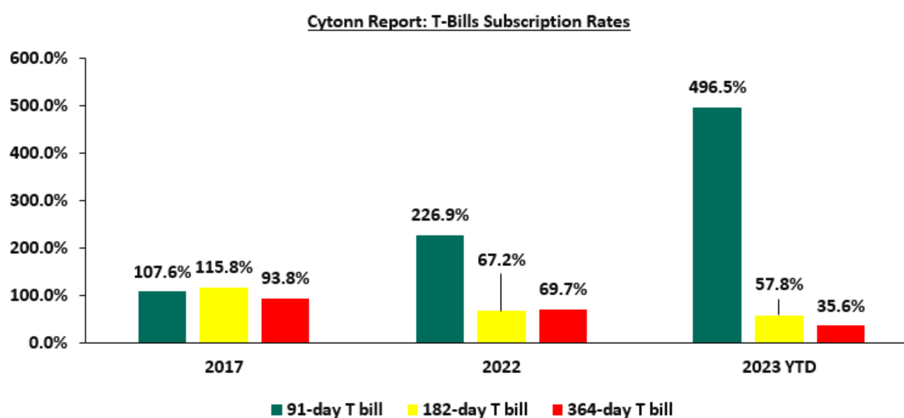
Education Investment Plans in Kenya, & Cytonn Weekly #29/2023

Fixed Income

Money Markets, T-Bills Primary Auction:

During the week, T-bills were oversubscribed for the third consecutive week, with the overall subscription rate coming in at 164.5%, up from an oversubscription rate of 151.8% 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 28.5 bn against the offered Kshs 4.0 bn, translating to an oversubscription rate of 711.6%, albeit lower than the 833.1% recorded the previous week. The subscription rate for the 364-day and 182-day papers increased to 23.8% and 86.4% respectively, up from 17.7% and 13.5% recorded the previous week. The government accepted a total of Kshs 36.7 bn worth of bids out of Kshs 39.5 bn of bids received, translating to an acceptance rate of 92.9%. The yields on the government papers continued to rise, with the yields on the 364-day, 182-day, and 91-day papers increasing by 25.6 bps, 5.1 bps, and 12.4 bps to 12.7%, 12.3%, and 12.2%, respectively. The chart below compares the overall average T- bills subscription rates obtained in 2017, 2022 and 2023 Year to Date (YTD):

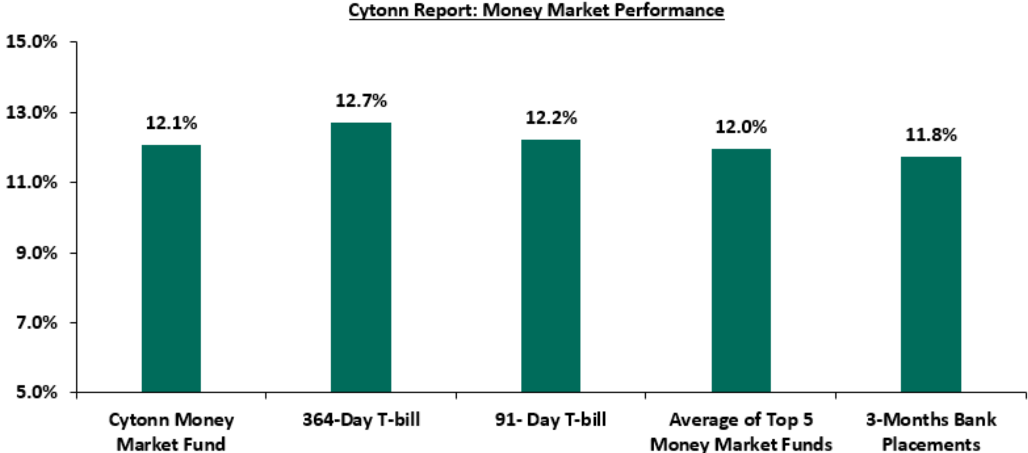


In the primary market, the Central Bank of Kenya released the auction results for the tap sale of the re-opened bond FXD1/2016/10 with a 3.2-year tenor to maturity and the newly issued bond FXD1/2023/05 with a tenor to maturity of 5 years. The tap sale was oversubscribed, receiving bids worth Kshs 44.4 bn against the offered Kshs 20.0 bn, translating to a 222.1% oversubscription rate. The government accepted bids worth Kshs 43.4 bn, translating to an acceptance rate of 97.8%. The coupon rates for FXD1/2016/10 and FXD1/2023/05 are 15.0% and 16.8%, respectively, and the allocated average rates for accepted bids are 16.3% and 16.8% for FXD1/2016/10 and FXD1/2023/05, respectively.

Money Market Performance:

In the money markets, 3-month bank placements ended the week at 11.8% (based on what we have been offered by various banks), while the yields on the 364-day and 91-day papers increased by 25.6

bps and 12.4 bps to 12.7% and 12.2%, respectively. The yield of the Cytonn Money Market Fund decreased by 1.0 bp to remain relatively unchanged at 12.1% from what was recorded the previous week. However, the average yields of the Top 5 Money Market Funds increased by 31.4 bps to 12.0% from 11.6% recorded the previous week:



The table below shows the Money Market Fund Yields for Kenyan Fund Managers as published on 21 July 2023:

Cytonn Report: Money Market Fund Yield for Fund Managers as published on 21st July 2023

Rank	Fund Manager	Effective Annual Rate
1	Etica Money Market Fund	12.4%
2	**Cytonn Money Market Fund (dial *809# or download Cytonn App)**	**12.1%**
3	Enwealth Money Market Fund	12.1%
4	Madison Money Market Fund	11.8%
5	GenAfrica Money Market Fund	11.5%
6	GenCap Hela Imara Money Market Fund	11.4%
7	Jubilee Money Market Fund	11.4%
8	Old Mutual Money Market Fund	11.3%
9	Co-op Money Market Fund	11.2%
10	AA Kenya Shillings Fund	11.0%
11	Apollo Money Market Fund	11.0%
12	Kuza Money Market fund	10.9%
13	Nabo Africa Money Market Fund	10.8%
14	Sanlam Money Market Fund	10.8%
15	ICEA Lion Money Market Fund	10.5%
16	Dry Associates Money Market Fund	10.4%
17	KCB Money Market Fund	10.3%
18	NCBA Money Market Fund	10.3%

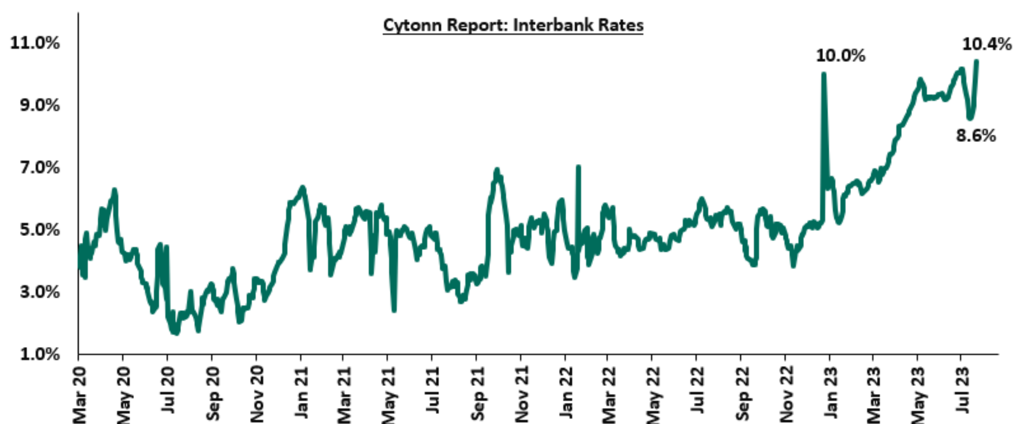
Cytonn Report: Money Market Fund Yield for Fund Managers as published on 21st July 2023

Rank	Fund Manager	Effective Annual Rate
19	CIC Money Market Fund	10.0%
20	Absa Shilling Money Market Fund	10.0%
21	Zimele Money Market Fund	9.9%
22	British-American Money Market Fund	9.8%
23	Orient Kasha Money Market Fund	9.4%
24	Mali Money Market Fund	9.1%
25	Equity Money Market Fund	8.5%

Source: Business Daily

Liquidity:

During the week, liquidity in the money markets tightened, with the average interbank rate increasing to 9.4% from 8.8% recorded the previous week, partly attributable to tax remittances that offset government payments. The average interbank volumes traded increased by 22.6% to Kshs 21.8 bn from Kshs 17.8 bn recorded the previous week. The chart below shows the interbank rates in the market over the years:



Source: CBK

Kenya Eurobonds:

During the week, the yields on Eurobonds recorded mixed performance, with the yield of the 10-year Eurobond issued in 2014 increasing the most by 0.3% points to 12.8% from 12.5% recorded the previous week. The table below shows the summary of the performance of the Kenyan Eurobonds as of 20th July 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)	**2.0 bn**	**1.0 bn**	**1.0 bn**	**0.9 bn**	**1.2 bn**	**1.0 bn**
Years to Maturity	**0.9**	**4.6**	**24.7**	**3.8**	**8.9**	**10.5**
Yields at Issue	**6.6%**	**7.3%**	**8.3%**	**7.0%**	**7.9%**	**6.2%**
02-Jan-23	12.9%	10.5%	10.9%	10.9%	10.8%	9.9%
03-Jul-23	12.5%	11.0%	11.0%	11.2%	11.0%	10.3%
13-Jul-23	12.5%	11.5%	11.4%	11.9%	11.4%	10.8%
14-Jul-23	12.6%	11.5%	11.4%	11.9%	11.4%	10.8%
17-Jul-23	12.7%	11.5%	11.4%	12.0%	11.4%	10.8%
18-Jul-23	12.6%	11.5%	11.4%	12.0%	11.4%	10.8%
19-Jul-23	12.5%	11.4%	11.4%	11.9%	11.4%	10.8%
20-Jul-23	12.8%	11.4%	11.3%	12.0%	11.3%	10.8%
Weekly Change	**0.3%**	**(0.1%)**	**(0.1%)**	**0.1%**	**(0.0%)**	**0.1%**
MTD Change	**0.3%**	**0.5%**	**0.3%**	**0.8%**	**0.4%**	**0.5%**
YTD Change	**(0.1%)**	**0.9%**	**0.4%**	**1.1%**	**0.6%**	**1.0%**

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

Kenya Shilling:

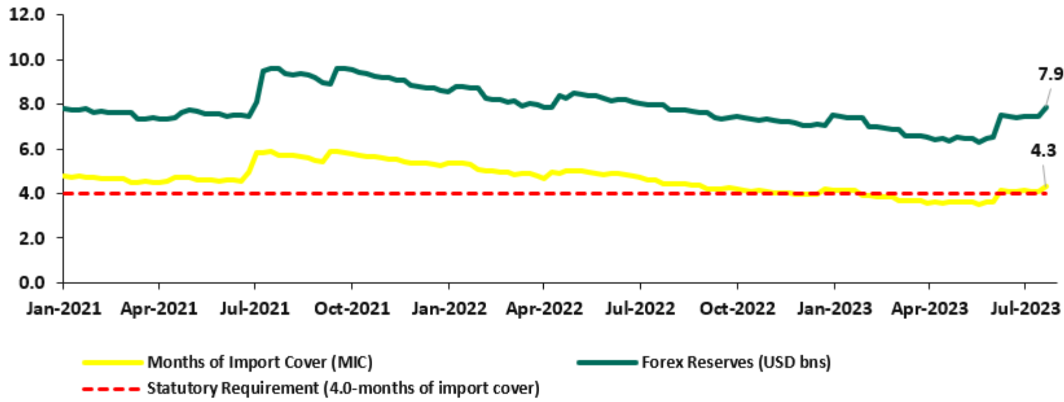
During the week, the Kenya Shilling remained under pressure, having depreciated by 0.3% against the US dollar to close the week at Kshs 141.8 from Kshs 141.4 recorded the previous week, partly attributable to the persistent high dollar demand from importers, especially in the oil and energy sectors. On a year-to-date basis, the shilling has depreciated by 14.9% 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. An ever-present current account deficit, which came at 2.3% of GDP in Q1'2023 from 4.2% recorded in a similar period last year, and,
ii. The need for government debt servicing, continues to put pressure on forex reserves given that 66.8% of Kenya's external debt is US Dollar denominated as of April 2023, and,

The shilling is however expected to be supported by:

i. Diaspora remittances standing at a cumulative USD 2,033.8 mn in 2023 as of June 2023, albeit 0.5% lower than the USD 2,044.6 mn recorded over the same period in 2022, and,
ii. The tourism inflow receipts which came in at Kshs 268.1 bn in 2022, a significant 82.9% increase from Kshs 146.5 bn inflow receipts recorded in 2021.
iii. Sufficient forex reserves currently at USD 7.9 bn (equivalent to 4.3-months of import cover), which is above the statutory requirement of maintaining at least 4.0-months of import cover.

The chart below summarizes the evolution of Kenya months of import cover over the years:



Weekly Highlights:

I. **International Monetary Fund (IMF) Loan facility**

During the week, the International Monetary Fund (IMF) announced that it had completed the fifth review of the 38-month Extended Fund Facility (EFF) and Extended Credit Facility (ECF) financing for Kenya allowing for an immediate disbursement of USD 415.4 mn (Kshs 58.9 bn), inclusive of USD 110.3 mn (Kshs 15.6 bn) from an augmentation of access. The board also approved Kenya's request for a 20-month arrangement under the Resilience and Sustainability Facility (RSF), amounting to USD 551.4 mn (Kshs 78.1 bn) in a bid to build resilience against the impacts of climate change and attract additional private investment towards climate-related initiatives. Additionally, the board approved a 10-month extension of the current 38-month EFF/ECF arrangements to a 48-month arrangement running through to April 2025 to allow the government sufficient time to implement its economic reform agenda. The disbursement brings the total amount disbursed under the EFF and ECF arrangements to USD 2,056.6 mn (Kshs 291.2 bn). To the country's reprieve, the Board approved changes to program conditions, waivers of non-observance of the continuous performance criteria on accumulation of external arrears and end-June 2023 tax revenue target, and waivers of applicability for all other end-June 2023 and continuous quantitative performance criteria. While concluding the review, the IMF commended Kenya's economic resilience despite going through the worst drought in many decades and the challenging economic environment, and lauded the government's commitment to robust policies, such as the approval of the FY2023/24 Budget and the 2023 Finance Act, to sustain reforms that promote resilient and inclusive growth. The Board expressed continued support for Kenya's positive medium-term prospects. The table below shows the funding the government has received so far out of the original amount:

Cytonn Report: International Monetary Fund (IMF) EFF and ECF Financing Programme

Date	Amount Received (USD mn)	Amount Received (Kshs bn, 1 USD= Kshs 141.6)
Apr-21	307.5	43.5
Jun-21	407.0	57.6
Dec-21	258.1	36.5
Jul-22	235.6	33.4
Nov-22	433.0	61.3
Jul-23	415.4	58.8
Total Amount Received	**2,056.6**	**291.2**
Amount Pending	**283.4**	**40.1**

The disbursement is expected to shore up and increase the country’s foreign exchange reserves, which have been under pressure during the first half of the year, and consequently help support the Kenya shilling from further depreciation, which has depreciated by 14.9% year to date. Additionally, the loan disbursement will support the country’s Medium Term Debt Strategy, which aims to optimize the use of concessional loans and reduce the use of costly commercial loans, and the new administration’s plans to cut public expenditure to reduce the budget deficit. According to the IMF, Kenya’s economy growth rate is projected to improve to 5.0% in 2023 from the 4.8% growth rate recorded in 2022, mainly attributable to favourable weather conditions boosting agricultural production, which is one of Kenya’s main GDP contributors. However, the tighter fiscal and monetary environment, such as the suspension of subsidies and increased taxes, put in place by the national treasury to maintain macroeconomic stability and the ongoing political tension disrupting supply chains are expected to weigh on growth in the year.

II. **Kenya’s Fitch Ratings**

During the week, Fitch Ratings, a global credit rating agency, revised the outlook on Kenya's Long-Term Foreign-Currency Issuer Default Rating (IDR) to negative from stable and affirmed the IDR at 'B', mainly due to external financing constraints amid high funding requirements, including a USD 2.0 bn Eurobond maturity in 2024, weakening forex reserves, rising financing costs, and uncertainty regarding the fiscal trajectory. Notably, this confirms the global ratings agency Moody's decision in May 2023 to cut Kenya's senior unsecured debt rating as well as long-term foreign-currency and local-currency issuer ratings to B3 from B2 mainly due to an increase in government liquidity risks.

According to Fitch Ratings, the downgrade in Kenya’s IDR was on the back of:

i. **Increased External Financing Challenges**: Kenya’s external debt service costs is expected to rise sharply by 53.6% to USD 4.3 bn in FY’2023/2024 up from USD 2.8 bn that was spent on debt service in the previous year, FY’2022/2023. The high debt servicing cost is mainly due to the USD 2.0 bn Eurobond maturing in June 2024. Due to the expected continuation of the global tightening cycle, Kenya is likely to face headwinds in servicing the Eurobond since the government plans to refinance the Eurobond in external markets,
ii. **Increased Pressures on Reserves:** The forex reserves remain under pressure despite the recovery and the disbursements from the IMF due to increased commercial demands. Notably, for the majority of the first half of the year, the Forex Reserves remained below the statutory minimum requirement of maintaining at least 4 months of import cover. Fitch projects that reserves will decline further to USD 7.0 bn which translates to 2.8 months of import cover at the end of 2024, below the projected ‘B’ median (3.4 months), reflecting financing constraints and persistent depreciation pressures on the Kenyan Shilling,
iii. **High Debt and Currency Risk:** Fitch estimates that the government Debt to GDP ratio rose by 3.7% points, to 71.0% in FY’2022/2023 from 67.3% in FY’2021/22, mainly due to currency risk since half of Kenya’s debt is foreign currency denominated and 66.8% of external debt is denominated in USD as of April 2023. Therefore, the continued depreciation of the Kenya shillings continues to inflate external debt in local currency terms , with the shilling having depreciated by 14.9% year to date. Additionally, following the parliament's approval of the debt to GDP anchor of 55.0% in terms of present value, to replace the current nominal benchmark debt ceiling of Kshs 10.0 tn, Fitch projects government debt to decline to 68.5% of GDP in 2025,
iv. **Tighter Domestic Financing Conditions:** The country’s inability to access international markets in recent years has increased its reliance on domestic financing, putting upward pressure on interest costs, mainly on the back of tight monetary policy. Shorter-dated government paper yields have increased, with the 91-day, 182-day, and 364-day papers all having yields above 12.0%. As a result, the sustainability of debt is at risk due to the rising trend in debt servicing costs. Fitch projects government interest payments to reach 28% of revenue in FY’2024/2025, about 3 times the current ‘B’ median forecast of 10.0%,

v. **Fiscal Consolidation Faces Risks:** The government has remained committed to fiscal consolidation, with Fitch projecting the budget deficit to decline to 5.5% of GDP FY’2024/2025 from an estimate of 6% of GDP in FY’2023/2024. However, the budget spending cuts are expected to experience offsetting pressure from rising government costs, especially increases in debt servicing costs and government pensions and gratuities. Additionally, the Finance Bill 2023, which seeks to enhance revenue mobilization through measures such as increasing the VAT rate on petroleum products, continues to face execution challenges due to protests and legal challenges. Therefore, further delays could undermine the government's fiscal consolidation strategy, increase financing needs, and negatively impact domestic financing conditions,

vi. **Protests Threaten the Socio-Political Climate:** The ongoing anti-government protests addressing the high cost of living, fueled by the Finance Bill 2023 present heightened social pressures on the government.

vii. **Elevated Inflation amidst Currency Depreciation**: Inflation has persistently remained above the Central Bank of Kenya's (CBK) inflation target band of 2.5-7.5%, in the last 13 months to June 2023, mainly due to high food and energy prices amid the weaker shilling. Currently, inflation rate stands at 7.9% as of June 2023, and Fitch forecasts that average annual inflation will rise by 0.4% points, to 8.0% in 2023 from 7.6% in 2022, before falling back below 7.0% in 2024.

The agency noted that despite the ongoing policy tightening, higher inflation, and external headwinds, the Kenyan economy remains resilient. The economic growth slowed down to 4.8% in 2022 compared to a growth rate of 7.6% in 2021 and this remains strong. As such, the agency expects economic growth to rebound to 5.2% in 2023, supported by growth in the services sector and improved weather conditions expected to support the agriculture sector.

Rates in the Fixed Income market have been on an upward trend given the continued high demand for cash by the government and the occasional liquidity tightness in the money market. The government is 61.0% ahead its prorated net domestic borrowing target of Kshs 37.8 bn, having a net borrowing position of Kshs 60.9 bn of the domestic net borrowing target of Kshs 598.3 bn for the FY’2023/2024. 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