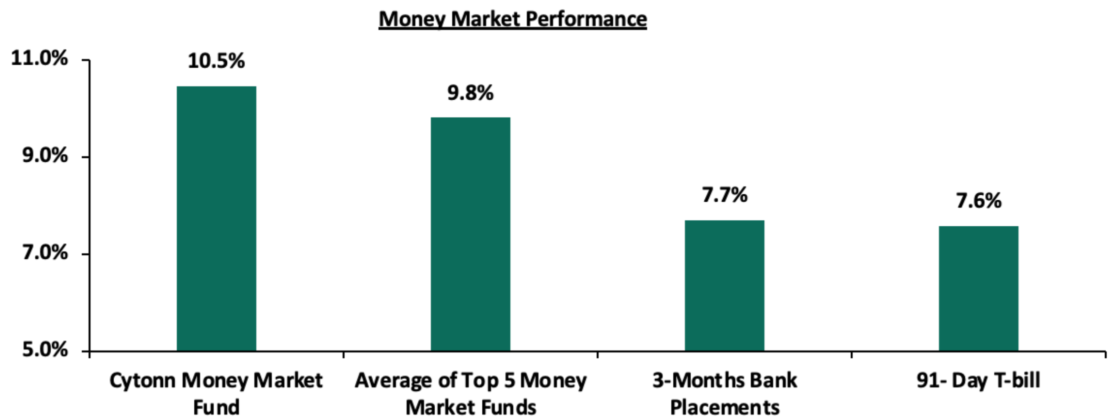
Infrastructure in the Nairobi Metropolitan Area (NMA): Roads, Water & Sewer Coverage, & Cytonn Weekly #18/2022

Fixed Income

Money Markets, T-Bills & T-Bonds Primary Auction:

During the week, T-bills were undersubscribed, with the overall subscription rate coming in at 70.2%, down from the 117.8% recorded the previous week. The 91-day paper recorded the highest subscription rate, receiving bids worth Kshs 5.3 bn against the offered Kshs 4.0 bn, translating to a subscription rate of 131.3%, a decline from the 254.6% recorded the previous week. The continued investor preference for the 91-day paper is partly attributable to the higher return on a risk-adjusted basis. The subscription rate for the 364-day and 182-day papers declined to 78.8% and 37.2%, from 93.9% and 87.0%, respectively, recorded the previous week. The yields on the government papers were on an upward trajectory, with the yields on the 364-day, 182-day and the 91-day papers increasing by 6.4 bps, 8.4 bps and 8.3 bps to 9.8%, 8.5% and 7.6%, respectively. The government accepted all the Kshs 16.8 bn worth of bids received, translating to an acceptance rate of 100.0%, reflecting the elevated borrowing appetite by the government as it nears the end of the current fiscal year 2021/2022.



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 8.3 bps to 7.6%. The yield on the Cytonn Money Market Fund and average yield of the Top 5 Money Market Funds remained relatively unchanged at 10.5% and 9.8%, respectively as recorded the previous week.

The table below shows the Money Market Fund Yields for Kenyan Fund Managers as published on 6th May 2022:

Money Market Fund Yield for Fund Managers as published on 6th May 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	9.8%
4	Sanlam Money Market Fund	9.6%
5	Dry Associates Money Market Fund	9.4%
6	Madison Money Market Fund	9.4%
7	Apollo Money Market Fund	9.3%
8	CIC Money Market Fund	9.1%
9	ICEA Lion Money Market Fund	8.7%
10	GenCap Hela Imara Money Market Fund	8.7%
11	Co-op Money Market Fund	8.6%
12	NCBA Money Market Fund	8.4%
13	Orient Kasha Money Market Fund	8.4%
14	AA Kenya Shillings Fund	7.7%
15	Old Mutual Money Market Fund	7.5%
16	British-American Money Market Fund	7.4%

Source: Business Daily

Liquidity:

During the week, liquidity in the money markets remained relatively stable, with the average interbank rate remaining relatively unchanged at 4.8%, as recorded the previous week, partly attributable to government payments which offset tax remittances. The average interbank volumes traded increased by 1.6% to Kshs 17.3 bn, from Kshs 17.0 bn recorded the previous week.

Kenya Eurobonds:

During the week, the yields on Eurobonds were on an upward trajectory, attributable to the heightened perceived risks by investors on the back of the rising inflation and the upcoming August 2022 elections. The yields on the 10-year Eurobond issued in 2014 and the 7-year Eurobond issued in 2019 increasing by 0.6% points to 9.3% and 11.1%, from 8.7% and 10.5%, respectively. The 30-year Eurobond issued in 2018, and the 12-year Eurobonds issued in 2019 and 2021 all increased by 0.3% points to 11.3%, 10.7% and 10.3%, from 11.0%, 10.4% and 10.0%, respectively. Similarly, the 10-year Eurobond issued in 2018 increased by 0.2% points to 10.2% from 10.0%:

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%	8.1%	8.1%	5.6%	6.7%	6.6%
29-April-22	8.7%	10.0%	11.0%	10.5%	10.4%	10.0%
02-May-22	8.8%	10.0%	11.1%	10.5%	10.8%	10.2%

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**
03-May-22	9.2%	10.2%	11.2%	10.8%	10.7%	10.3%
04-May-22	9.2%	10.4%	11.3%	10.8%	10.7%	10.4%
05-May-22	9.3%	10.2%	11.3%	11.1%	10.7%	10.3%
Weekly Change	**0.6%**	**0.2%**	**0.3%**	**0.6%**	**0.3%**	**0.3%**
MTD Change	**0.6%**	**0.2%**	**0.3%**	**0.6%**	**0.3%**	**0.3%**
YTD Change	**4.9%**	**2.1%**	**3.2%**	**5.5%**	**4.0%**	**3.7%**

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 115.9, from Kshs 115.8 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 year to date basis, the shilling has depreciated by 2.4% 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. Rising global crude oil prices on the back of supply constraints and geopolitical pressures at a time when demand is picking up with the easing of COVID-19 restrictions and as economies reopen. Key to note, risks abound the recovery following the emergence of the new COVID-19 variants,
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. 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 5.6% of GDP in the 12 months to February 2022 compared to the 4.3% for a similar period in 2021. The wider deficit reflects a higher import bill, particularly for oil, which more than offset increased receipts from agricultural and services exports, and remittances, and,
d. The aggressively growing government debt, with Kenya’s public debt having increased at a 10-year CAGR of 18.6% to Kshs 8.2 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. It is worth noting that the average GDP growth over the same period has been 3.9%, an indicator that the increase in debt is not translating into GDP growth.

The shilling is however expected to be supported by:

i. High Forex reserves currently at USD 8.4 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 750.0 mn World Bank loan facility received in March 2022 and are expected to be boosted further by the expected USD 244.0 bn from the International Monetary Fund (IMF), and,
ii. Improving diaspora remittances evidenced by a 25.0% y/y increase to USD 363.6 mn as of March 2022, from USD 290.8 mn recorded over the same period in 2021, the highest figure ever which

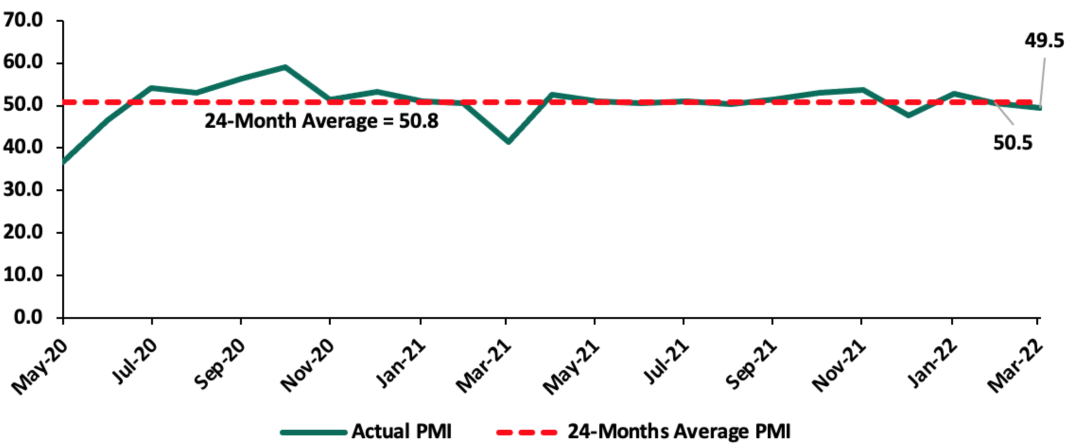
has continued to cushion the shilling against further depreciation.

Weekly Highlights:

I. **Stanbic Bank's April 2022 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 April 2022 declined to 49.5 from 50.5 recorded in March 2022 pointing towards a deterioration in the business environment in the Kenyan private sector. The decline was partly attributable to a rise in input costs, marking an eight – year high and a decline in output on the back of persistent supply chain constraints which led to increased cost pressures on the consumers. Consequently, new order volumes declined as consumers reduced their spending. Key to note, purchasing activity by businesses continued to increase despite the rise in prices as businesses sought to restock goods amid concerns that supply would worsen. Additionally, firms reported a slower increase in employment in April helped in stabilizing the work backlog, amid lower demand. The chart below summarizes the evolution of the PMI over the last 24 months:

Kenya PMI Index for 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.*

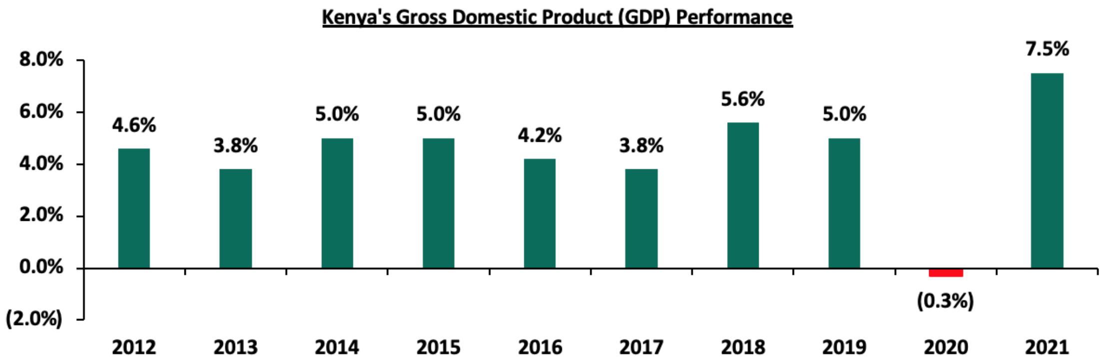
The average PMI for the first four months of 2022 came in at 50.1, higher than the 49.1 recorded in the same period in 2021 indicative of an improved business environment over the period. However, the general business environment deteriorated in April following two months of improvement and is expected to continue deteriorating in the short term on the back of the increasing cost of products which have led to a rise in the cost of living. As such, we maintain a cautious outlook in the short-term owing to the continued rise in cost of fuel and production materials which has led to reduced consumer spending. 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. Additionally, we believe that the stabilization under the fuel subsidy program by the National Treasury is unsustainable given the continued rise in the average landed cost of fuel with the cost having increased by 20.5%, 24.7% and 11.8% for super petrol, diesel and kerosene in April 2022. Further, the uncertainties surrounding the upcoming August elections, are likely to have a negative effect on the business environment as the elections are expected to disrupt the economy in general.

II. **KNBS Economic Survey 2022**

During the week, the Kenya National Bureau of Statistics (KNBS) released the Economic Survey 2022, highlighting that the economy expanded by 7.5% in 2021, from the 0.3% contraction that was recorded in 2020. The Nominal GDP grew by 12.9% to Kshs 12.1 tn in 2021, from Kshs 10.7 tn in 2020. The growth was mainly driven by the resumption of most economic activities following the lifting of COVID-19 containment measures put in place in 2020 to curb the spread of the virus, which led to the recovery of most sectors of the economy. Notably, all sectors of the economy expanded apart from the agricultural sector which contracted by 0.2%. Some of the key take-outs from the report include;

i. The agriculture, forestry and fishing sector, the largest contributor to GDP accounting for 22.4% in 2021, contracted by 0.2% from a growth rate of 4.6%. The performance is mainly attributable to unfavorable weather conditions coupled with the continued ban on logging activities in government forests since 2018 which has curtailed growth in the forestry sector. There was a decline in production of the key food crops while production of cash crops recorded mixed performance with increases being recorded in horticultural production,
ii. The manufacturing sector recorded 6.9% growth in 2021, up from the 0.4% contraction recorded in 2020. The growth is largely attributable the reopening of the economy both locally and internationally, which saw an increase in demand and activities in the economy. Notably, the food sub sector grew by 5.5% while the non-food sub sector expanded by 8.8% in 2021,
iii. The accommodation and food service sector recorded robust growth, expanding by 52.5% in 2021 from the 47.7% contraction recorded in 2020. Notably, the number of international arrivals increased by 50.3% to 0.9 mn visitors from 0.6 mn visitors in 2020 largely due to the easing of the COVID-19 related restrictions in most parts of the world. Additionally, bed night occupancy increased by 50.3% to 5.5 mn in 2021 from 3.7 mn in 2020,
iv. Other key GDP contributors such as Transportation and Storage, and, Real estate also recorded growth, growing by 7.2% and 6.7% buoyed by the easing of COVID-19 measures that had constrained activities in the sector for the better part of 2020 and increased activity in the real estate sector, respectively, and,
v. The Central Bank of Kenya (CBK) maintained the Central Bank Rate (CBR) at 7.0% during the year in a bid support economic recovery from the adverse effects of COVID-19. During the review period, there was a general increase in the interest rates with the lending rate for commercial banks' loans and advances increasing to 12.2% in December 2021, from 12.0% in December 2020 while the average deposit rate increased to 6.5% in 2021 from 6.3% in 2020.

Below is the overall Gross Domestic Product (GDP) performance over the last 10 years:



Some other key highlights from the Economic Survey 2022 report include:

i. **Public Debt**: Total stock of public debt rose by 14.9% to Kshs 7,188.1 bn in June 2021 from Kshs 6,254.4 bn as at June 2020, with public external debt accounting for 53.5% of the total debt. In FY'2021/22 a total of Kshs 1,094.0 bn is expected to be spent on servicing public debt, a 53.4% increase from Kshs 713.3 bn in FY'2020/2021. This translates to a debt service to GDP of 9.0% in FY'2021/2022, up from 6.7% in FY'2020/2021,
ii. **Employment**: During the year, total employment outside small-scale agriculture and pastoralist activities grew by 5.3% to 18.3 mn in 2021 from 17.4 mn in 2020 as firms sought to clear backlog and as the economy recovered. Total number of self-employed and unpaid family workers within the modern sector remained relatively unchanged at 0.2 mn in 2021 as was recorded in 2020. Informal sector accounted for 81.4% of total employment outside of small-scale agriculture and pastoralist activities while the formal sector accounted for 18.6% of the total employment,

iii. **Money Supply**: Broad money supply increased by 6.1% to Kshs 4,235.2 bn in December 2021 from Kshs 3,990.0 bn in December 2020. Total domestic credit grew at slower rate of 15.1% compared to a growth of 18.5% seen in 2020, partly attributable to slower growth in credit extended to the National Government of 29.3% compared to a growth of 50.9% as at end of December 2020,
iv. **Liquidity**: Quasi money, money supply (M2), broad money supply (M3), and overall liquidity grew by 3.5%, 5.6%, 6.1%, and 9.5% respectively in the review period,
v. **Imports & Exports**: Total exports increased by 15.5% to Kshs 743.7 bn in 2021, from Kshs 643.7 bn in 2020, mainly on account of increased value of domestic exports such as horticulture. On the other hand, imports grew by 30.9% to Kshs 2,151.2 bn, from Kshs 1,643.6 bn in 2020. As a result, the balance of trade widened by 40.8% to a deficit of Kshs 1,407.6 bn in 2021, from 999.9 bn in 2020. The total value of trade transactions declined to Kshs 2,287.3 bn, from Kshs 2,403.0 bn in 2020, and,
vi. **Balance of Payments**: The overall Balance of Payment position improved to a deficit of Kshs 20.4 bn, from a deficit of Kshs 152.5 bn in 2020, partly attributable to the reopening of economies which saw an improvement in international trade, and,
vii. **Current Account**: The current account balance deteriorated to a deficit of Kshs 663.8 bn in 2021 from a deficit of Kshs 510.1 bn in 2020. The current account deficit as a percentage of GDP came in at 5.5% in 2021, in comparison to the 4.8% recorded in 2020.

The Kenyan economy has had robust recovery from the adverse effects of COVID-19 and is expected to grow at a slower rate of 5.9% in 2022 driven by the global recovery and the easing of COVID-19 containment measures following an increase in vaccination rates and reduced infections. We expect to see continued growth in key sectors such as the manufacturing, tourism and accommodation sectors in tandem with the global recovery. The agricultural sector is also expected to grow in 2022 supported by the better weather conditions and the fertilizer subsidy extended by the government. However, the key challenges remain the rising fuel prices, increase in costs of production inputs, external risks such as weaker global growth, erratic weather conditions and the uncertainty surrounding the upcoming August 2022 elections.

Rates in the Fixed Income market have remained stable due to the relatively ample liquidity in the money market. The government is 1.9% ahead of its prorated borrowing target of Kshs 572.6 bn having borrowed Kshs 583.3 bn of the Kshs 661.6 bn borrowing target for the FY'2021/2022. We expect a gradual economic recovery as evidenced by the revenue collections of Kshs 1.2 tn during the first eight months of the current fiscal year, which was equivalent to 100.8% of the prorated revenue collection target. However, despite the projected high budget deficit of 8.1% and the affirmation of the `B+' rating with negative outlook by Fitch Ratings, 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.