Cytonn Annual Markets Review - 2021

Fixed Income

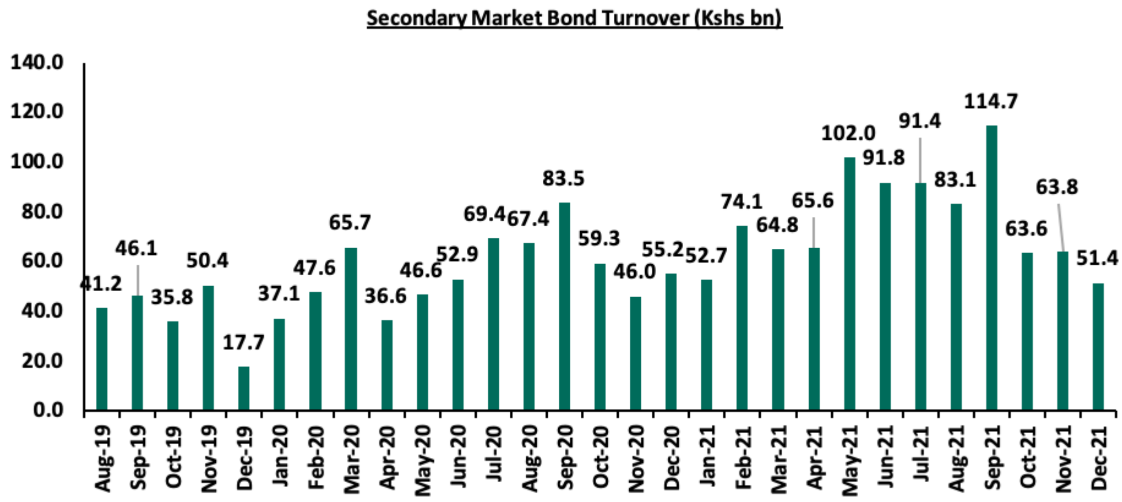
T-Bills & T-Bonds Primary Auction:

During the year, T-bills auction recorded an undersubscription, with the average subscription rate coming in at 94.1% compared to an average of 130.9% in 2020, as investors shifted their interest to the bond market in search of higher yields. The yields on the 91-day and 182-day papers increased by 10 bps and 7.1 bps to 7.0% and 7.6%, respectively while the yield on the 364-day paper declined by 1.8 bps to 8.5% in 2021. Yields on government securities remained relatively stable, mainly due to the Central Bank of Kenya’s (CBK’s) efforts to keep rates low by rejecting expensive bids in the auction market.

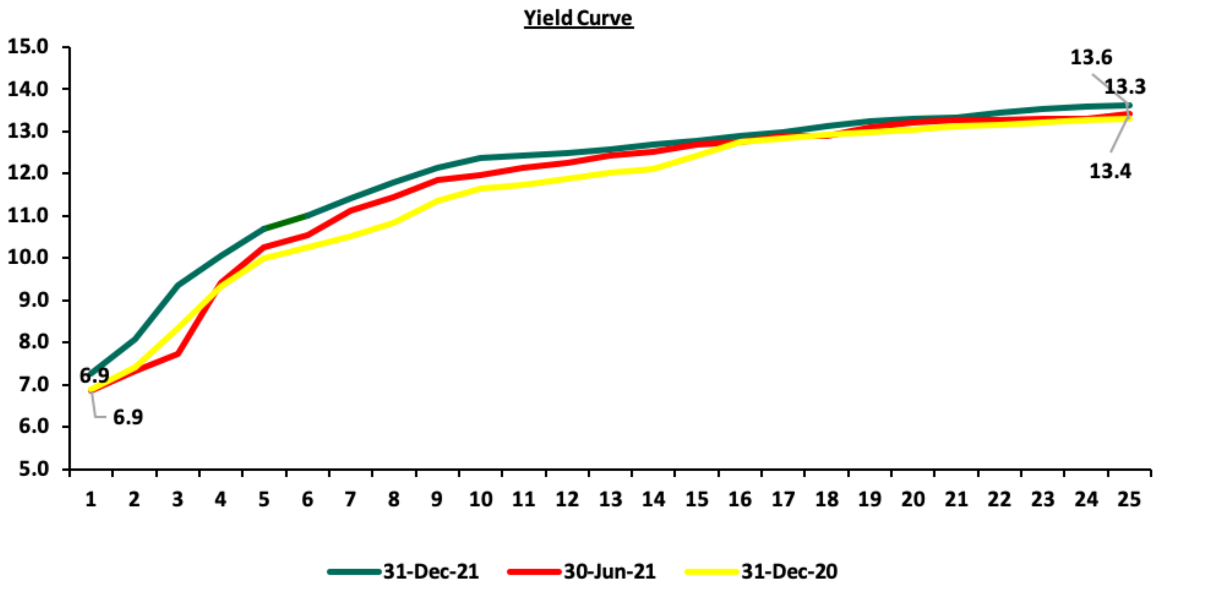
Primary T-bond auctions in 2021 were oversubscribed, with the subscription rate averaging 147.6%, which was higher than the 130.6% average subscription rate recorded in 2020, partly attributable to the ample liquidity in the money market. The market preferred the medium-term bonds, owing to concerns that risks on the longer end of the yield curve may not be sufficiently priced. The average acceptance rate came in at 79.9% in 2021, an 11.4% points increase from the 68.5% recorded in 2020 as the market adjusted to the efforts of the CBK to maintain the rates at low levels.

Secondary Bond Market Activity:

The secondary bond market recorded increased activity with the turnover having increased by 50.2% to Kshs 919.1 bn, from Kshs 667.3 bn in 2020. This is attributable to local institutional investors increasing their allocation to treasury bonds as they sort for higher returns offered by the asset class.



In 2021, the yield curve experienced upward pressure, partly attributable to the increased government borrowing and partly due to the increasing inflation seen in 2021 given that the higher the current rate of inflation and the higher the expected future rates of inflation, the higher the yields will rise across the yield curve, as investors will demand higher yield to compensate for inflation risk. The FTSE NSE bond index declined by 2.2% to close the year at 96.1, from 98.3 at the end of 2020. The chart below is the yield curve movement during the period;

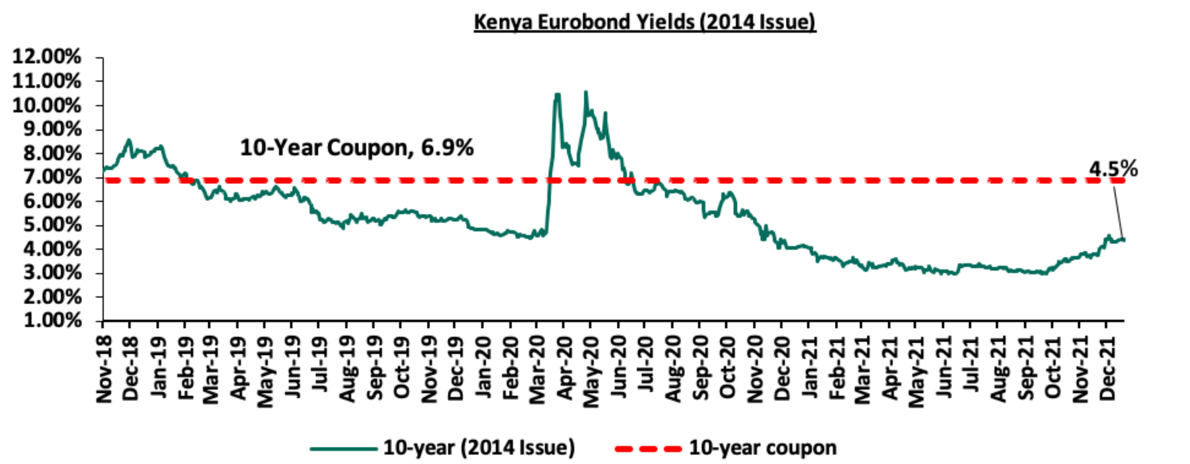


Liquidity:

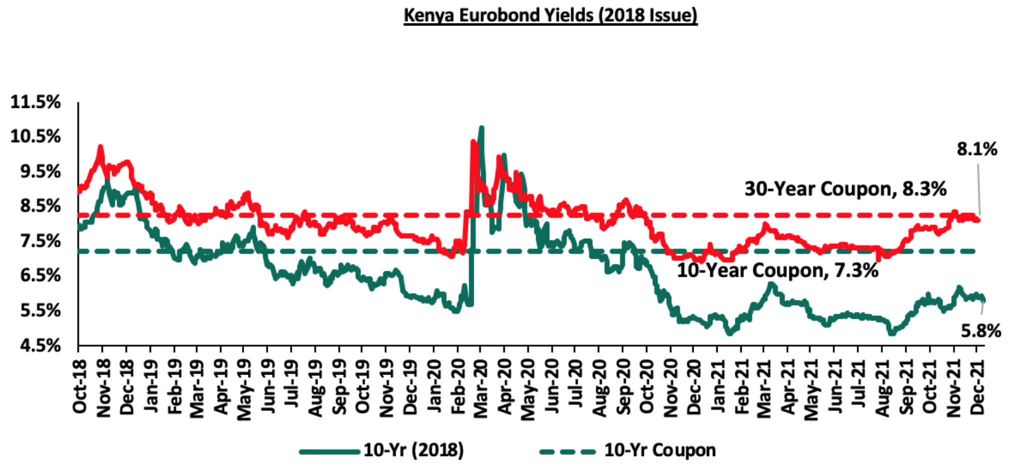
During the year, liquidity levels tightened as evidenced by the increase in the average interbank rate to 4.7% in 2021, from 3.7% in 2020. The tightened liquidity is partly due to government remittances which offset payments. The average volumes traded in the interbank market declined marginally by 0.3% to Kshs 10.65 bn in 2021 from Kshs 10.68 bn recorded in 2020.

Kenya Eurobonds:

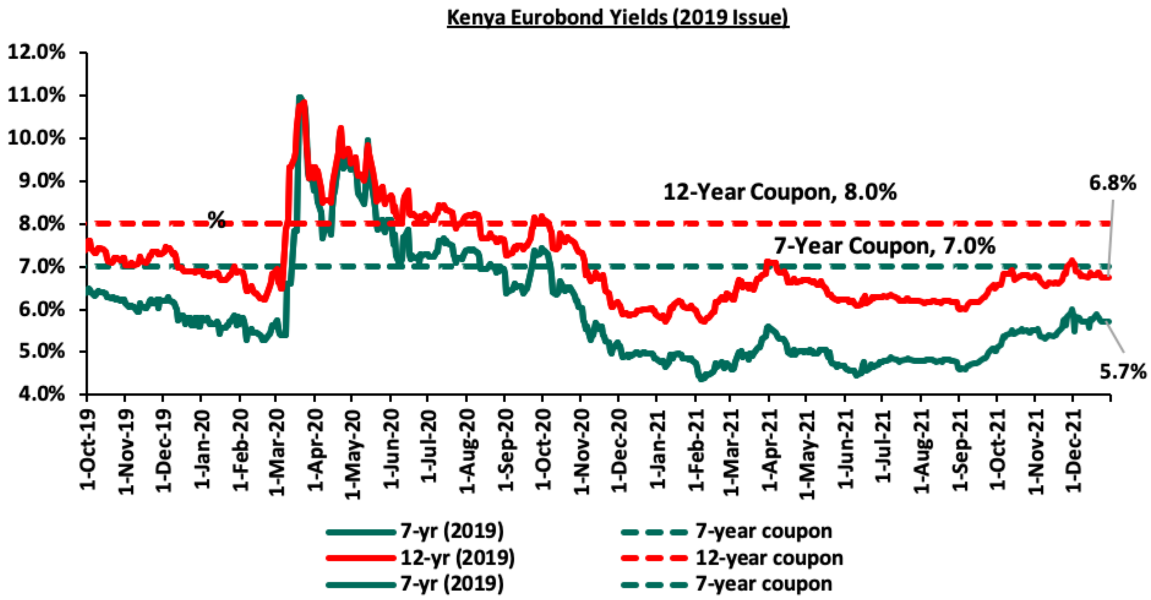
Yields on all Kenyan Eurobonds generally increased in 2021, pointing towards concerns by the investors on the economic status of the country. According to the CBK, the yields on the 10-Year Eurobond issued in 2014 increased by 0.6% points to 4.5%, from 3.9% recorded at the end of 2021.



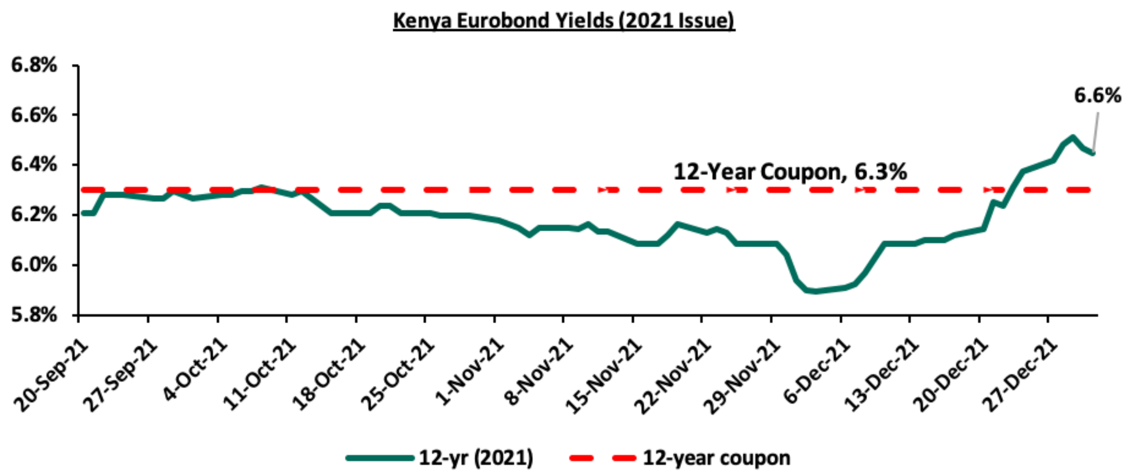
For the 2018 Eurobond issue, the yields on the 10-year Eurobond and the 30-year Eurobond both increased by 0.6% points and 1.1% points to close the year at 5.8% and 8.1%, from yields of 5.0% and 7.0% at the close of 2020 respectively.



For the 2019 Dual-tranche Eurobond issue, the yields on the 7-year Eurobond and the 12-year Eurobond increased by 0.8% points and 0.9% points to close the year at 5.7% and 6.8%, from 4.9% and 5.9% at the close of 2020, respectively.



For the 13-Year Eurobond issued in 2021 closed the year at a yield of 6.6%.



Rates in the fixed income market have remained relatively stable with an upward bias due to the tightened but sufficient levels of liquidity in the money markets and the high appetite for debt by the government. The government is 5.9% ahead of its prorated borrowing target of Kshs 341.9 bn having borrowed Kshs 362.1 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.

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