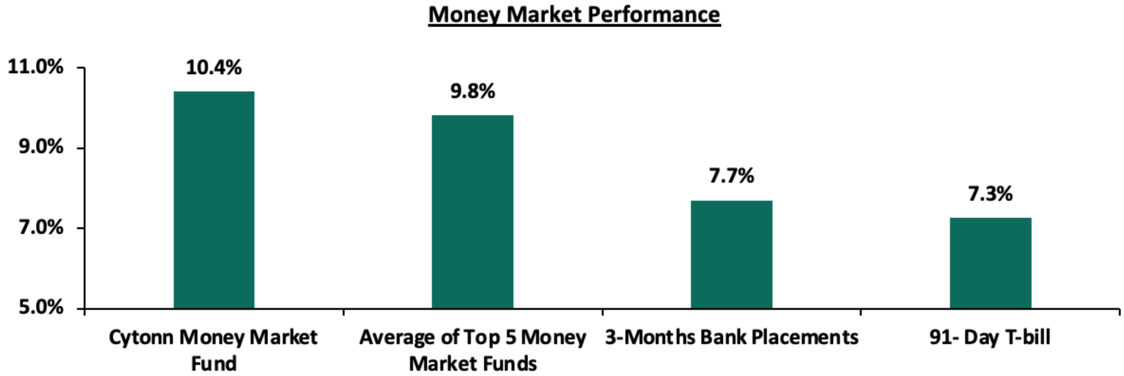
Student Housing in the Nairobi Metropolitan Area, & Cytonn Weekly #08/2022

Fixed Income

Money Markets, T-Bills Primary Auction:

During the week, T-bills were undersubscribed, with the overall subscription rate coming in at 63.6%, down from the 111.5% recorded the previous week. The undersubscription is partly attributable to the concurrent Kenya Mortgage Refinance Mortgage Company (KMRC) bond issue which recorded a subscription rate of 478.6% as investors preferred the higher yield of 12.5% on offer. The 364-day paper recorded the highest subscription rate, receiving bids worth Kshs 9.2 bn against the offered Kshs 10.0 bn, translating to a subscription rate of 92.2%, a decline from the 151.3% recorded the previous week. The subscription rate for the 182-day paper declined to 40.3%, from 101.5% recorded the previous week, while that of the 91-day paper increased to 50.3%, from 37.2% recorded last week. The yields on the government papers recorded mixed performance, with the yields on the 364-day and the 91-day papers increasing by 4.0 bps and 0.4 bps to 9.8% and 7.3%, respectively, while that of the 182-day paper declined by 1.3 bps to 8.1%. The government accepted bids worth Kshs 12.7 bn, out of the Kshs 15.3 bn worth of bids received, translating to an acceptance rate of 83.1%.

In the Primary Bond Market, the government reopened three bonds, FXD1/2021/05, FXD1/2020/15 and FXD1/2021/25, with tenors to maturity of 4.7 years, 12.9 years, and 24.2 years, respectively, in a bid to raise Kshs 50.0 bn for budgetary support. The period of sale for the issue runs from 24th February 2022 to 8th March 2022. The coupon rates are 11.3%, 12.8% and 13.9% for FXD1/2021/05, FXD1/2020/15 and FXD1/2021/25, respectively. We expect investors to prefer the longer dated paper, FXD1/2021/25, in search of higher yields. The bonds are currently trading in the secondary market at yields of 11.6%, 13.0% and 13.7%, for FXD1/2021/05, FXD1/2020/15 and FXD1/2021/25, respectively, and as such, our recommended bidding range for the three bonds is: 11.4%-11.8% for FXD1/2021/05, 12.8%-13.2% for FXD1/2020/15 and 13.5%-13.9% for FXD1/2021/25 within which range bonds of a similar tenor are trading at.



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 0.4 bps to 7.3%. The average yield of the Top 5 Money Market Funds increased marginally by 0.1% points to 9.8%, from 9.7% recorded the previous week. The yield of the Cytonn Money Market Fund declined 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 25th February 2022:

Money Market Fund Yield for Fund Managers as published on 25th February 2022

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	9.6%
5	Madison Money Market Fund	9.5%
6	Apollo Money Market Fund	9.4%
7	GenCapHela Imara Money Market Fund	9.0%
8	CIC Money Market Fund	8.9%
9	Dry Associates Money Market Fund	8.9%
10	Orient Kasha Money Market Fund	8.6%
11	Co-op Money Market Fund	8.6%
12	ICEA Lion Money Market Fund	8.4%
13	NCBA Money Market Fund	8.4%
14	British-American Money Market Fund	8.3%
15	AA Kenya Shillings Fund	7.7%
16	Old Mutual Money Market Fund	7.3%

Source: Business Daily

Liquidity:

During the week, liquidity in the money markets tightened, with the average interbank rate increasing to 5.5% from 4.5%, recorded the previous week, partly attributable to settlement of government securities coupled with tax remittances which offset government payments. The average interbank volumes traded decreased by 57.2% to Kshs 5.0 bn, from Kshs 11.8 bn recorded the previous week.

Kenya Eurobonds:

During the week, the yields on Eurobonds were on an upward trajectory attributable to increased sell offs by foreign investors. The yields on the 10-year bond issued in 2014 increased by 0.7% points to 5.0%, while the yields on the 10-year and 30-year bonds issued in 2018 increased by 1.0% and 0.6% points to 8.1% and 9.5%, respectively. The 7-year and 12-year bonds issued in 2019 increased by 1.1% and 0.9% points to 8.1% and 8.6%, respectively. The 12-year bond issued in 2021 increased by 0.8% points to 8.6%. 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%	5.8%	8.1%	5.6%	6.7%	6.6%
1-Feb-22	4.2%	6.6%	8.6%	6.3%	7.1%	7.1%
18-Feb-22	4.3%	7.1%	8.9%	7.0%	7.7%	7.8%
21-Feb-22	4.4%	7.4%	9.1%	7.1%	8.1%	7.9%
22-Feb-22	4.4%	7.5%	9.1%	7.2%	8.2%	7.9%
23-Feb-22	4.5%	7.6%	9.2%	7.5%	8.2%	8.0%
24-Feb-22	5.0%	8.1%	9.5%	8.1%	8.6%	8.6%
Weekly Change	**0.7%**	**1.0%**	**0.6%**	**1.1%**	**0.9%**	**0.8%**
MTD Change	**0.8%**	**1.5%**	**0.9%**	**1.8%**	**1.5%**	**1.5%**
YTD Change	**0.6%**	**2.3%**	**1.4%**	**2.5%**	**1.9%**	**2.0%**

Source: Central Bank of Kenya

Kenya Shilling:

During the week, the Kenyan shilling remained relatively stable, depreciating marginally by 0.1% against the US dollar to close the week at Kshs 113.8, from Kshs 113.7 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 0.6% 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.

The shilling is however expected to be supported by:

i. High Forex reserves currently at USD 8.1 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 21.7% y/y increase to USD 338.7 mn in January 2022, from USD 278.3 mn recorded over the same period in 2021, which has continued to cushion the shilling against further depreciation.

Weekly Highlight:

I. **February 2022 Inflation projections**

We are projecting the y/y inflation rate for February 2022 to fall within the range of 5.3% - 5.7%. The key drivers include:

- **Fuel prices for the period 15th February 2022 to 14th March 2022 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. With fuel being a major contributor to Kenya's headline inflation, maintaining constant fuel prices is expected to have a muted impact on the inflation basket,**

- Increasing food prices as evidenced by the 8.9% y/y increase in the prices food & non-alcoholic beverages as of January 2022 due to increased costs of production. Food prices increased by 1.1% m/m from December 2021 mainly due to increases in the prices of sifted maize flour, kale, spinach and irish potatoes among other food items, and,
- The price of electricity reduced by 15.7% in January 2022 marking the first phase of compliance with President Uhuru Kenyatta’s directive to cut the cost of electricity by 30.0% in order to reduce the cost of living. The reduction in electricity costs helped prices of goods remain stable during the month of February 2022 due to lower production costs. Additionally, the further 15.0% reduction in the cost of electricity is expected to be done within Q1’2022, which will help mute inflationary pressures going forward.

Going forward, we expect the inflation rate to remain within the government’s set range of 2.5% - 7.5%. However, concerns remain high on the widening trade deficit as global fuel prices continue to rise due to supply bottlenecks. The rising global fuel prices could deplete the fuel subsidy program currently in place and further lead to a depreciation of the local currency.

Rates in the Fixed Income market have remained stable due to the relatively ample liquidity in the money market. The government is 16.7% ahead of its prorated borrowing target of Kshs 443.2 bn having borrowed Kshs 517.3 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 1.1 tn during the first seven months of the current fiscal year, which is equivalent to 103.8% 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.