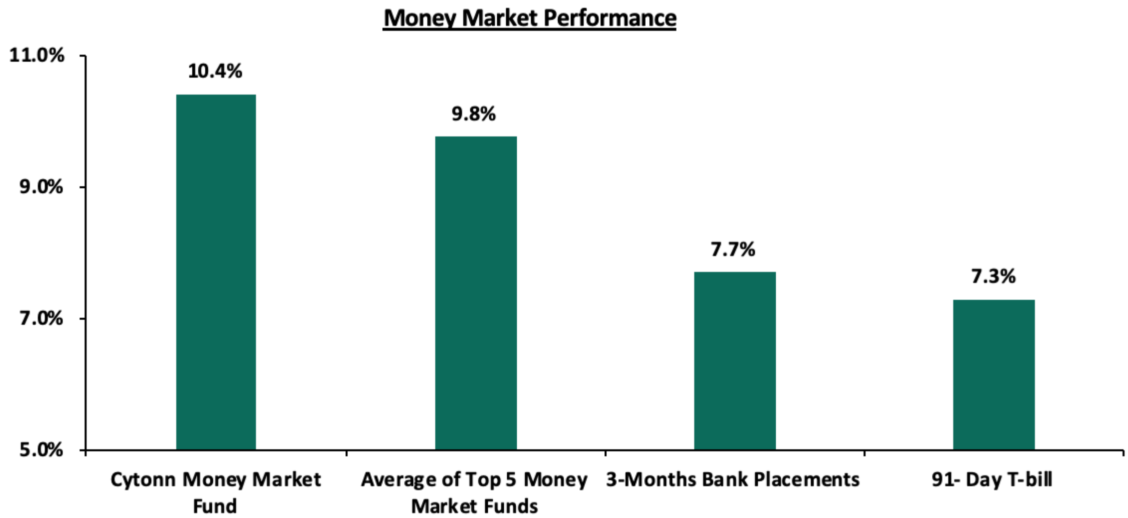
Review of the Kenyan Shilling Performance, & Cytonn Weekly #50/2021

Fixed Income

Money Markets, T-Bills Primary Auction:

During the week, T-bills remained undersubscribed, with the overall subscription rate coming in at 87.4%, up from 65.7% recorded the previous week. The 91-day paper recorded the highest subscription rate, receiving bids worth Kshs 4.5 bn against the offered Kshs 4.0 bn. This translated to a subscription rate of 113.3%, a decline from the 126.9% recorded the previous week. The subscription rate for the 182-day and 364-day papers increased to 112.2% and 52.3%, from 55.2% and 51.7%, respectively. The yields on the Treasury Bills recorded mixed performance, with the 91-day and 182-day papers yields declining by 1.5 bps and 0.7 bps to 7.3%, and 8.0%, respectively, while the yield on the 364-day paper increased by 7.3 bps to 9.2%. The government continued to reject expensive bids, accepting Kshs 17.9 bn of the Kshs 21.0 bn worth of bids received, translating to an acceptance rate of 85.5%.



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 yields on the 91-day T-bill decreased by 1.5 bps to 7.3%. The average yield of the Top 5 Money Market Funds remained relatively unchanged at 9.8%, while the yield on the Cytonn Money Market Fund decreased marginally by 0.1% points to 10.4%, from 10.5% recorded the previous week.

The table below shows the Money Market Fund Yields for Kenyan Fund Managers as published on 17th December 2021:

Money Market Fund Yield for Fund Managers as published on 17th December 2021

Rank	Fund Manager	Effective Annual Rate
1	Cytonn Money Market Fund	10.4%
2	Zimele Money Market Fund	9.9%
3	Nabo Africa Money Market Fund	9.7%
4	Sanlam Money Market Fund	9.5%
5	CIC Money Market Fund	9.3%
6	Madison Money Market Fund	9.3%
7	Apollo Money Market Fund	9.0%
8	GenCapHela Imara Money Market Fund	8.8%
9	Co-op Money Market Fund	8.7%
10	Dry Associates Money Market Fund	8.7%
11	British-American Money Market Fund	8.5%
12	Orient Kasha Money Market Fund	8.4%
13	ICEA Lion Money Market Fund	8.3%
14	NCBA Money Market Fund	8.3%
15	Old Mutual Money Market Fund	7.3%
16	AA Kenya Shillings Fund	7.0%

Source: Business Daily

Liquidity:

During the week, liquidity in the money markets eased, with the average interbank rate declining to 4.3% from the 4.8% recorded the previous week, partly attributable to government payments, including Term Auction Deposits (TADs) maturities of Kshs 49.9 bn, which offset tax remittances and settlements of government securities. The average interbank volumes traded increased by 203.6% to Kshs 19.7 bn, from Kshs 6.5 bn recorded the previous week partly attributable to the eased liquidity ahead of the upcoming festive season.

Kenya Eurobonds:

During the week, the yields on Eurobonds recorded mixed performance, with yields on the 12-year bond issued in 2019 and the 30-year bond issued in 2018 increasing marginally by 0.1% points to 6.8% and 8.2%, from 6.7% and 8.1%, respectively. The yields on the 10-year bond issued in 2014, 10-year bond issued in 2018, 7-year bond issued in 2019 and 12-year bond issued in 2021, remained unchanged at 4.4%, 5.9%, 5.7% and 6.6%, 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%	-

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**
30-Nov-21	4.4%	6.2%	8.4%	6.0%	7.1%	7.0%
10-Dec-21	4.4%	5.9%	8.1%	5.7%	6.7%	6.6%
13-Dec-21	4.4%	5.9%	8.2%	5.7%	6.8%	6.6%
14-Dec-21	4.4%	5.9%	8.2%	5.8%	6.8%	6.7%
15-Dec-21	4.4%	6.0%	8.2%	5.8%	6.9%	6.7%
16-Dec-21	4.4%	5.9%	8.2%	5.7%	6.8%	6.6%
Weekly Change	**0.0%**	**0.0%**	**0.1%**	**0.0%**	**0.1%**	**0.0%**
MTD Change	**0.0%**	**(0.3%)**	**(0.2%)**	**(0.3%)**	**(0.4%)**	**(0.3%)**
YTD Change	**0.5%**	**0.7%**	**1.2%**	**0.8%**	**0.9%**	**-**

Source: CBK

Kenya Shilling:

During the week, the Kenyan shilling depreciated marginally by 0.1% against the US dollar to close the week at Kshs 113.0, from Kshs 112.9 recorded the previous week, mainly attributable to increased dollar demand from the oil and energy sectors. Key to note, this is the lowest the Kenyan shilling has ever depreciated against the dollar. On a YTD basis, the shilling has depreciated by 3.5% 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. Increased demand from merchandise traders as they beef up their hard currency positions in anticipation for more trading partners reopening their economies globally,
c. Widening current account deficit which stood at 5.4% of GDP in the 12-months to October 2021 compared to the 4.8% of GDP in the 12 months to October 2020 attributable to a higher import bill which offset increased receipts from agricultural and services exports and remittances, and,
d. Rising global crude oil prices on the back of supply constraints at a time when demand is picking up with the easing of COVID-19 restrictions and as economies reopen. Key to note, risks abound this global recovery following the emergence of the new COVID-19 Omicron variant. We are of the view that should the variant continue to spread; most nations will respond swiftly by adopting stringent containment measures to curb the spread.

The shilling is however expected to be supported by:

i. The Forex reserves, currently at USD 8.6 bn (equivalent to 5.3-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. Key to note, the forex reserves have been steadily declining and are currently at a 3-month low. In addition, the reserves were boosted by the USD 1.0 bn proceeds from the Eurobond issued in July 2021 coupled with the USD 407.0 mn IMF disbursement and the USD 130.0 mn World Bank loan financing received in June 2021, and,

ii. Improving diaspora remittances evidenced by a 24.2% y/y increase to USD 320.1 mn in November 2021, from USD 257.7 mn recorded over the same period in 2020, which has continued to cushion the shilling against further depreciation.

Weekly Highlights:

I. **Fuel Prices**

During the week, the Energy and Petroleum Regulatory Authority (EPRA) released their monthly statement on the maximum retail prices in Kenya effective 15th December 2021 to 14th January 2022. Notably, fuel prices remained unchanged at Kshs 129.7 per litre for Super Petrol, Kshs 110.6 per litre for Diesel and Kshs 103.5 per litre for Kerosene. Below are the key take-outs from the statement:

- The performance in fuel prices was attributable to:
  i. The fuel subsidy program under the Petroleum Development Fund which resulted in subsidies of Kshs 18.3 on Super Petrol, Kshs 21.9 on Diesel and Kshs 23.5 on Kerosene,
  ii. Removal of suppliers margins of Kshs 6.3 on Super Petrol, Kshs 5.5 on Diesel and Kshs 7.7 on Kerosene, and,
  iii. The decline in the Free on Board (FOB) price of Murban crude oil in October 2021 by 5.1% to USD 69.7 per barrel, from USD 73.5 per barrel in September 2021.

- The retention of fuel prices was despite:

  i. An increase in the average landed costs of Super Petrol by 3.6% to USD 627.8 per cubic meter in November 2021, from USD 606.1 per cubic meter in October 2021,
  ii. Increase in the average landed costs of diesel by 7.0% to USD 600.2 per cubic meter in November 2021, from USD 561.1 per cubic meter in October 2021,
  iii. Increase in the average landed costs of Kerosene by 15.8% to USD 604.4 per cubic meter in November 2021, from USD 522.1 per cubic meter in October 2021, and,
  iv. Depreciation of the Kenyan shilling by 1.1% to Kshs 112.3 in November 2021, from Kshs 111.1 in October 2021.

Global fuel prices declined by 8.1% in the first two weeks of December 2021, but have increased by 46.8% on a YTD basis, to USD 73.7 from USD 50.2 at the end of 2020. The decline in global prices in December 2021 is attributable to reduced oil demand following the emergence of the Omicron corona virus variant which is expected to weigh down the global economic recovery as countries embark on restrictive measures to curb the spread of the virus.

Going forward, we expect muted pressure on the inflation basket as fuel prices which are among the major contributors to Kenya's headline inflation remain constant following the Fuel Subsidy program. However, we believe the stabilization under the fuel subsidy program by the National Treasury will be unsustainable should the average landed costs of fuel keep rising. The National Treasury will also have to compensate the Oil Marketing companies and suppliers whose margins were decreased by 100.0% in the most recent review putting further strain on the program's viability.

II. **Revenue and Net Exchequer for FY'2021/2022**

The National Treasury gazetted the revenue and net expenditures for the first five months of FY'2021/2022, ending 30th November 2021. Below is a summary of the performance:

FY'2021/2022 Budget Outturn - As at 30th November 2021

Amounts in Kshs billions unless stated otherwise

Item	12-months Original Estimates	Actual Receipts/Release	Percentage Achieved	Prorated Estimates	% achieved of prorated
Opening Balance		21.3			
Tax Revenue	1,707.4	688.1	40.3%	711.4	96.7%
Non-Tax Revenue	68.2	30.7	45.0%	28.4	108.0%
Total Revenue	**1,775.6**	**740.0**	**41.7%**	**739.8**	**100.0%**
External Loans & Grants	379.7	11.8	3.1%	158.2	7.5%
Domestic Borrowings	1,008.4	430.1	42.6%	420.2	102.4%
Other Domestic Financing	29.3	4.2	14.2%	12.2	34.0%
Total Financing	**1,417.4**	**446.1**	**31.5%**	**590.6**	**75.5%**
Recurrent Exchequer issues	1,106.6	432.6	39.1%	461.1	93.8%
CFS Exchequer Issues	1,327.2	472.5	35.6%	553.0	85.4%
Development Expenditure & Net Lending	389.2	123.8	31.8%	162.2	76.3%
County Governments + Contingencies	370.0	108.5	29.3%	154.2	70.4%
Total Expenditure	**3,193.0**	**1,137.4**	**35.6%**	**1,330.4**	**85.5%**
Fiscal Deficit excluding Grants	**(1,417.4)**	**(397.4)**	**28.0%**	**(590.6)**	**67.3%**
Fiscal Deficit as a % of GDP*	**7.5%**	**3.2%**			
Total Borrowing	**1,388.1**	**441.9**	**31.8%**	**578.4**	**76.4%**

***Projected Fiscal Deficit as a % of GDP**

The key take-outs from the report include:

a. Total revenue collected as at the end of October 2021 amounted to Kshs 740.0 bn, equivalent to 41.7% of the original estimates of Kshs 1.8 tn and is 100.0% of the prorated estimates of Kshs 739.8 bn. Cumulatively, Tax revenues amounted to Kshs 688.1 bn, equivalent to 40.3% of the target of Kshs 1,707.4 bn and are 96.7% of the prorated estimates of Kshs 711.4 bn. Notably, this is the first time the revenues have not outperformed the prorated target in the first five months of the current fiscal year,
b. Total financing amounted to Kshs 446.1 bn, equivalent to 31.5% of the original estimates of Kshs 1,417.4 bn and is 75.5% of the prorated estimates of Kshs 590.6 bn. The drag is on the external borrowings which is only at 7.5% of the prorated amounts as the government continues to seek cheaper debts and minimize servicing costs. Additionally, domestic borrowing amounted to Kshs 430.1 bn, equivalent to 42.6% of the original estimates of Kshs 1.0 tn and is 102.4% of the prorated estimates of Kshs 420.2 bn,
c. The total expenditure amounted to Kshs 1,137.4 bn, equivalent to 35.6% of the original estimates of Kshs 3,193.0 bn, and is 85.5% of the prorated expenditure estimates of Kshs 1.3 tn. Additionally, the net disbursements to recurrent expenditures came in at Kshs 432.6 bn, equivalent to 39.1% of the original estimates and 93.8% of the prorated estimates of Kshs 461.1

bn, and development expenditure amounted to Kshs 123.8 bn, equivalent to 31.8% of the original estimates of Kshs 389.2 bn and is 76.3% of the prorated estimates of Kshs 162.2 bn,

d. Consolidated Fund Services (CFS) Exchequer issues lagged behind their target of Kshs 1,327.2 bn after amounting to Kshs 472.5 bn, equivalent to 35.6% of the target, and are 85.4% of the prorated amount of Kshs 553.0 bn. The cumulative public debt servicing cost amounted to Kshs 417.8 bn which is 35.7% of the original estimates of Kshs 1,169.2 bn, and is 85.8% of the prorated estimates of Kshs 487.2 bn, and,
e. Total Borrowings as at the end of November 2021 amounted to Kshs 441.9 bn, equivalent to 31.8% of the Kshs 1,388.1 bn target and are 76.4% of the prorated estimates of Kshs 578.4 bn. The cumulative domestic borrowing target of Kshs 1.0 tn comprises of adjusted Net domestic borrowings of Kshs 661.6 bn and Internal Debt Redemptions (Roll-overs) of Kshs 346.8 bn.

The revenue performance in the first five months of the current fiscal year point towards continued economic recovery following the ease of COVID-19 containment measures. Further, the total expenditures have remained below the prorated target in line with the government's efforts to rationalize spending in a bid to narrow the fiscal deficit. Given that this is the first time revenues have not outperformed the prorated target, we expect KRA to implement more measures to boost revenue collection in the coming months. We also believe that the current measures as well as the implementation of the Finance Act 2021 which brought changes to the Excise Duty Tax, Income Tax as well as the Value Added Tax will play a big role in expanding the tax base and consequently enhance revenue collection. Additionally, should the government continue channelling funds to priority programmes, the expenditure levels are expected to remain below the target and consequently reduce the fiscal deficit. However, risks abound the outlook owing to the emergence of the Omicron variant which is expected to bring about new restrictive measures that will likely lead to a slowdown in economic recovery.

III. **IMF Second Review on Kenya's Extended Fund Facility and Extended Credit Facility**

During the week, the International Monetary Fund (IMF) completed the second review of the 38-month Extended Fund Facility (EFF) and Extended Credit Facility (ECF) - funded program. The completion of the review allows Kenya to access approximately USD 258.1 mn (Kshs 29.2 bn), bringing the total support from IMF to Kenya to USD 972.6 mn (Kshs 109.9 bn) in 2021. The decision follows Kenya's sustained economic recovery from the COVID-19 pandemic especially in the second half of 2021 coupled with the improving revenue performance. We believe that the program will continue supporting Kenya's COVID-19 response as well as the government's economic restructuring efforts, which were hampered by the pandemic. Furthermore, we believe that shifting from expensive commercial debts to concessional loans will reduce borrowing costs since such loans have more favourable terms and conditions than those offered by commercial finance markets, such as lower interest rates and deferred or income-contingent repayments. However, concerns remain elevated as more virus variants emerge, global financial conditions tighten and potential pressures ahead of the 2022 August elections heat up posing a downside risk to the economic recovery.

Rates in the fixed income market have remained relatively stable due to the tightened but sufficient levels of liquidity in the money markets. The government is 20.7% ahead of its prorated borrowing target of Kshs 316.6 bn having borrowed Kshs 382.1 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 740.0 bn in revenues during the first five months of the current fiscal year, which is equivalent to 100.0% 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 support from the IMF and World Bank will mean that the interest rate environment will remain stable since the government is not desperate for cash.