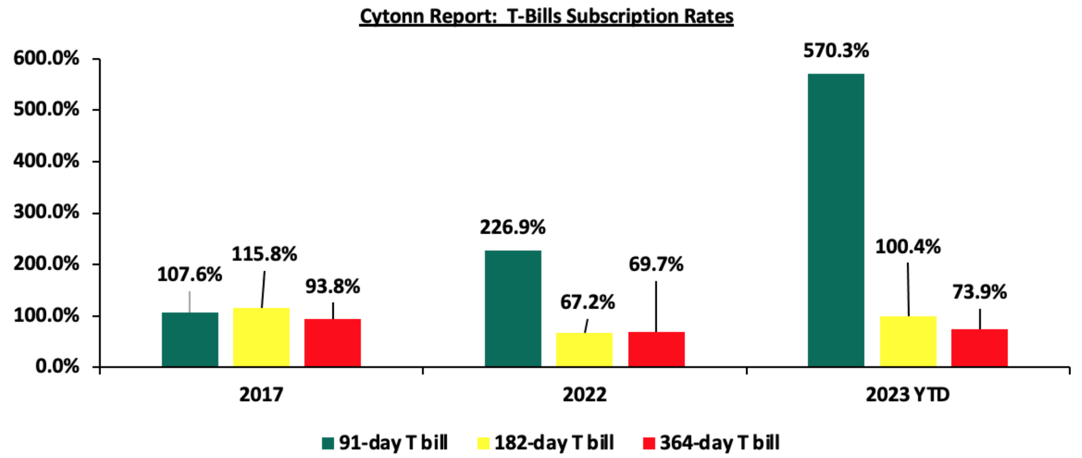
Unit Trust Funds (UTFs) Performance, Q3'2022, & Cytonn Monthly

Fixed Income

Money Markets, T-Bills Primary Auction:

During the month of January, T-bills were oversubscribed, with the overall average subscription rate coming in at 126.5%, an increase from 77.8% recorded in the month of December 2022. The average subscription rate for the 364-day, 182-day and 91-day papers increased to 42.5%, 92.3% and 422.1% from 22.8%, 33.0% and 327.4%, respectively, recorded in December 2022. The average yields on the government papers were on an upward trajectory, with the average yields on the 364-day, 181-day papers and 91-day papers increasing by 16.6 bps, 8.2 bps and 11.8 bps to 10.4%, 9.9% and 9.5%, from 10.3%, 9.8% and 9.3%, respectively recorded in December 2022. For the month of January, the government accepted a total of Kshs 119.0 bn of the Kshs 121.5 bn worth of bids received, translating to an acceptance rate of 97.9%.

During the week, T-bills remained oversubscribed, with the overall subscription rate coming in at 208.9%, up from the 142.9% recorded the previous week. Investor's preference for the shorter 91-day paper persisted, with the paper receiving bids worth Kshs 28.7 bn against the offered Kshs 4.0 bn, translating to a subscription rate of 718.6%, up from 458.9% recorded the previous week. The significant oversubscription is partly attributable to the high yields being offered on the shorter dated papers coupled with investors seeking to avoid duration risk. The subscription rates for the 364-day and 182-day papers also increased to 105.3% and 108.5% from 56.8% and 102.6%, respectively, recorded the previous week. The government accepted bids worth Kshs 32.4 bn out of the Kshs 50.1 bn total bids received, translating to an acceptance rate of 64.7%. The yields on the government papers were on an upward trajectory, with the yields on the 364-day paper increasing by 4.6 bps to 10.6%, while 182-day and 91-day papers increasing by 4.3 bps each to 10.0% and 9.6%, respectively. The chart below compares the overall average T- bills subscription rates obtained in 2017, 2022 and 2023 Year to Date (YTD):



The January 2023 bonds were oversubscribed, with the average subscription rate coming in at 131.7%, up from 47.7% recorded in December 2022. The reopened bonds FXD1/2020/005 and FXD1/2022/015 received bids worth Kshs 41.6 bn against the offered Kshs 50.0 bn, translating to a subscription rate of 83.3% with the government accepting bids worth Kshs 31.5 bn translating to an acceptance rate of 75.7%. Their subsequent tap sale received bids worth Kshs 18.0 bn against the offered Kshs 10.0 bn, translating to an oversubscription rate of 180.2%, with the government accepting bids worth Kshs 17.6 bn translating to an acceptance rate of 97.8%. The table below provides more details on the bonds issued during the month of January 2023:

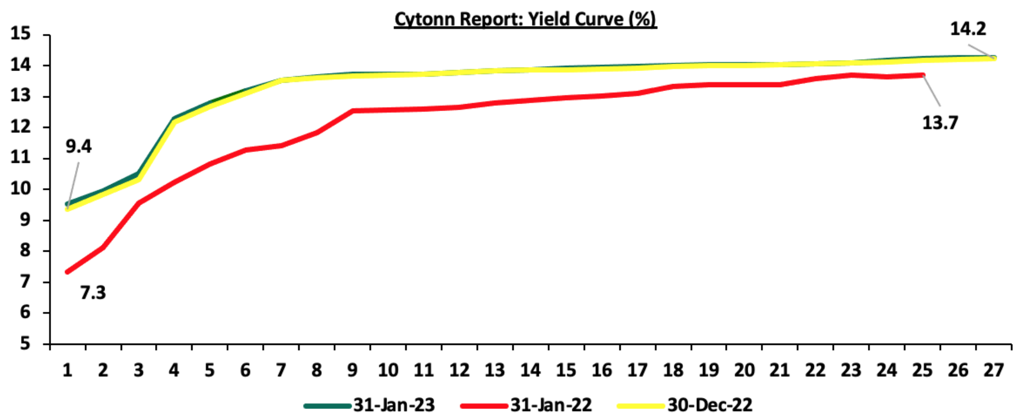
Cytonn Report: Treasury Bonds Issued in January 2023

Issue Date	Bond Auctioned	Effective Tenor to Maturity (Years)	Coupon	Amount offered (Kshs bn)	Actual Amount Raised (Kshs bn)	Total bids received	Average Accepted Yield	Subscription Rate	Acceptance Rate
16/01/2023	FXD1/2020/005 (re-opened)	2.4	11.7%	50.0	31.5	41.6	12.9%	83.3%	75.7%
	FXD1/2022/015 (re-opened)	14.3	13.9%				14.3%		
20/01/2023	FXD1/2020/005 - Tapsale	2.4	11.7%	10.0	17.6	18.0	12.9%	180.2%	97.8%
	FXD1/2022/015 - Tapsale	14.3	13.9%				14.2%		
Jan 2023 Average		**8.4**	**12.8%**	**30.0**	**24.6**	**29.8**	**13.6%**	**131.7%**	**86.8%**
Dec 2022 Average		**10.6**	**13.6%**	**49.3**	**21.1**	**23.6**	**13.7%**	**47.7%**	**86.5%**

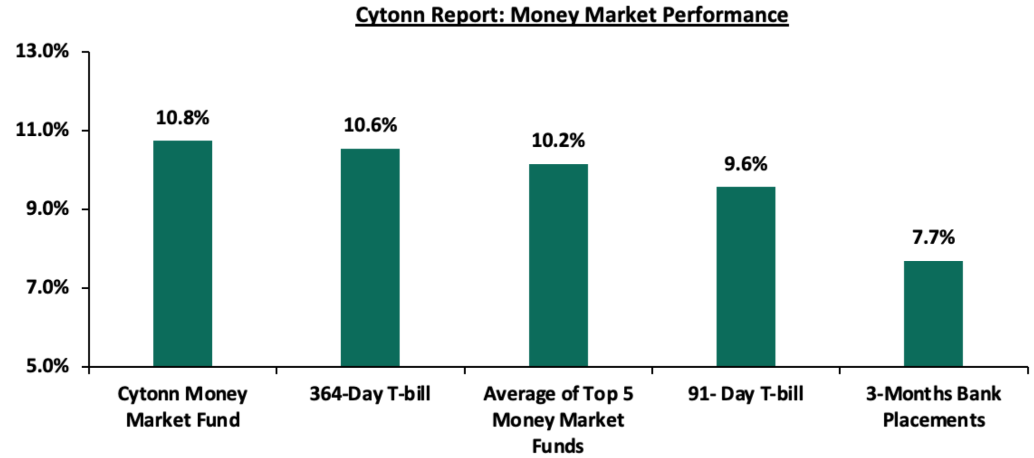
Source: Central Bank of Kenya (CBK)

Secondary Bond Market:

The yields on the government securities increased during the month compared to the same period in 2022 as a result of the elevated inflationary pressures leading to investors attaching higher risk premiums. The chart below shows the yield curve movement during the period:



The secondary bond turnover declined by 8.3% to Kshs 44.0 bn, from Kshs 48.0 bn recorded in December 2022, pointing towards reduced activity by commercial banks in the secondary bonds market, attributable to the higher yields in the primary bond market which are more appealing to investors as well as high coupons on newly issued bonds. On a year on year basis, the bonds turnover declined by 5.9% to Kshs 44.0 bn, from Kshs 46.8 bn worth of treasury bonds transacted over a similar period last year.



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 364-day and 91-day T-bill increased by 4.6 and 4.3 bps to 10.6% and 9.6%. The average yield of the Top 5 Money Market Funds and the Cytonn Money Market Fund remained unchanged at 10.2% and 10.8%, respectively

The table below shows the Money Market Fund Yields for Kenyan Fund Managers as published on 3rd February 2023:

Cytonn Report: Money Market Fund Yield for Fund Managers as published on 3rd February 2023

Rank	Fund Manager	Effective Annual Rate
1	Cytonn Money Market Fund (dial *809# or download Cytonn App)	10.8%
2	Apollo Money Market Fund	10.2%
3	GenCap Hela Imara Money Market Fund	10.1%
4	Zimele Money Market Fund	9.9%
5	NCBA Money Market Fund	9.9%
6	Sanlam Money Market Fund	9.8%
7	Kuza Money Market fund	9.8%
8	Nabo Africa Money Market Fund	9.7%
9	Old Mutual Money Market Fund	9.7%
10	Dry Associates Money Market Fund	9.6%
11	Madison Money Market Fund	9.5%
12	AA Kenya Shillings Fund	9.5%
13	Co-op Money Market Fund	9.3%
14	CIC Money Market Fund	9.2%
15	ICEA Lion Money Market Fund	8.9%
16	British-American Money Market Fund	8.9%
17	Orient Kasha Money Market Fund	8.6%
18	Absa Shilling Money Market Fund	8.2%

Cytonn Report: Money Market Fund Yield for Fund Managers as published on 3rd February 2023

Rank	Fund Manager	Effective Annual Rate
19	Equity Money Market Fund	7.7%

Source: Business Daily

Liquidity:

Liquidity in the money markets tightened in the month of January 2023, with the average interbank rate increasing to 6.0%, from 5.6%, recorded in December 2022. Also during the week, liquidity in the money markets tightened, with the average interbank rate increasing to 6.5% from 6.2% recorded the previous week, partly attributable to tax remittances that offset government payments. The average interbank volumes traded increased by 71.0% to Kshs 27.2 bn from Kshs 15.9 bn recorded the previous week.

Kenya Eurobonds:

During the month, the yields on the Eurobonds were on a downward trajectory. The yield on the 10-year Eurobond issued in 2014 recorded the largest decline, having declined by 1.7% points to 11.2% from 12.9%, recorded in December 2022 partly attributable to increased investor sentiments following International Monetary Fund (IMF) positive reviews as well as the new administration's pledge on honoring debt payments.

During the week, the yields on Eurobonds recorded mixed performance with the yield on the 7-year Eurobond issued in 2019 recording the largest gain having gained by 0.3% points to 10.1% from 9.8%, recorded the previous week. The table below shows the summary of the performance of the Kenyan Eurobonds as of 2nd February 2023;

Cytonn Report: Kenya Eurobonds Performance

	2014	2018		2019		2021
Date	**10-year issue**	**10-year issue**	**30-year issue**	**7-year issue**	**12-year issue**	**12-year issue**
Amount Issued (USD bn)	**2.0**	**1.0**	**1.0**	**2.1***		**1.0**
Years to Maturity	**1.3**	**5.0**	**25.0**	**4.2**	**9.2**	**11.3**
Yields at Issue	**6.6%**	**7.3%**	**8.3%**	**7.0%**	**7.9%**	**6.2%**
30-Dec-22	12.9%	10.5%	10.9%	10.9%	10.8%	9.9%
2-Jan-23	12.9%	10.5%	10.9%	10.9%	10.8%	9.9%
26-Jan-23	10.4%	9.7%	10.3%	9.8%	10.0%	9.4%
27-Jan-23	10.9%	9.8%	10.4%	9.8%	10.0%	9.4%
30-Jan-23	11.0%	9.9%	10.4%	10.0%	10.1%	9.5%
31-Jan-23	11.2%	10.1%	10.7%	10.4%	10.4%	9.8%
1-Feb-23	11.2%	10.2%	10.6%	10.5%	10.3%	9.8%

Cytonn Report: Kenya Eurobonds Performance

	2014	2018		2019		2021
Date	**10-year issue**	**10-year issue**	**30-year issue**	**7-year issue**	**12-year issue**	**12-year issue**
Amount Issued (USD bn)	**2.0**	**1.0**	**1.0**	**2.1***		**1.0**
Years to Maturity	**1.3**	**5.0**	**25.0**	**4.2**	**9.2**	**11.3**
Yields at Issue	**6.6%**	**7.3%**	**8.3%**	**7.0%**	**7.9%**	**6.2%**
2-Feb-23	10.6%	9.9%	10.4%	10.1%	10.0%	9.5%
Weekly Change	**0.2%**	**0.2%**	**0.1%**	**0.3%**	**0.0%**	**0.1%**
MTM Change	**(1.7%)**	**(0.4%)**	**(0.2%)**	**(0.5%)**	**(0.4%)**	**(0.1%)**
YTD Change	**(2.3%)**	**(0.6%)**	**(0.5%)**	**(0.8%)**	**(0.8%)**	**(0.4%)**
Issue to Date Change	**4.0%**	**2.6%**	**2.1%**	**3.1%**	**2.1%**	**3.3%**

**2019 aggregate amount issued for the two issues was USD 2.1 bn*

Source: Central Bank of Kenya (CBK)

Kenya Shilling:

During the month, the Kenya Shilling depreciated by 0.8% against the US Dollar, to close the month at Kshs 124.4, from Kshs 123.4 recorded at the end of December 2022, partly attributable to the increased dollar demand from importers, especially oil and energy sectors against a slower supply of hard currency.

During the week, the Kenyan shilling depreciated by 0.2% against the US dollar to close the week at Kshs 124.6, from Kshs 124.4 recorded the previous week, partly attributable to increased dollar demand from importers, especially oil and energy sectors against a slower supply of hard currency. On a year to date basis, the shilling has depreciated by 0.9% against the dollar, adding to the 9.0% depreciation recorded in 2022. We expect the shilling to remain under pressure in 2023 as a result of:

i. High global crude oil prices on the back of persistent supply chain bottlenecks coupled with high demand,
ii. An ever-present current account deficit estimated at 4.9% of GDP in 2022, despite improving by 0.3% points from 5.2% recorded in 2021,
iii. The need for Government debt servicing which continues to put pressure on forex reserves given that 69.3% of Kenya's External debt was US Dollar denominated as of October 2022, and,
iv. A continued hike in the US Fed interest rates in 2023 to a range of 4.5% - 4.75% in February 2023 has strengthened the dollar against other currencies by causing capital outflows from other global emerging markets.

The shilling is however expected to be supported by:

a. Improved diaspora remittances standing at a cumulative USD 4.0 bn for the year 2022, representing an 8.3% y/y increase from a cumulative USD 3.7 bn recorded in 2021. Notably on a m/m basis, the remittance for the month of December 2022 increased by 3.4% to USD 0.4 bn, from USD 0.3 bn recorded in November 2022.

Key to note, Kenya's forex reserves remained relatively unchanged at USD 7.0 bn as at 2nd February 2023. As such, the country's months of import cover remained unchanged at 3.9 months, which are marginally below the statutory requirement of maintaining at least 4.0-months of import. The chart below summarizes the evolution of Kenya months of import cover over the last 10 years

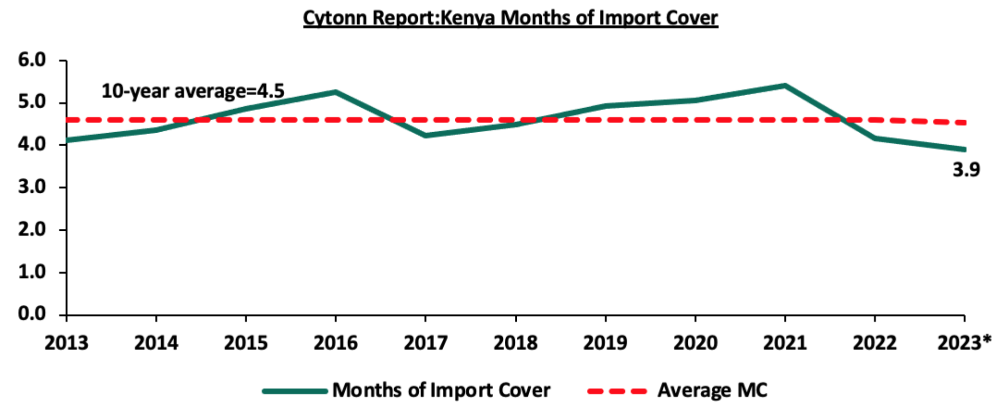


**Figure as of 2nd February* 2023

Weekly Highlights:

I. **January 2023 Inflation**

The y/y inflation in January 2023 came at 9.0%, marginally easing from the 9.1% recorded in December 2022. This was against our expectations of an increase within a range of 9.2%-9.6%, driven by an expected increase in the Housing, water Electricity, Gas and other fuel index following the increase in electricity prices. January 2023 inflation remained elevated compared to 5.4% recorded in January 2022 and above the CBKs target range of 2.5%-7.5%. The elevated annual inflation was mainly due to an increase in prices of commodities under, transport index, food and non-alcoholic beverages index, and, housing, water, electricity, gas and other fuel index. The table below shows a summary of both the year on year and month on month commodity indices performance:

Cytonn Report: Major Inflation Changes – January 2023

Broad Commodity Group	Price change m/m (December-2022/January-2023)	Price change y/y (January-2022/January-2023)	Reason
Food and Non-Alcoholic Beverages	0.2%	12.8%	The m/m increase was mainly driven by increase in price commodities such as tomatoes, beans and Beef. The increase was, however, mitigated by drop in prices of commodities such as mangoes, potatoes - irish, cowpeas, onions, maize grain and kales
Housing, Water, Electricity, Gas and Other Fuel	0.3%	7.3%	The m/m change was mainly due to increase in prices of 50 Kilowatts electricity units and 200 Kilowatts electricity units
Transport cost	0.0%	13.1%	The index remained unchanged as the prices of diesel and petrol remained unchanged in January 2023.
Overall Inflation	**0.2%**	**9.0%**	**The m/m was mainly driven by 0.3% increase in Housing, Water, Electricity, Gas and Other Fuel**

Source: Kenya National Bureau of Statistics (KNBS)

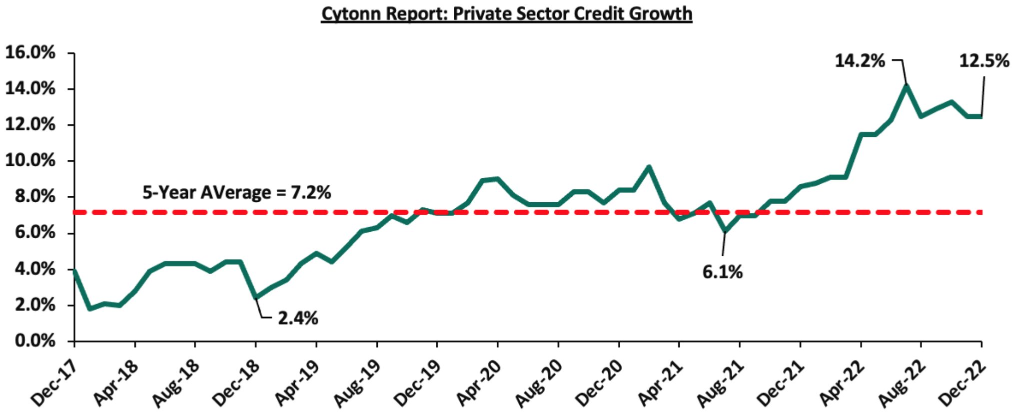
Despite the slight ease in inflationary pressures, we expect the overall inflation to remain elevated in the short term but ease in the long-term as global supply constraints eases. The high inflation is mainly on the back of high fuel prices following the scaling down of the fuel subsidy and increased electricity prices due to high tariffs. With fuel and electricity being a major input in most businesses, we expect the high prices to continue elevating the cost of production and consequently leading to high commodities prices. Key to note, the full anchoring of the domestic inflationary pressures is largely pegged on how soon the global supply constrained is restored.

II. **January 2023 MPC Meeting**

The Monetary Policy Committee (MPC) met on 30th January, 2023 to review the outcome of its previous policy decisions and recent economic developments, and to decide on the direction of the Central Bank Rate (CBR). The MPC retained the CBR rate at 8.75%, which was against our expectation of an increase by 25.0 bps to 9.0%. Below are some of the key highlights from the meeting:

i. The headline inflation eased to 9.1% in December 2022 from 9.5% in November 2022 driven by softened food prices. Food inflation declined to 13.8% in December 2022 from 15.4% in November 2022, attributable to decrease in prices of maize and milk products owing to the ongoing harvests and the impact of the recent short rains, respectively. Fuel inflation during the month of December 2022 also declined to 12.7% from 13.8% in November 2022, mainly due to lower international oil prices. However, the prices of fuel remained elevated following the scaling down of the fuel subsidy and increased electricity prices due to high tariffs. We expect the overall inflation to remain elevated in the short term, however, to ease in the long-term as global supply constraints eases,
ii. The recently released GDP data for Q3'2022 together with leading economic indicators showed the Kenya economy registered a strong growth, recording a real GDP growth of 4.7% in Q3'2022. The growth was mainly driven by increased activities in sectors such as Wholesale and retail trade, electricity and water, and, real estate. Based on the available economic indicators, the economy is estimated to have grown by 5.6% in 2022,
iii. Goods export remained strong with export growing by 10.9% in 2022 compared with 11.1% in 2021. Receipts from tea and manufactured goods exports increased by 16.1% and 22.1%, respectively, attributed to increased demand from traditional markets. Additionally, imports grew by 5.8% in 2022, compared to 25.4% in 2021, the slowed growth of imports is partly attributable to drop of imports of infrastructure related equipment, mainly on the back of completed projects. Receipts from services exports rebounded significantly reflecting sustained improvement in international travel and transport. Remittances in 2022 totaled to USD 4.0, 8.3% higher than USD 3.7 bn recorded in 2021. Despite the development, the current account deficit is estimated at 4.9% of the GDP in 2022 and projected at 5.4% of GDP in 2023,
iv. The CBK foreign exchange reserves which currently stand at USD 7.0 bn representing a 3.9 months of import cover, continues to provide adequate cover against any short term shocks in the foreign exchange markets,
v. The banking sector remained stable and resilient, with strong liquidity and capital adequacy ratios. The ratio of gross non-performing loans (NPLs) to gross loans stood at 13.3% in December 2022, compared to 13.8% in October 2022. Repayments and recoveries were noted in sectors such as, tourism, restaurant and hotels, transport and communication and manufacturing. Additionally, the banking sector asset base increased by 10.0% to Kshs 6.6 tn in 2022 from Kshs 6.0 tn at the end of 2021, attributable to banks reviewing their business models leveraging on technology and innovation, enhanced capital and liquidity buffers and continued focus on customer-centricity,
vi. Growth in private sector credit increased to 12.5% in 2022 compared to 8.6% in 2021, attributed to strong credit growth in sectors such as; transport and communication, manufacturing, and, business services of 23.5%, 13.8% and 13.7%, respectively. Additionally, the number of loans approval increased, reflecting improved demand with increased economic activities. The chart

below shows the movement of the private sector credit growth of the last five years:

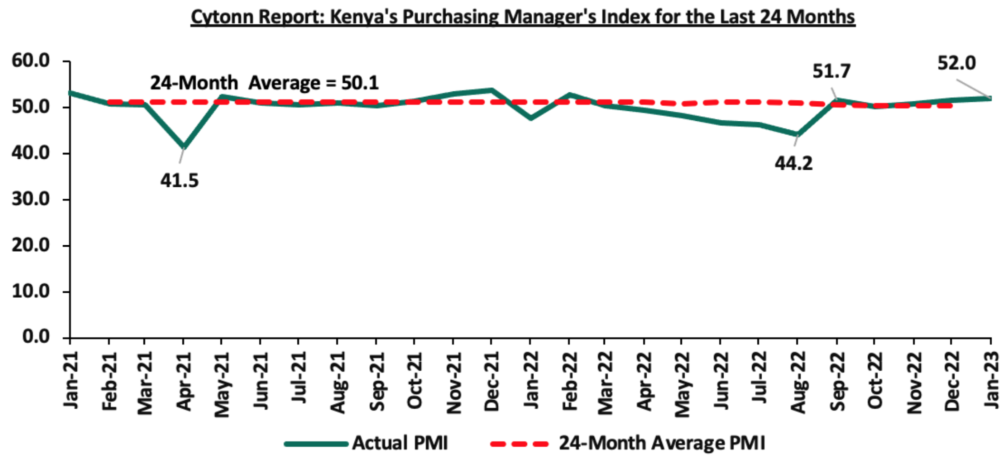


vii. The Committee noted the ongoing implementation of the FY2022/23 Government Budget, particularly the recent strong tax revenue collection reflecting enhanced tax administration efforts, evidenced by the revenue collections of Kshs 987.9 bn in the FY'2022/2023 as at the end of December, equivalent to 92.3% of its prorated target of Kshs 1.1 tn. The committee also noted the proposed FY2022/23 Supplementary Budget, and rationalization of expenditure which is expected to support the envisaged fiscal consolidation in the medium term.

The committee noted that, the impact of its move to tighten the monetary policy in November 2022 to anchor inflationary pressures was still in effect to the economy and therefore it concluded that the current stance on monetary policy was appropriate and decided to retain the Central Bank Rate at 8.75%. Additionally, the committee noted that the recent measures by the government to allow limited duty free imports on certain food items, such as maize, sugar and rice which are expected to moderate prices and consequently ease domestic inflationary pressures. However, we expect the inflationary pressures to remain elevated in the short term above the CBK's ceiling of 7.5% mainly on the back of high food and fuel prices, which are key components in headline inflation index. The Committee will meet again in March 2023, but will closely monitor the impact of the policy measures as well as development in domestic and global economy and take additional measures as necessary.

III. **Stanbic Bank Kenya January 2023 Purchasing Manager's Index (PMI)**

During the week, Stanbic bank released its monthly Purchasing Managers Index (PMI), highlighting that the index for the month of January 2023 came in at 52.0, up from 51.6 recorded in December 2022, pointing towards a sustained improvement in the business environment for a fifth consecutive month. The improvement is largely attributable to rising demand levels, as well as improved operating conditions which boosted business confidence. This was evidenced by solid increase in new business volume which rose at the quickest pace within a year. Additionally, high sales growth was registered in sectors such as; agriculture, manufacturing, services, and, wholesale & retail, while construction was the only sector to record a decline in sales for the second consecutive month. However, many businesses continued to struggle due to the elevated inflationary pressures, higher tax burdens, as well as, the persistent depreciation of the Kenya shilling against the US dollar which continued to raise the cost of production. The chart below summarizes the evolution of PMI over the last 24 months.



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

Going forward, we maintain a cautious outlook in the business environment in the short-term owing to the elevated inflationary pressures, as well as the persistent depreciation of the shilling, with the shilling having depreciated by 0.9% year to date against the dollar, adding to the 9.0% depreciation recorded in 2022. Despite the inflation rate in the month of January 2023 marginally easing to 9.0%, from 9.1% recorded in December 2022, it remained above the Central Bank of Kenya (CBK) upper ceiling of 7.5%, and thus it is expected to continue to weigh down economic activities as well as hampering consumer demand. Additionally, we expect the cost of production to remain elevated following the scaling down of the fuel subsidy and increased electricity prices due to high tariffs. Consequently, this will lead to high commodities prices thus exerting pressure on consumer wallet.

Monthly Highlights:

1. Stanbic Bank released its monthly Purchasing Manager's Index (PMI), highlighting that the index for the month of December picked up to a three-month high of 51.6, from 50.9 in November 2022, pointing towards a sustained improvement in the business environment for a fourth consecutive month. The rebound in business activity in the country is linked to factors such as increase in demand, favourable weather conditions and softer price pressures as firms saw input costs increase at the slowest rate in 12 months. For more information, please see our Cytonn Weekly #01/2023,
2. The National Treasury gazetted the revenue and net expenditures for the first half of FY'2022/2023, ending 30th December 2022, highlighting that the total revenue collected as at the end of December 2022 amounted to Kshs 987.9 bn, equivalent to 92.3% of the prorated estimates of Kshs 1070.8 bn. For more information, please see our Cytonn Weekly #02/2023,
3. The Energy and Petroleum Regulatory Authority (EPRA) released their monthly statement on the maximum retail fuel prices in Kenya effective 15th January 2023 to 14th February 2023. Notably, fuel prices remained unchanged for the second consecutive month at Kshs 177.3, Kshs 162.0 and Kshs 145.9 per litres of Super Petrol, Diesel and Kerosene, respectively. For more information, please see our Cytonn Weekly #02/2023,
4. The Kenya Revenue Authority released the draft regulations for the Excise Duty (Excisable Goods Management Systems)(Amendment) Regulations, 2023 having reviewed the previous Excise Duty (Excisable Goods Management Systems)(Amendment) Regulations, 2017, under the Excise Duty Act No. 23 of 2015, seeking to increase the stamp duty fees on various commodities. For more information, please see our Cytonn Weekly #03/2023, and,
5. The National Treasury released the Draft 2023 Budget Policy Statement, projecting a 59.2% increase in tax revenue in the medium term to Kshs 4.0 tn by the end of FY'2026/27 from the Kshs 2.5 tn original FY'2022/23 budget estimates. For more information, please see our Cytonn Weekly #03/2023,

Rates in the Fixed Income market have remained relatively stable due to the relatively ample liquidity in the money market. The government is 8.5% behind its prorated borrowing target of Kshs 351.6 bn having borrowed Kshs 321.8 bn of the Kshs 581.7 bn domestic borrowing target for the FY'2022/2023. We expect sustained gradual economic recovery as evidenced by the revenue collections of Kshs 987.9 bn in the FY'2022/2023 as at the end of December, equivalent to a 46.1% of its annual target of Kshs 2.1 tn, and 92.3% of its prorated target of Kshs 1.1 tn. Despite the performance, we believe that the projected budget deficit of 6.2% is relatively ambitious given the downside risks and deteriorating business environment occasioned by high inflationary pressures. We however expect the support from the IMF and World Bank to ease the need for elevated borrowing and thus help maintain a stable interest rate environment 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.
