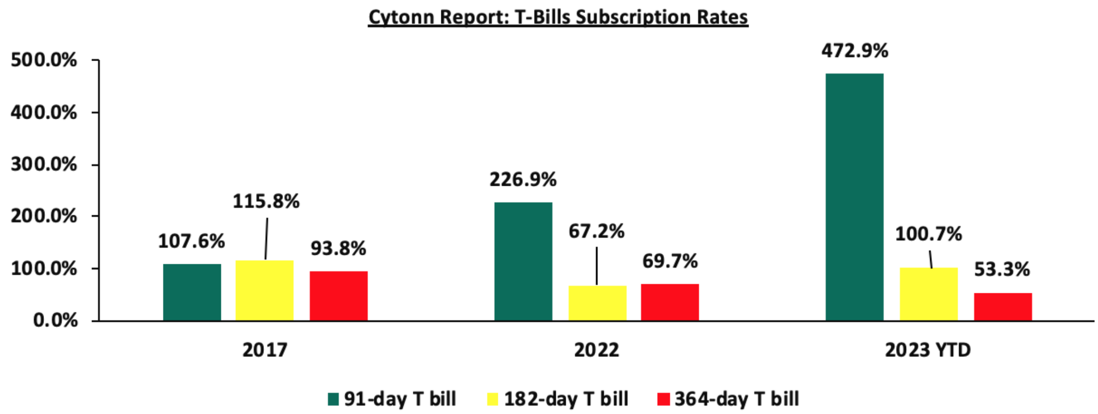
Nairobi Metropolitan Area Commercial Office Report 2023, & Cytonn Weekly #11/2023

Fixed Income

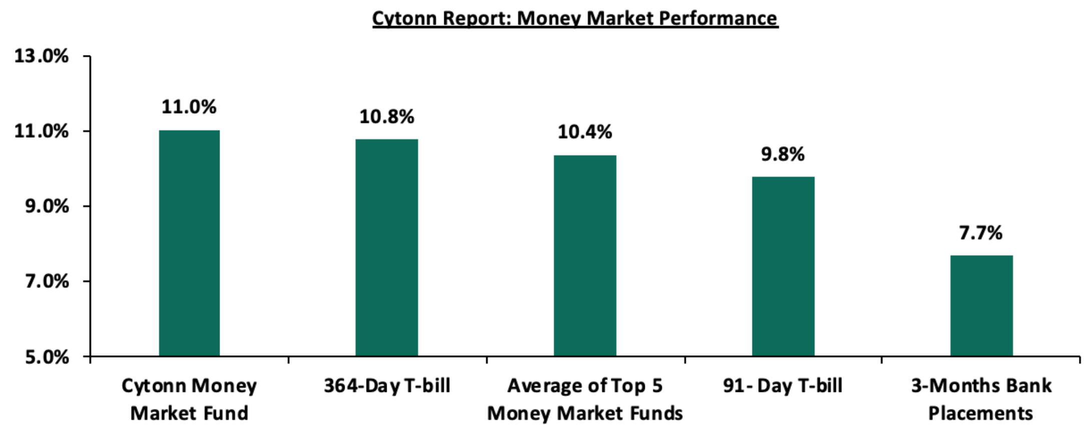
Money Markets, T-Bills Primary Auction:

During the week, T-bills remained oversubscribed, with the overall subscription rate coming in at 121.6%, albeit lower than the 148.5% recorded the previous week. Investor's preference for the shorter 91-day paper persisted as they sought to avoid duration risk, with the paper receiving bids worth Kshs 7.3 bn against the offered Kshs 4.0 bn, translating to an oversubscription rate of 182.3%, although significantly lower than the 501.0% recorded the previous week. Similarly, the 182-day paper recorded an oversubscription rate of 174.7%, a shift from the undersubscription rate of 79.1% recorded the previous week. On the other hand, the subscription rates for the 364-day paper declined to 44.3% from 76.8% recorded the previous week. The government accepted bids worth Kshs 28.8 bn out of the Kshs 29.2 bn total bids received, translating to an acceptance rate of 98.6%. The yields on the government papers were on an upward trajectory, with the yields on the 364-day paper, 182-day and 91-day papers increasing by 3.0 bps, 6.9 bps and 3.8 bps to 10.8%, 10.3% and 9.8%, respectively. The chart below compares the overall average T- bills subscription rates obtained in 2017, 2022 and 2023 Year to Date (YTD):



In the primary market the government was seeking to raise an additional Kshs 20.0 bn for infrastructural development by offering a tap sale of bond issue no. IFB1/2023/017 with tenor to maturity of 17.0 years. The bond received bids worth Kshs 12.7 bn translating to an undersubscription rate of 63.6% with the government accepting bids worth Kshs 12.7 bn translating to an acceptance rate of 100.0%. The average rate for the accepted bids and coupon rate for the bond is 14.4%. Additionally, the government re-opened three bonds FXD2/2018/10, FXD1/2022/03 and FXD1/2019/15 seeking to raise additional Kshs 50.0 bn for budgetary support. The government seeks to raise Kshs 20.0 bn through the FXD2/2018/10, with closure date for bidding set on 4th April, 2023 and Kshs 30.0 bn through the FXD1/2022/03 and FXD1/2019/15, with closure date for bidding set on 18th April, 2023. The bonds have tenors to maturity of 2.1 years, 5.8 years and 10.9 years for the FXD1/2022/03, FXD2/2018/10 and FXD1/2019/15 respectively, and coupon rates of 11.8%, 12.5% and 12.9% for the FXD1/2022/03, FXD2/2018/10 and FXD1/2019/15 respectively. We anticipate the bonds to be undersubscribed as investors seek to avoid duration risk, as well as concerns on the government's ability to sustain the current debt servicing costs. Our recommended bidding range for the bonds are; 12.6%-13.1% for FXD1/2022/03, 13.7%-14.2% for the FXD2/2018/10 and 13.9%-14.4% for the FXD1/2019/15 based on bonds of similar tenor trading range.

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 3.0 bps and 3.8 bps to 10.8% and 9.8% from 10.7% and 9.7% respectively, recorded the previous week. Similarly, the average yields of the Top 5 Money Market Funds increased by 5.4 bps to close the week at 10.4%, from 10.3% recorded the previous week. The yield on Cytonn Money Market Fund remained relatively unchanged at 11.0%, from what was recorded the previous week.



The table below shows the Money Market Fund Yields for Kenyan Fund Managers as published on 17th March 2023:

Cytonn Report: Money Market Fund Yield for Fund Managers as published on 17th March 2023

Rank	Fund Manager	Effective Annual Rate
1	Cytonn Money Market Fund (dial *809# or download Cytonn App)	11.0%
2	Dry Associates Money Market Fund	10.3%
3	Apollo Money Market Fund	10.2%
4	Madison Money Market Fund	10.2%
5	NCBA Money Market Fund	10.1%
6	Kuza Money Market fund	10.1%
7	Nabo Africa Money Market Fund	10.0%
8	Zimele Money Market Fund	9.9%
9	Sanlam Money Market Fund	9.9%
10	Old Mutual Money Market Fund	9.9%
11	KCB Money Market Fund	9.6%
12	Co-op Money Market Fund	9.6%

Cytonn Report: Money Market Fund Yield for Fund Managers as published on 17th March 2023

Rank	Fund Manager	Effective Annual Rate
13	AA Kenya Shillings Fund	9.6%
14	GenCap Hela Imara Money Market Fund	9.5%
15	Jubilee Money Market Fund	9.4%
16	CIC Money Market Fund	9.3%
17	GenAfrica Money Market Fund	9.3%
18	British-American Money Market Fund	9.3%
19	ICEA Lion Money Market Fund	8.8%
20	Orient Kasha Money Market Fund	8.8%
21	Absa Shilling Money Market Fund	8.2%
22	Mali Money Market Fund	8.2%
23	Equity Money Market Fund	6.6%

Source: Business Daily

Liquidity:

During the week, liquidity in the money markets tightened, with the average interbank rate increasing to 6.9% from 6.7% recorded the previous week, partly attributable to tax remittances that offset government payments. The average interbank volumes traded declined by 17.6% to Kshs 17.5 bn from Kshs 21.3 bn recorded the previous week.

Kenya Eurobonds:

During the week, the yields on Eurobonds were on an upward trajectory with the yield on the 7-year Eurobond issued in 2019 increasing the most, having gained by 2.3% points to 13.4% from 11.1% recorded the previous week. The rise in the country's Eurobond yields is mainly on the back of increased concerns about the United States dollar shortages currently experienced in the economy, coupled with increased debt servicing concerns and S&P Global Ratings downgrading of Kenya's outlook to negative from stable last month, citing a weakening liquidity position. The table below shows the summary of the performance of the Kenyan Eurobonds as of 16th March 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**	**0.9**	**1.2**	**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-Jan-23	12.9%	10.5%	10.9%	10.9%	10.8%	9.9%
1-Mar-23	12.1%	10.7%	11.0%	10.9%	10.8%	10.2%
9-Mar-23	11.8%	11.2%	11.3%	11.1%	11.3%	10.5%
10-Mar-23	11.9%	11.4%	11.4%	11.5%	11.4%	10.6%

Cytonn Report: Kenya Eurobonds Performance

	2014	2018		2019		2021
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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%**
13-Mar-23	12.4%	11.5%	11.5%	11.8%	11.6%	10.9%
14-Mar-23	12.9%	11.9%	11.7%	12.5%	11.8%	11.1%
15-Mar-23	13.2%	12.2%	11.9%	12.8%	12.1%	11.3%
16-Mar-23	14.0%	12.8%	12.3%	13.4%	12.5%	11.6%
Weekly Change	**2.2%**	**1.6%**	**1.0%**	**2.3%**	**1.2%**	**1.1%**
MTD Change	**1.9%**	**2.1%**	**1.3%**	**2.5%**	**1.7%**	**1.4%**
YTD Change	**1.1%**	**2.3%**	**1.4%**	**2.5%**	**1.7%**	**1.7%**

Source: Central Bank of Kenya (CBK) and National Treasury

Kenya Shilling:

During the week, the Kenya Shilling depreciated by 0.8% against the US dollar to close the week at Kshs 129.9, from Kshs 128.9 recorded the previous week, partly attributable to increased dollar demand from manufacturers and importers, especially oil and energy sectors against a slower supply of hard currency. On a year to date basis, the shilling has depreciated by 5.2% 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. The high crude oil prices have inflated Kenya's import bill and as a result, petroleum products imports have continued to weigh heavily on the country's import bill, and accounted for 27.6% of the total import bill in Q3'2022, up from 25.6% in Q2'2022 and much higher than 15.2% recorded in Q3'2021,
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,

The shilling is however expected to be supported by:

i. Diaspora remittances standing at a cumulative USD 658.6 mn in 2023 as of February 2023, albeit 0.3% lower than the USD 660.3 mn recorded over the same period in 2022.

Key to note, Kenya's forex reserves remained relatively unchanged at USD 6.6 bn as at 16th March 2023, similar to what was recorded the previous week. As such, the country's months of import cover also remained unchanged at 3.7 months, similar to what was recorded the previous week, and 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:

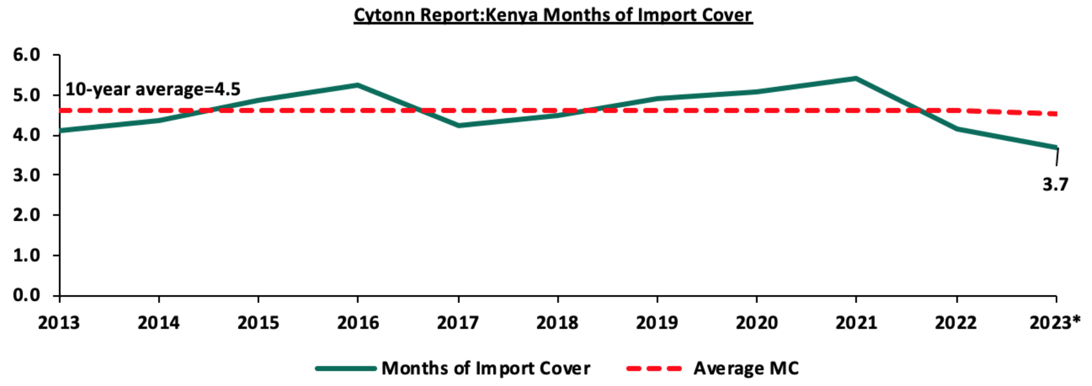

**Figure as at 16th March 2023*

Weekly Highlights:

I. **Revenue and Net Exchequer for FY'2022/23**

During the week, the National Treasury gazetted the revenue and net expenditures for the eight months of FY'2022/2023, ending 28th February 2023. Below is a summary of the performance:

Cytonn Report: FY'2022/2023 Budget Outturn - As at 28th February 2023

Amounts in Kshs billions unless stated otherwise

Item	12-months Original Estimates	Actual Receipts/Release	Percentage Achieved	Prorated	% achieved of prorated
Opening Balance		0.6			
Tax Revenue	2,071.9	1,236.2	59.7%	1,381.3	89.5%
Non-Tax Revenue	69.7	44.5	63.9%	46.4	95.9%
Total Revenue	**2,141.6**	**1,281.3**	**59.8%**	**1,427.7**	**89.7%**
External Loans & Grants	349.3	201.0	57.5%	232.9	86.3%
Domestic Borrowings	1,040.5	333.3	32.0%	693.6	48.0%
Other Domestic Financing	13.2	15.5	117.4%	8.8	176.1%
Total Financing	**1,403.0**	**549.8**	**39.2%**	**935.3**	**58.8%**
Recurrent Exchequer issues	1,178.4	726.9	61.7%	785.6	92.5%
CFS Exchequer Issues	1,571.8	756.5	48.1%	1,047.9	72.2%
Development Expenditure & Net Lending	424.4	162.6	38.3%	282.9	57.5%
County Governments + Contingencies	370.0	183.2	49.5%	246.7	74.3%
Total Expenditure	**3,544.6**	**1,829.1**	**51.6%**	**2,363.1**	**77.4%**
Fiscal Deficit excluding Grants	**1,403.0**	**547.8**	**39.0%**	**935.3**	**58.6%**
Total Borrowing	**1,389.8**	**534.3**	**38.4%**	**926.5**	**57.7%**

Source: National Treasury and Kenya Gazette

Key takeouts from the release include;

i. Total revenue collected as at the end of February 2023 amounted to Kshs 1,281.3 bn, equivalent to 59.8% of the original estimates of Kshs 2,141.6 bn for FY'2022/2023 and is 89.7% of the prorated estimates of Kshs 1,427.7 bn. We note that the government has not been able to meet its prorated revenue targets eight months into the FY'2022/2023 partly attributable to the tough macroeconomic environment in the country as a result of elevated inflationary pressures with

February 2023 coming in at 9.2%, above the CBK ceiling of 7.5%. Cumulatively, tax revenues amounted to Kshs 1,236.2 bn, equivalent to 59.7% of the original estimates of Kshs 2,071.9 bn and 89.5% of the prorated estimates of Kshs 1,381.3 bn,

ii. Total financing amounted to Kshs 549.8 bn, equivalent to 39.2% of the original estimates of Kshs 1,403.0 bn and is equivalent to 58.8% of the prorated estimates of Kshs 935.3 bn. Additionally, domestic borrowing amounted to Kshs 333.3 bn, equivalent to 32.0% of the original estimates of Kshs 1,040.5 bn and is 48.0% of the prorated estimates of Kshs 693.6 bn,

iii. The total expenditure amounted to Kshs 1,829.1 bn, equivalent to 51.6% of the original estimates of Kshs 3,544.6 bn, and is 77.4% of the prorated target expenditure estimates of Kshs 2,363.1 bn. Additionally, the net disbursements to recurrent expenditure came in at Kshs 726.9 bn, equivalent to 61.7% of the original estimates of Kshs 1,178.4 bn and 92.5% of the prorated estimates of Kshs 785.6 bn,

iv. Consolidated Fund Services (CFS) Exchequer issues (refers to the Consolidated Fund established in the Kenya's constitution into which development partners deposit funds before disbursing to the Exchequer accounts for projects such as servicing of public debt, payment of pensions and gratuities, salaries and allowances and subscription to International Organizations) came in at Kshs 756.5 bn, equivalent to 48.1% of the original estimates of Kshs 1,571.8 bn, and 72.2% of the prorated amount of Kshs 1,047.9 bn. The cumulative public debt servicing cost amounted to Kshs 694.0 bn which is 49.8% of the original estimates of Kshs 1,393.1 bn, and is 74.7% of the prorated estimates of Kshs 926.5 bn. Notably, the Kshs 694.0 bn debt servicing cost is equivalent to 54.2% of the actual revenues collected as at the end of February 2023, further emphasizing on how much public debt servicing weighs on the country's expenditure. Additionally, Recurrent Exchequer issues came in at Kshs 726.9 bn equivalent to 61.7% of the original estimates of Kshs 1,178.4 bn and are 92.5% of the prorated estimates of Kshs 785.6, and,

v. Total Borrowings as at the end of February 2023 amounted to Kshs 534.3 bn, equivalent to 38.4% of the original estimates of Kshs 1,389.8 bn for FY'2022/2023 and are 57.7% of the prorated estimates of Kshs 926.5 bn. The cumulative domestic borrowing target of Kshs 1,040.5 bn comprises of adjusted Net domestic borrowings of Kshs 579.1 bn and Internal Debt Redemptions (Roll-overs) of Kshs 461.4 bn.

The government has been unable to meet its revenue prorated targets for the eight months of the FY'2022/2023 on the back of the tough economic situation exacerbated by the elevated inflationary pressures that have remained above the CBK ceiling of 7.5%, with the year on year inflation rate in February 2023 coming in at 9.2%. Notably, the situation is further aggravated by the US dollar shortage that is currently experienced in the economy, resulting in high consumer prices as companies pass the high cost of import and production to consumers by hike in commodities prices. The February Purchasing Managers Index (PMI) also pointed towards a solid deterioration in operating condition with the index registering at 46.6, the first time in six months the index came below the 50.0 no change threshold. In a bid to expand its revenue base and seal tax leakage, the government through the Kenya Revenue Authority recently suspended all tax relief payments. The agency also disclosed that in the past five years it had granted total tax reliefs and incentives amounting to Kshs 610.0 bn, translating to an average of Kshs 122.0 per year which had continued to weigh down the government's tax collections. We still hold the view that the government revenue targets are relatively ambitious, owing to the current tough economic situation which is expected to continue to impede revenue collection efforts as firms' records low commodities demand as consumers cut back on spending.

II. **Fuel Prices**

During the week, the Energy and Petroleum Regulatory Authority (EPRA) released their monthly statement on the maximum retail fuel prices in Kenya effective 15th March 2023 to 14th April 2023. Notably, prices of Super Petrol increased by Kshs 2.0 per litre to Kshs 179.3, while prices of Diesel and Kerosene remained unchanged for the fourth consecutive month at Kshs 162.0 and Kshs 145.9

per litres, respectively. Other key take-outs from the performance include;

i. The average landed costs of super-petrol, diesel and kerosene by 0.1%, 2.5% and 1.5% to USD 659.5 per cubic metre, USD 759.9 per cubic metre and USD 763.3 per cubic metre in February 2023, from USD 659.9 per cubic metre, USD 779.5 per cubic metre and USD 775.0 per cubic metre in January 2023, respectively,
ii. The Free On Board (FOB) price of Murban crude oil declined by 11.9% to USD 80.1 per barrel in February 2023 from USD 90.9 per barrel recorded in January 2023,
iii. The Kenyan Shilling depreciated against the US Dollar by 2.6% to Kshs 134.0 in February 2023 from 130.6 in January 2023, and,
iv. The price of diesel has been cross subsidized with that of super-petrol, while maintaining a subsidy of Kshs 23.5 per litre on Kerosene in order to cushion consumers from the otherwise high prices.

Key to note, EPRA maintained the Kshs 12.4 per litre margin to Oil Marketing Companies for Super Petrol and increased Diesel margins by 16.0% to Kshs 2.9 per litre from 2.5 per litre, while Kerosene margins remained withheld. This is attributable to super-petrol recording a price stabilization surplus of Kshs 9.0 per litre, diesel remaining balanced, while kerosene recorded a deficit of Kshs 9.4 per litre.

Notably, despite the global fuel prices dropping by 37.3% to USD 73.8 per barrel as of 16th March 2023, from a peak of USD 117.7 per barrel recorded on 1st June 2022, and the average landed costs declining during the month, the prices of super-petrol in the country increased while prices of diesel and kerosene remain elevated based on historical levels. This is mainly attributable to the decision by the government to scale down fuel subsidies coupled with the US dollar shortage being experienced in the economy driven by elevated cost of fuel import. In a bid to alleviate the high demand of US dollar by petroleum importers which consequently leads to high cost of fuel importation, the government signed a deal with foreign government-owned fuel producers’ entities, the Saudi Aramco (ARAMCO), Abu Dhabi National Oil Company (ADNOC) and Emirates National Oil Company (ENOC) to supply Kenya with diesel and super petrol for the next six months on credit. In our view, it is only a temporary fix, and unless the government expedites measures to buffer foreign reserves and resuscitate the currently frail interbank forex market, the economy will once again be hit by elevated US dollar demand 6 months down the line. Furthermore, we still hold the view that, as a measure of fiscal consolidation, the government should eliminate the fuel subsidies, which continue to weigh on its expenditure.

Rates in the Fixed Income market have remained relatively stable due to the relatively ample liquidity in the money market. The government is 6.6% behind its prorated borrowing target of Kshs 418.7 bn having borrowed Kshs 391.2 bn of the Kshs 581.7 bn borrowing target for the FY’2022/2023. We believe that the projected budget deficit of 5.7% is relatively ambitious given the downside risks and deteriorating business environment occasioned by high inflationary pressures. Further, revenue collections are lagging behind, with total revenue as at February 2023 coming in at Kshs 1.3 tn in the FY’2022/2023, equivalent to 59.8% of its target of Kshs 2.1 tn and 89.7% of the prorated target of Kshs 1.4 tn. Therefore, we expect a continued upward readjustment of the yield curve in the short and medium term, with the government looking to bridge the fiscal deficit through the domestic market. Owing to this, our view is that investors should be biased towards short-term fixed-income securities to reduce duration risk.

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