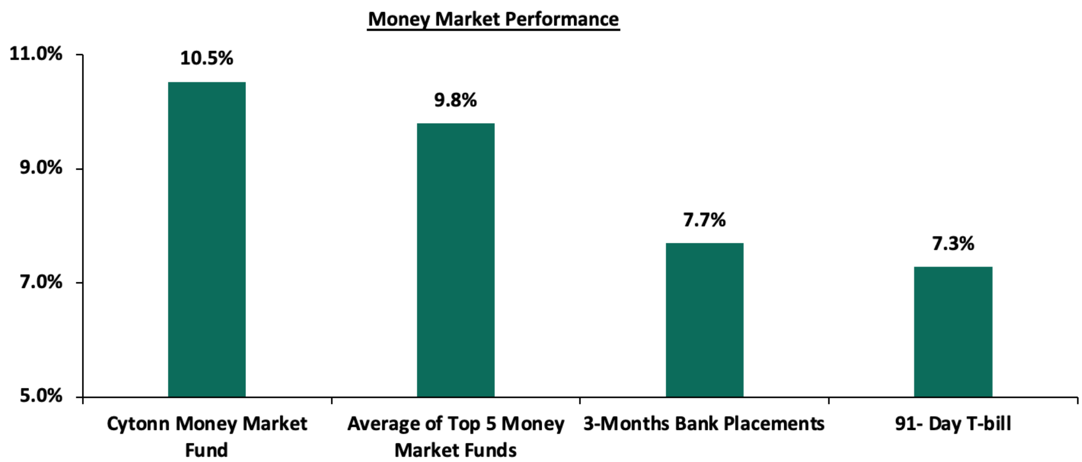
Alternative Financing for Real Estate Developments, & Cytonn Weekly #06/2022

Fixed Income

Money Markets, T-Bills Primary Auction:

During the week, T-bills were undersubscribed, with the overall subscription rate coming in at 83.5%, a decline from the 115.8% recorded the previous week, partly attributable to the tightened liquidity in the money markets, with the interbank rates increasing marginally to 4.5%, from 4.4% recorded the previous week. The 364-day paper recorded the highest subscription rate, receiving bids worth Kshs 10.8 bn against the offered Kshs 10.0 bn, translating to a subscription rate of 107.6%, a decline from the 161.7% recorded the previous week. The continued oversubscription witnessed for the 364-day paper is attributable to investors' preference for the longer-dated paper which offers a higher yield of 9.7% compared to the 7.3% and 8.1% yields offered by the 91-day and 182-day papers, respectively. The subscription rate for the 91-day and 182-day papers declined to 72.3% and 64.0%, from 84.6% and 82.4%, respectively, recorded the previous week. The yields on the government papers recorded mixed performance, with the yields on the 91-day declining by 3.2 bps to 7.3%, while those of the 182-day and 364-day papers increased by 1.3 bps and 7.4 bps to 8.1% and 9.7%, respectively. The government accepted bids worth Kshs 19.9 bn, out of the Kshs 20.0 bn worth of bids received, translating to an acceptance rate of 99.3%.



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 declined by 3.2 bps to 7.3%. The average yield of the Top 5 Money Market Funds and the yield of the Cytonn Money Market Fund increased to 9.8% and 10.5%, from 9.7% and 10.3%, respectively, as was recorded the previous week.

The table below shows the Money Market Fund Yields for Kenyan Fund Managers as published on 12th February 2022:

Money Market Fund Yield for Fund Managers as published on 12th February 2022

Rank	Fund Manager	Effective Annual Rate
1	Cytonn Money Market Fund	10.53%
2	Zimele Money Market Fund	9.91%
3	Nabo Africa Money Market Fund	9.70%
4	Madison Money Market Fund	9.47%
5	Sanlam Money Market Fund	9.38%
6	GenCapHela Imara Money Market Fund	8.97%
7	Apollo Money Market Fund	8.95%
8	CIC Money Market Fund	8.84%
9	Dry Associates Money Market Fund	8.78%
10	Orient Kasha Money Market Fund	8.70%
11	Co-op Money Market Fund	8.53%
12	NCBA Money Market Fund	8.35%
13	ICEA Lion Money Market Fund	8.32%
14	AA Kenya Shillings Fund	7.60%
15	British-American Money Market Fund	7.42%
16	Old Mutual Money Market Fund	7.41%

Source: Business Daily

Liquidity:

During the week, liquidity in the money markets tightened, with the average interbank rate increasing marginally to 4.5%, from 4.4% recorded the previous week, partly attributable to tax remittances which offset government payments made during the week. The average interbank volumes traded declined by 5.4% to Kshs 10.9 bn, from Kshs 11.5 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 4.1%, while yields on the 10-year bond issued in 2018 and 7-year bond issued in 2019 both increasing by 0.2% points to 6.8% and 6.6%, respectively. Yields on the 30-year bond issued in 2018 increased marginally by 0.1% points to 8.7%, while the yields on the 12-year bond issued in 2019 and 12-year bond issued in 2021 both increasing by 0.3% points to 7.5% and 7.4%, 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
3-Jan-22	4.4%	5.7%	8.1%	5.6%	6.7%	6.6%
04-Feb-22	4.1%	6.5%	8.5%	6.3%	7.2%	7.1%
07-Feb-22	4.2%	6.6%	8.6%	6.4%	7.3%	7.2%

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**
08-Feb-22	4.1%	6.7%	8.7%	6.5%	7.4%	7.3%
09-Feb-22	4.2%	6.8%	8.6%	6.5%	7.5%	7.3%
10-Feb-22	4.1%	6.8%	8.7%	6.6%	7.5%	7.4%
Weekly Change	**0.0%**	**0.2%**	**0.1%**	**0.2%**	**0.3%**	**0.3%**
M/M Change	**(0.3%)**	**0.8%**	**0.5%**	**0.8%**	**0.6%**	**0.6%**
YTD Change	**(0.3%)**	**1.1%**	**0.6%**	**1.0%**	**0.8%**	**0.8%**

Source: Central Bank of Kenya

Kenya Shilling:

During the week, the Kenyan shilling remained relatively stable, depreciating marginally by 0.02% against the US dollar to close the week at Kshs 113.63, from Kshs 113.60 recorded the previous week, partly 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 0.4% 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. An ever present current account deficit due to an imbalance between imports and exports, with Kenya's current account deficit estimated to come in at 5.4% of GDP in 2021, having expanded by 27.4% in Q3'2021 to Kshs 184.6 bn, from Kshs 145.0 bn recorded in Q3'2020, attributable 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 18.4% to Kshs 8.0 tn in December 2021, from Kshs 1.5 tn in December 2011 thus putting pressure on forex reserves to service 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 variants. We are of the view that should the variants continue to spread; most nations will respond swiftly by adopting stringent containment measures to curb transmissions.

The shilling is however expected to be supported by:

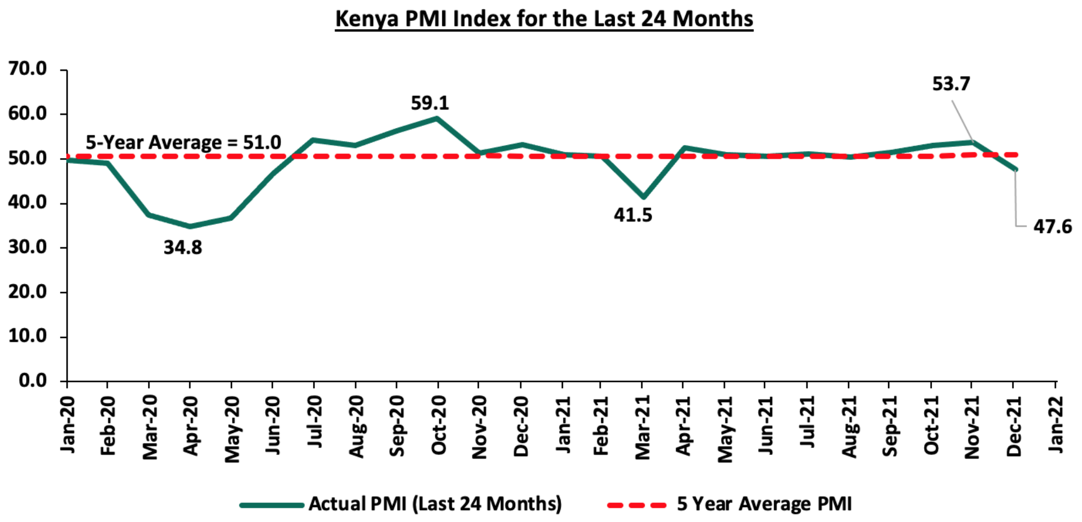
i. High Forex reserves, currently at USD 8.2 bn (equivalent to 5.0-months of import cover), which is above the statutory requirement of maintaining at least 4.0-months of import cover, and the EAC region's convergence criteria of 4.5-months of import cover. In addition, the reserves were boosted by the 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 17.0% y/y increase to USD 350.6 mn in December 2021, from USD 299.6 mn recorded over the same period in 2020, which has continued to cushion

the shilling against further depreciation.

Weekly Highlight:

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 January 2022 declined to 47.6, from the 14-month high of 53.7 that was recorded in December 2021, pointing towards significant deterioration of the business environment in the country. Notably, this is the lowest PMI recorded in the nine months since April 2021 when the index was 41.5, attributable to lower domestic spending and travel stemming from strong price pressures and sustained high COVID-19 cases from the Omicron Variant at the start of the year. Key to note, overall cost pressures in the Kenyan private sector remained elevated in January 2022 due to high input purchasing prices driven by higher taxes and higher fuel and raw material prices during the month. Additionally, employment growth slowed during the month resulting in a lower consumer purchasing power. 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.*

As a result of the decline in PMI index in January 2022, we maintain a cautious outlook in the short-term owing to the increasing cost pressures, high cost of living and political pressures ahead of the August 2022 elections. The existence and emergence of new COVID-19 variants, such as the Omicron variant, still pose economic uncertainty as it may lead to another wave of infections and consequently tighter restrictions that will further negatively affect the general business environment. In the FY'2021/2022 Supplementary Budget I, the Ministry of Health was allocated Kshs 136.0 bn, a 12.3% increase from the Kshs 121.1 bn original estimates to aid in combating the COVID-19 pandemic and curb its spread through the acquisition of more vaccines. As such, we look forward to see these efforts support the economic recovery and consequently trickle down to improving the country's PMI. However, we note that the private sector credit growth has remained relatively muted, coming in at 8.6% in December 2021, lower than the historical average of 10.3%. Further, with fuel being a major input cost to many businesses, we expect the increasing global fuel prices to further contribute to the deterioration of business conditions in the country. We are of the opinion that the fuel subsidy under the National Treasury is unsustainable and will be depleted should average landed costs of fuel continue to rise, coupled with the diversion of funds under the program to cater for other government expenditure.

Rates in the Fixed Income market have remained relatively stable due to high liquidity in the money market. The government is 6.2% ahead of its prorated borrowing target of Kshs

392.6 bn having borrowed Kshs 443.6 bn of the Kshs 658.5 bn borrowing target for the FY'2021/2022. We expect a gradual economic recovery as evidenced by the revenue collections of Kshs 926.3 bn during the first six months of the current fiscal year, which is equivalent to 104.3% of the prorated revenue collection target. However, despite the projected high budget deficit of 11.4% 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. Owing to this, our view is that investors should be biased towards short-term fixed-income securities to reduce duration risk.
