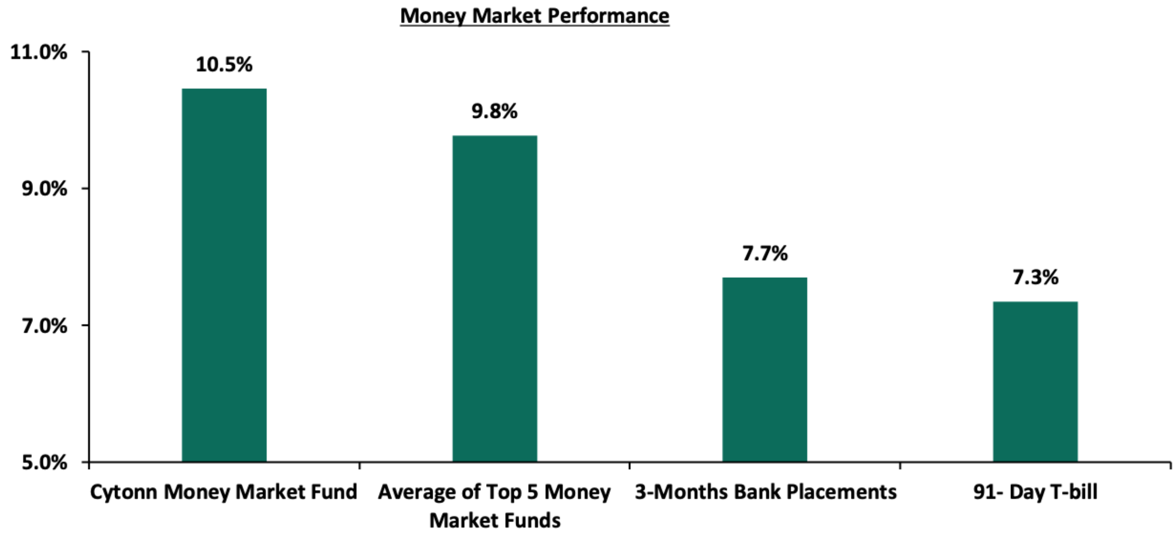
Affordable Housing in the Nairobi Metropolitan Area (NMA), & Cytonn Weekly #01/2022

Fixed Income

Money Markets, T-Bills Primary Auction:

During the week, T-bills remained undersubscribed, with the overall subscription rate coming in at 96.6%, up from the 32.6% recorded the previous week. The 91-day paper recorded the highest subscription rate, receiving bids worth Kshs 5.7 bn against the offered Kshs 4.0 bn, translating to a subscription rate of 141.3%, an increase from the 14.3% recorded the previous week, partly attributable to the eased liquidity in the money market with the interbank rates decreasing to 4.5%, from 5.5% recorded the previous week. The subscription rates for the 364-day and 182-day papers increased as well to 112.0% and 63.3% respectively, from 49.4% and 23.2% recorded the previous week. The yields on the government papers recorded mixed performance with the 91-day and 364-day papers increasing by 7.4 bps and 7.7 bps to 7.3% and 9.4%, respectively, while the yield on the 182-day paper declined by 5.4 bps to 8.0%. The government accepted Kshs 23.15 bn bids out of the Kshs 23.19 bn worth of bids received, translating to an acceptance rate of 99.9%.

In the Primary Bond Market, the government the government released the auction results for the recently issued five-year treasury bond, FXD1/2020/005, which recorded an undersubscription of 94.6%. The government sought to raise Kshs 30.0 bn for budgetary support, received bids worth Kshs 28.4 bn and accepted bids worth Kshs 27.4 bn, translating to a 96.6% acceptance rate. The bond had a coupon rate of 11.7% and a market weighted average rate of 11.3%. In December, the Government had re-opened two other bonds for the month of January, namely: FXD2/2018/10 and FXD1/2021/20, whose period of sale will end on 18th January 2022 and we expect investors to prefer these longer dated bonds since they offer higher yields of 12.5% and 13.4%, respectively, for the FXD2/2018/10 and FXD1/2021/20 respectively, compared to the 11.7% yield offered by the 5-year bond.



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 7.4 bps to 7.3%. The average yield of the Top 5 Money Market Funds marginally increased by 0.02% points to 9.78% from the 9.76% recorded the previous week while the yield on the Cytonn Money Market Fund remained relatively unchanged at 10.5%.

The table below shows the Money Market Fund Yields for Kenyan Fund Managers as published on 7th January 2021:

Money Market Fund Yield for Fund Managers as published on 7th January 2022

Rank	Fund Manager	Effective Annual Rate
1	Cytonn Money Market Fund	10.5%
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	9.2%
7	Apollo Money Market Fund	9.0%
8	GenCapHela Imara Money Market Fund	8.7%
9	Dry Associates Money Market Fund	8.7%
10	British-American Money Market Fund	8.5%
11	Co-op Money Market Fund	8.5%
12	Orient Kasha Money Market Fund	8.4%
13	NCBA Money Market Fund	8.4%
14	ICEA Lion Money Market Fund	8.3%
15	AA Kenya Shillings Fund	7.3%
16	Old Mutual Money Market Fund	7.3%

Source: Business Daily

Liquidity:

During the week, liquidity in the money markets eased, with the average interbank rate declining to 4.5% from the 5.5% recorded the previous week, partly attributable to government payments inclusive of maturities of government securities worth Kshs 20.5 bn, which offset tax remittances. The average interbank volumes traded declined by 2.3% to Kshs 13.9 bn, from Kshs 14.3 bn recorded the previous week.

Kenya Eurobonds:

During the week, the yields on Eurobonds recorded mixed performance, with yields on the 10-year bond issued in 2014 remaining unchanged at 4.4% as was recorded the previous week. Yields on the 10-year and 30-year bonds issued in 2018, the 7-year and 12-year bonds issued in 2019 and the yield on the 12-year bond issued in 2021 all increased by 0.1% points to 5.9%, 8.2%, 5.7%, 6.8% and 6.7%, from the 5.8%, 8.1%, 5.6%, 6.7% and 6.6% respectively, recorded the previous week. 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-21	4.4%	5.8%	8.1%	5.6%	6.7%	6.6%
3-Jan-22	4.5%	5.7%	8.1%	5.6%	6.7%	6.6%
4-Jan-22	4.4%	5.7%	8.1%	5.6%	6.7%	6.5%
5-Jan-22	4.3%	5.7%	8.1%	5.6%	6.7%	6.5%
6-Jan-22	4.4%	5.9%	8.2%	5.7%	6.8%	6.7%
Weekly Change	**0.0%**	**0.1%**	**0.1%**	**0.1%**	**0.1%**	**0.1%**
M/M Change	**0.0%**	**0.2%**	**0.1%**	**0.2%**	**0.1%**	**0.1%**
YTD Change	**(0.1%)**	**0.2%**	**0.1%**	**0.1%**	**0.1%**	**0.1%**

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 113.2, from Kshs 113.1 recorded the previous week, partly attributable to increased dollar demand from traders as they resume operating after the festive season. 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 0.1% against the dollar, in comparison to the 3.6% depreciation recorded in 2021. We expect the shilling to remain under pressure in 2022 as a result of:

a. Increased demand from merchandise traders as they beef up their hard currency positions in anticipation for more trading partners reopening their economies globally,
b. Ever present current account deficit due to an imbalance between imports and exports with Kenya's current account deficit having expanded by 27.4% in Q3'2021, to Kshs 184.6 bn, from Kshs 145.0 bn recorded in Q3'2020. This was attributed to a robust increase in merchandise imports by 39.6% to Kshs 321.8 bn in Q3'2021, from Kshs 230.5 bn in Q3'2020,
c. The aggressively growing government debt, with Kenya's public debt having increased at a 10-year CAGR of 17.7% to Kshs 7.8 tn in July 2021, from Kshs 1.5 tn in July 2011 thus putting

pressure on forex reserves to repay some of the public debt, 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.

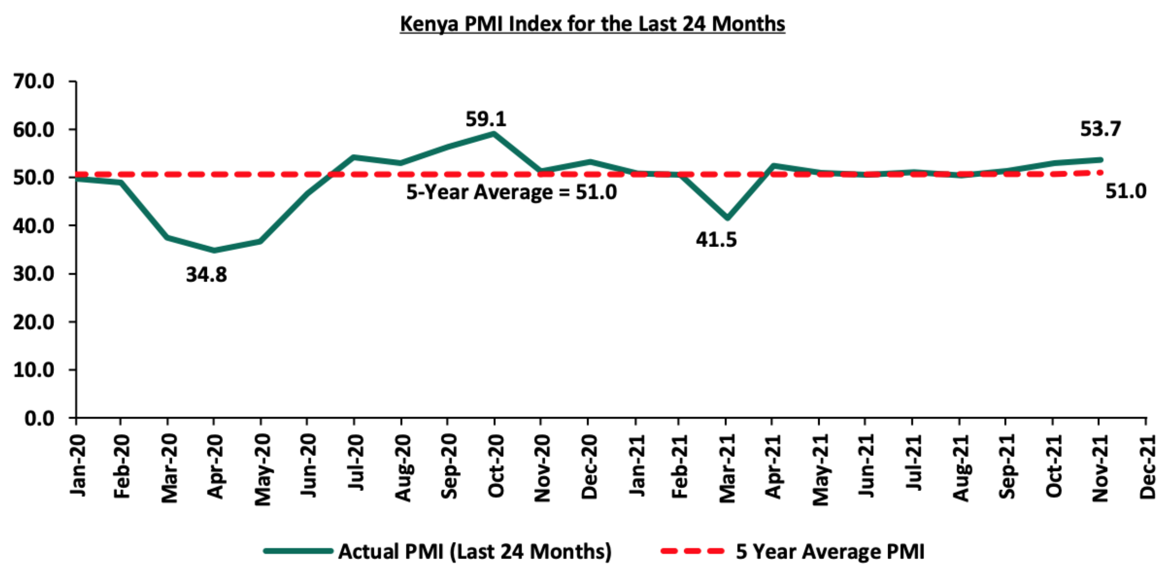
The shilling is however expected to be supported by:

i. High Forex reserves, currently at USD 8.8 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. In addition, the reserves were boosted by the USD 1.0 bn proceeds from the Eurobond issued in July, 2021 coupled with the USD 972.6 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. **Stanbic Bank's Monthly Purchasing Manager's Index (PMI)**

During the week, Stanbic Bank released its monthly Purchasing Manager's Index (PMI) highlighting that the index for the month of December increased for the third straight month to 53.7 from 53.0 recorded in November 2021, pointing towards solid improvement of business activities and continued growth of new business. Notably, this is the highest PMI recorded since October 2020 when the index was 59.1, and it is attributable to upturn in sales and growth in cash flow on the back of continued economic recovery. Key to note, overall cost pressures in the Kenyan private sector increased sharply in December 2021 due to high input purchasing prices driven by higher taxes and higher raw material prices during the month. The chart below summarizes the evolution of the PMI over the last 24 months:



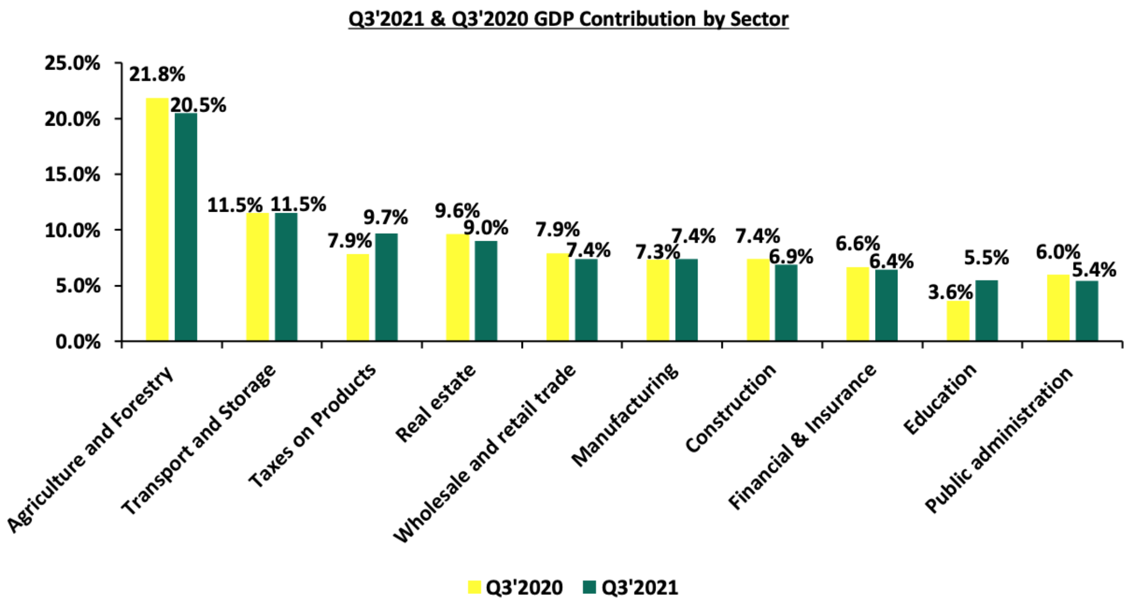
*** *Key to note, a reading above 50.0 signals an improvement in business conditions, while readings below 50.0 indicate a deterioration.*

Despite the increase of the PMI index reading for the month of December 2021, we maintain a cautious outlook in the short-term owing to the increasing cost pressures, high cost of living, political pressures ahead of the August 2022 elections and concerns of an uptick in COVID-19 infections from the new Omicron variant. We expect the easing of COVID-19 containment measures coupled with the continued vaccine rollout across the country to support recovery of local businesses and consequently increase production and boost sales volumes. However, the existence and emergence of new COVID-19 variants, such as the Omicron variant, still pose economic uncertainty however it appears the variant is milder than the earlier Delta, hence we do not expect tighter restrictions, which could negatively affect the general business environment.

II. **Q3'2021 GDP Growth**

The Kenya National Bureau of Statistics (KNBS) released the Quarterly Gross Domestic Product Report, highlighting that the Kenyan economy recorded a 9.9% growth in Q3'2021, up from the 2.1% contraction recorded in a similar period in 2020, pointing towards continued economic recovery. Consequently, the average GDP growth rate for the 3 quarters in 2021 is a growth of 6.9%, an increase from the 0.8% contraction recorded during similar periods of review in 2020. The key take-outs from the report include;

i. **Sectoral Contribution to Growth** - The biggest gainers in terms of sectoral contribution to GDP were Education and Taxes on Products, increasing by 1.8% points each to 5.5% and 9.7%, from 3.6% and 7.9% in Q3' 2020, respectively. Agriculture was the biggest loser, declining by 1.3% points to 20.5% in Q3'2021, from 21.8% in Q3'2020, following the erratic weather conditions during the period. The Education sector recorded the highest growth rate in Q3'2021 growing by 64.7% compared to the 17.4% contraction recorded in Q3'2020. The performance is mainly attributable to the re-opening of schools following closure for the most of 2020 due to the pandemic. The chart below shows the top contributors to GDP by sector in Q3'2021:



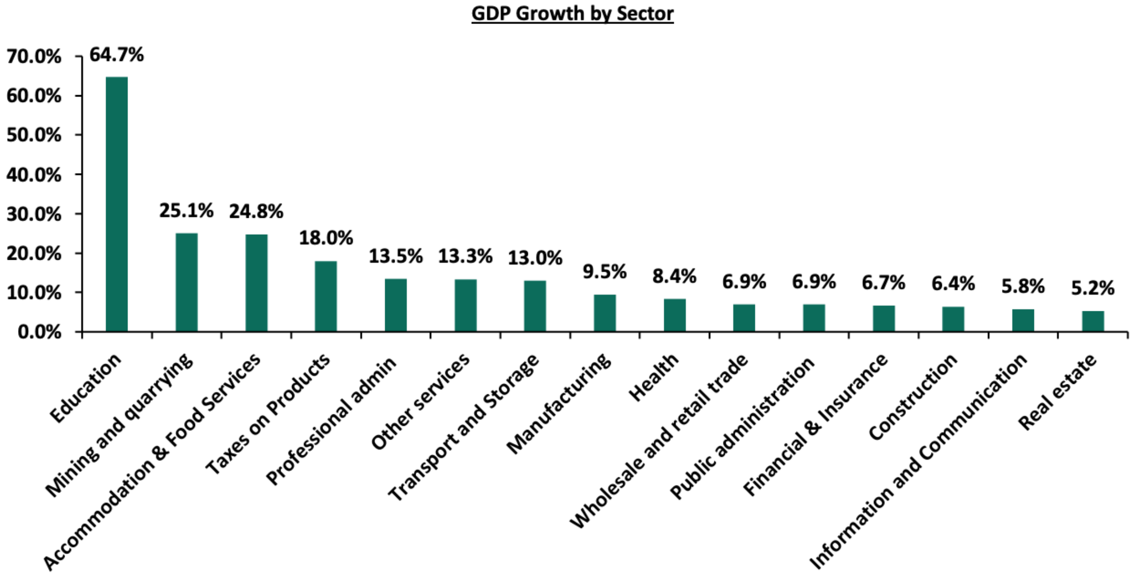
Source: KNBS Q3'2021 and Q3'2020 GDP Report

ii. **Subdued Growth in the Agricultural Sector** – Agriculture, Forestry and Fishing activities recorded a decline of 1.8% in Q3'2021 compared to a 4.2% growth in Q3'2020. The contraction during the quarters is mainly attributable to unfavorable weather conditions witnessed during the period. The sector's performance was however supported by a notable increase in cut flower and vegetable exports as well as increase in milk intake by processors,

iii. **Growth in the manufacturing sector** - The manufacturing sector reported a growth of 9.5% in Q3'2021 compared to a 1.7% contraction in a similar period of review in 2020. The sectoral contribution also increased marginally by 0.1% points to 7.4%, from 7.3% in Q3'2020, and,

iv. **Gradual rebound in the Accommodation and food services sector**- The sector recorded 24.8% growth in Q3'2021 compared to a 63.4% contraction recorded in Q3'2020, attributable to the relaxation of COVID-19 containment restrictions on the back of a positive vaccine rollout.

Additionally, the sectoral contribution increased to 0.4% from 0.3% as was recorded in Q3'2020. The chart below shows the different sectoral GDP growth rates for Q3'2021:



Source: KNBS Q3'2021 GDP Report

Going forward, we expect Kenya's GDP to continue growing in tandem with the global economy and as most sectors of the economy continue to recover. The lifting of the dawn to dusk curfew on 20th October 2021, that was put in place since March 2020 is expected to boost economic recovery in sectors such as the accommodation and food services sector as well as the manufacturing sector. We however note that agriculture being the main driver of economic growth, is expected to decline further in the remaining quarter of 2021 and remain subdued in 2022 due to the erratic weather conditions. Additionally, concerns remain elevated on the existence and emergence of new COVID-19 variants such as the Omicron variant. For more details on the GDP Report, see our Kenya Q3'2021 GDP Note.

III. **Kenya Q3'2021 Balance of Payments**

The Kenya National Bureau of Statistics released the Quarterly Balance of Payments report for Q3'2021 report highlighting that Kenya's balance of payments improved in Q3'2021, coming in at a deficit of Kshs 34.4 bn, from a deficit of Kshs 103.9 bn in Q3'2020. The decline was mainly attributable to an 11.9% increase in the stock of gross official reserve to Kshs 1,064.2 bn from Kshs 951.0 bn in Q3'2020. The decline was however weighed down by a 27.4% expansion of current account balance to Kshs 184.6 bn, from Kshs 145.0 bn in Q3'2020. The table below shows the breakdown of the various balance of payments components, comparing Q3'2021 and Q3'2020:

Q3'2021 Balance of Payments

Item	**Q3'2020**	**Q3'2021**	**% Change**
Current Account Balance	(145.0)	(184.6)	**27.4%**
Capital Account Balance	3.9	3.9	**(0.7%)**
Financial Account Balance	39.5	175.0	**342.8%**
Net Errors and Omissions	(2.4)	(28.6)	**1,111.0%**
Balance of Payments	**(103.9)**	**(34.4)**	**(66.9%)**

All values in Kshs bns

Key take-outs from the table include;

i. The current account deficit (value of goods and services imported exceeds the value of those exported) expanded by 27.4% to Kshs 184.6 bn, from Kshs 145.0 bn in Q3'2020, mainly attributable to widening of the Merchandise Trade Deficit by 39.6% to Kshs 321.8 bn, from Kshs 230.5 bn recorded in Q3'2020,
ii. The financial account balance (the difference between the foreign assets purchased by domestic buyers and the domestic assets purchased by the foreign buyers) increased by 342.8% to a surplus of Kshs 175.0 bn, from a surplus of Kshs 39.5 bn in Q3'2021. Similarly, the stock of gross official reserves increased by 11.9% to stand at Kshs 1,064.2 bn, from 951.0 bn in Q3'2020, and,
iii. Consequently, the Balance of Payments (BoP) position improved to a deficit of Kshs 34.4 bn from a deficit of Kshs 103.9 bn in Q3'2020, mainly due to the 11.9% increase in the stock of gross official reserves.

During the period of review, the Kenya shilling remained under pressure, deteriorating by 1.1% y/y to close the quarter at Kshs 109.2, from Kshs 107.9 at the end of Q3'2020. However, the shilling was supported by the high forex reserves held by the Central Bank of Kenya which increased by 9.5% in the same period to close the quarter at USD 9.4 bn, from USD 8.5 bn recorded at the end of Q3'2020. We expect relative stability in the business environment in the 2022 given the easing of the lockdown measures by Kenya's trading partners, positive COVID-19 vaccine rollout, and continued support from horticultural exports due to the normalised demand in Kenya's export markets as well as earnings from the tourism sector. However, risks remain elevated on the back of increasing global fuel prices that has led to increase in fuel importation cost, supply shortages and logistical bottlenecks, emergence of new COVID-19 variants which could lead to further restriction measures and the upcoming 2022 August elections. For a more in-depth analysis, see our Q3'2021 BOP Note.

Rates in the fixed income market have remained relatively stable due to the high liquidity in the money market. The government is 9.0% ahead of its prorated borrowing target of Kshs 354.6 bn having borrowed Kshs 386.4 bn of the Kshs 658.5 bn borrowing target for the FY'2021/2022. We expect a gradual economic recovery 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.