from Kshs 110.1 recorded the previous week, mainly attributable to increased dollar demand from oil and general merchandise importers. On a YTD basis, the shilling has depreciated by 1.1% 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 August 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 9.5 bn (equivalent to 5.8 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 14.2% y/y increase to USD 312.9 mn in August 2021, from USD 274.1 mn recorded over the same period in 2020, which has continued to cushion the shilling against further depreciation.

Weekly Highlight

I. **September MPC Meeting**

The Monetary Policy Committee (MPC) is set to meet on Tuesday, 28th September to review the outcome and effectiveness of its previous policy decisions and recent economic developments, and to decide on the direction of the Central Bank Rate (CBR) and any other policy measure like the Cash Reserve Ratio (CRR). In their previous meeting held on 28th July 2021, the committee maintained the CBR at 7.00%, in line with our expectations, citing that the accommodative policy stance adopted in March 2020 and all other sittings ever since, remained appropriate and were having the desired effects on the economy. We expect the MPC to maintain the Central Bank Rate (CBR) at 7.00% and to closely monitor the rising inflation rates. Some of the key driving factors shall include;

i. Inflation remaining within the government's target range of 2.5% - 7.5%. August's inflation stood at 6.6%, the highest reading since the pandemic began. We anticipate the Inflation pressures to remain elevated in the short term mainly driven by increases in food and fuel prices as well as the impact of the increase in tariffs and taxes as we foresee a concurrent contribution to the increase in the headline inflation. With the possibility of further fuel price increases, we might see an even higher inflation figure in the coming months as the cost of living remains elevated.,
ii. The need to support the economy and credit growth in the private sector. The current macro and business environment fundamentals might constrain the transmission of further easing, despite the need to stimulate economic growth. Kenya's private sector credit growth in July 2021 stood at 7.7%, below CBK's target of 10.2% by December 2021, an indication of the cautious lending by banks towards the Private Sector. We therefore believe that any additional rate cuts will not lead to a rise in private sector credit growth as banks will prefer lending to the government, and,
iii. The need to refine macroeconomic modelling and forecasting frameworks to reflect the economy's changing structure. Similar measures include improving the interbank market's functioning to strengthen monetary policy transmission and operations, and improving public understanding of monetary policy decisions. We expect this to support better anchoring of inflation expectations in view of the changing economic and financial environment.
iv. The shilling has remained range bound and therefore the need to ensure that the shilling is balanced and there is no significant pressure on it is key.

For a more detailed analysis, please see our MPC note here.

II. **September Inflation Projections**

We are projecting the y/y inflation rate for September 2021 to fall within the range of 6.6% - 7.0%. The key drivers include:

i. The recent hike in fuel prices, with Super Petrol prices increasing by 6.0% to Kshs 134.7 per litre, from Kshs 127.1 per litre. Diesel and Kerosene prices also increased by 7.4% and 13.2%, respectively to Kshs 115.6 and Kshs 110.8 per litre, from Kshs 107.7 and Kshs 97.9 per litre, respectively. With fuel being a major contributor to Kenya's headline inflation, the increase in fuel prices is expected to have a ripple effect in increasing the prices of other contributors to the consumer price index like food and transport,
ii. Increase in food and non-alcoholic drinks prices, which have the largest weighting in the consumer price index at 32.9%, attributable to an increase in imported components like cooking oil and below average rainfall recorded in most parts of the country, and,
iii. Upward readjustment of the fuel cost charge on electricity bills by 2.9% to Kshs 3.9 per Kilowatt hour (KWh) from Kshs 3.8 per Kilowatt hour (KWh) and foreign exchange fluctuation tariff for electricity usage to 76.0 cents per Kilowatt hour (KWh) in September from 68.0 cents per Kilowatt hour (KWh) in August. The readjustment will increase the cost of electricity consumption for households.

Going forward, we expect the inflation rate to remain within the government's set range of 2.5% - 7.5%. However, our concern on the inflation rate nearing the upper limit of 7.5% persists, driven by increases in fuel and food prices which are major contributors to Kenya's headline inflation. Should the increase in inflation persist, the CBK and the Government may have to intervene with monetary and fiscal policies in-order to comply with the conditions set by the IMF, in the Extended Credit facility agreement between the IMF and the Government in February 2021. In the agreement, IMF indicated that Kenya's inflation should remain well anchored and between the government target range so that Kenya can continue accessing the loan facility already approved. Given that the next IMF evaluation test date is in December 2021, the government has a sufficient period to readjust in the event of the spike in the inflation rate in the months in between.

Rates in the fixed income market have remained relatively stable due the sufficient levels of liquidity in the money market. The government is 63.4% ahead of its prorated borrowing target of Kshs 164.6 bn having borrowed Kshs 269.1 bn of the Kshs 658.5 bn borrowing target for the FY'2021/2022. We expect a gradual economic recovery going into FY'2021/2022 as evidenced by KRAs collection of Kshs 247.2 bn in revenues during the first two months of the current fiscal year, which is equivalent to 86.9% of the prorated revenue collection target. 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.
