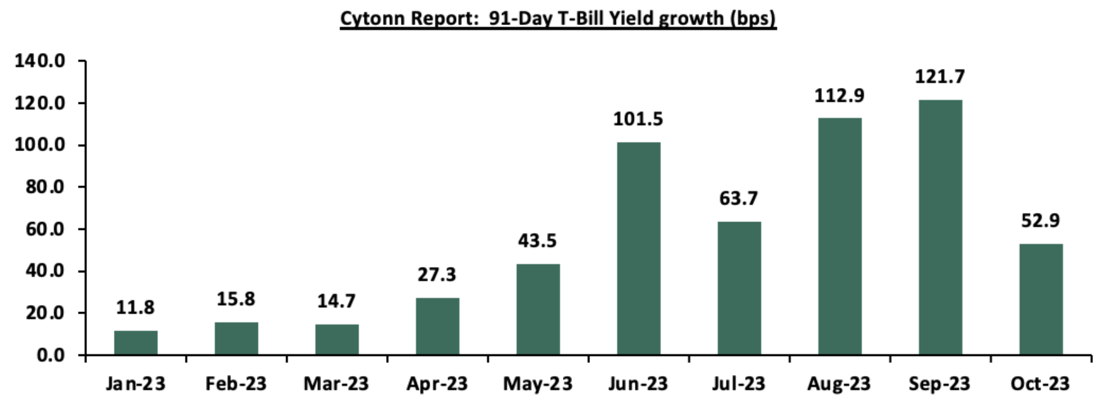
Cytonn Monthly - October 2023

Fixed Income

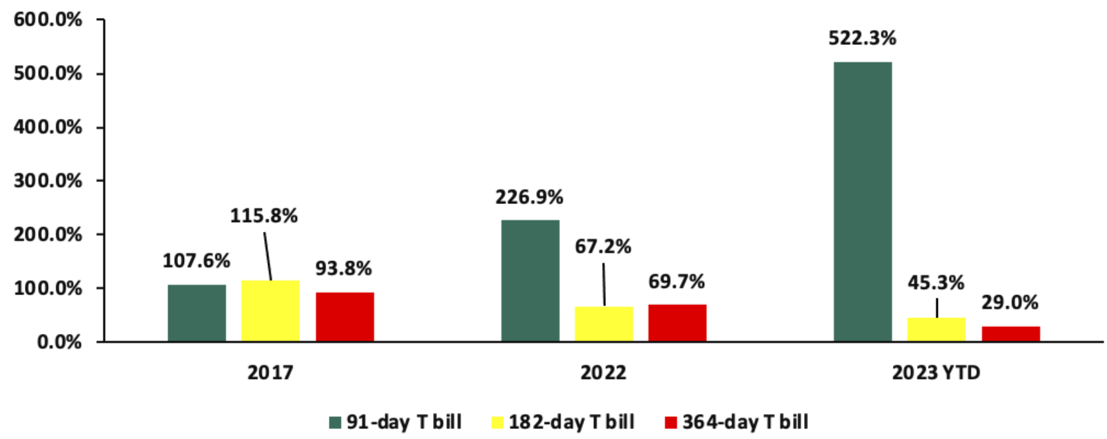
Money Markets, T-Bills Primary Auction:

During the month of October 2023, T-bills were oversubscribed, with the overall average subscription rate coming in at 129.3%, up from the undersubscription rate of 98.3% recorded in September 2023. The overall average subscription rates for the government papers increased with the 364-day, 182-day and 91-day papers increasing to 25.6%, 34.1% and 626.7%, from 22.4%, 10.6% and 507.5% respectively, which was recorded in September 2023. The average yields on the 364-day paper increased by 0.6% points to 15.3%, while the average yield on the 182-day and 91-day papers increased by 0.5% points each to 15.1% and 15.0% respectively. For the month of October, the government accepted a total of Kshs 111.3 bn of the Kshs 124.1 bn worth of bids received, translating to an acceptance rate of 89.6%. Notably, the growth in the government papers yields slowed down in October compared to September, with the yields on the 91-day paper growing by 52.9 bps, compared to 121.7 bps growth that was recorded in September, as the government tries to minimize debt cost through avoiding highly priced bids. The chart below shows the yields growth rate for the 91-day paper during the year:



This week, T-bills were oversubscribed, with the overall subscription rate coming in at 102.8%, higher than the undersubscription rate of 75.6% recorded the previous week. Investors' preference for the shorter 91-day paper persisted, with the paper receiving bids worth Kshs 22.5 bn against the offered Kshs 4.0 bn, translating to an oversubscription rate of 562.0%, higher than the oversubscription rate of 266.0% recorded the previous week. The subscription rates for the 182-day and 364-day papers decreased to 12.8% and 9.1%, from 56.7% and 18.4% respectively, recorded the previous week. The government accepted a total of Kshs 23.7 bn worth of bids out of Kshs 24.7 bn of bids received, translating to an acceptance rate of 96.1%. The yields on the government papers were on an upward trajectory, with the yields on the 364-day, 182-day and 91-day papers increasing by 5.2 bps, 14.2 bps and 7.5 bps to 15.4%, 15.3% and 15.2%, respectively; The chart below compares the overall average T- bills subscription rates obtained in 2017, 2022 and 2023 Year to Date (YTD):

Cytonn Report: T-Bills Subscription Rates



Additionally, October 2023 bonds were undersubscribed, with the overall subscription rate coming in at 31.5%, albeit lower than the undersubscription rate of 97.2% recorded in September 2023. The tapsales for the bonds FXD1/2023/02 and FXD1/2016/10 received bids worth Kshs 3.4 bn against the offered Kshs 15.0 bn, translating to an undersubscription rate of 23.0%, with the government accepting bids worth Kshs 3.4 bn, translating to an acceptance rate of 97.9%. The subsequent reopened bonds FXD1/2023/02 and FXD1/2023/05 received bids worth Kshs 12.3 bn against the offered Kshs 35.0 bn, translating to an undersubscription rate of 35.1%, with the government accepting bids worth Kshs 6.3 bn translating to an acceptance rate of 51.3%. The table below provides more details on the bonds issued during the month of October 2023:

Cytonn Report: Treasury Bonds Issued in October 2023

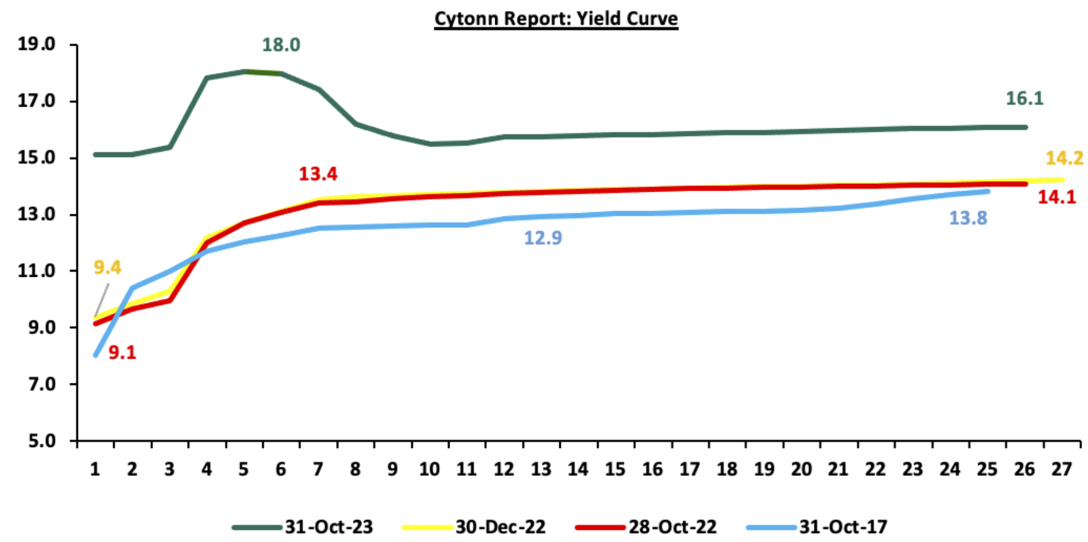
Issue Date	Bond Auctioned	Effective Tenor to Maturity (Years)	Coupon	Amount offered (Kshs bn)	Actual Amount Raised/Accepted (Kshs bn)	Total bids received (Subscription)	Average Accepted Yield	Subscription Rate	Acceptance Rate
10/2/2023	FXD1/2023/02- Tapsale	1.9	17.0%	15.0	2.6	2.6	17.5%	23.0%	**99.2%**
	FXD1/2016/10- Tapsale	2.9	15.0%		0.8	0.8	17.9%		**93.7%**
10/16/2023	FXD1/2023/02-Reopened	1.9	17.0%	35.0	4.8	6.5	17.7%	35.1%	**74.2%**
	FXD1/2023/05-Reopened	4.8	16.8%		1.5	5.8	18.0%		**25.6%**
Oct 2023 Average		**2.9**	**16.5%**	**50.0**	**9.7**	**15.7**	**17.8%**	**31.5%**	**61.5%**
Sep 2023 Average		**2.4**	**16.0%**	**35.0**	**21.6**	**34.0**	**17.7%**	**97.2%**	**63.6%**

Source: Central Bank of Kenya (CBK)

In the primary bond market, the government is seeking to raise additional Kshs 50.0 bn for infrastructure projects support in the FY'2023/24 by issuing the new 6.5-year bond IFB1/2023/6.5 with a tenor to maturity of 6.5 years. The bidding process opened on 20th October 2023 and will close on 8th November 2023, with the coupon rate to be determined by the market. The bonds value date will be 13th November 2023, with a maturity date of 6th May 2030 and will be tax free as is the case for infrastructure bonds as provided for under the Income Tax Act. We anticipate the bond to be oversubscribed, given that it is tax free in nature, however, investors are expected to attach higher yields as they seek to cushion themselves against future losses on the back of the government's debt sustainability concerns. Notably, the last infrastructure bond to be issued was the 7-year IFB1/2023/07 in June 2023 which sought to raise Kshs 60.0 bn. The bond registered an oversubscription rate of 367.5%, at a yield of 15.8%. Based on trading of bonds of similar tenor and nature, we expect the IFB1/2023/6.5 to price at 16.3%-16.7%.

Secondary Bond Market:

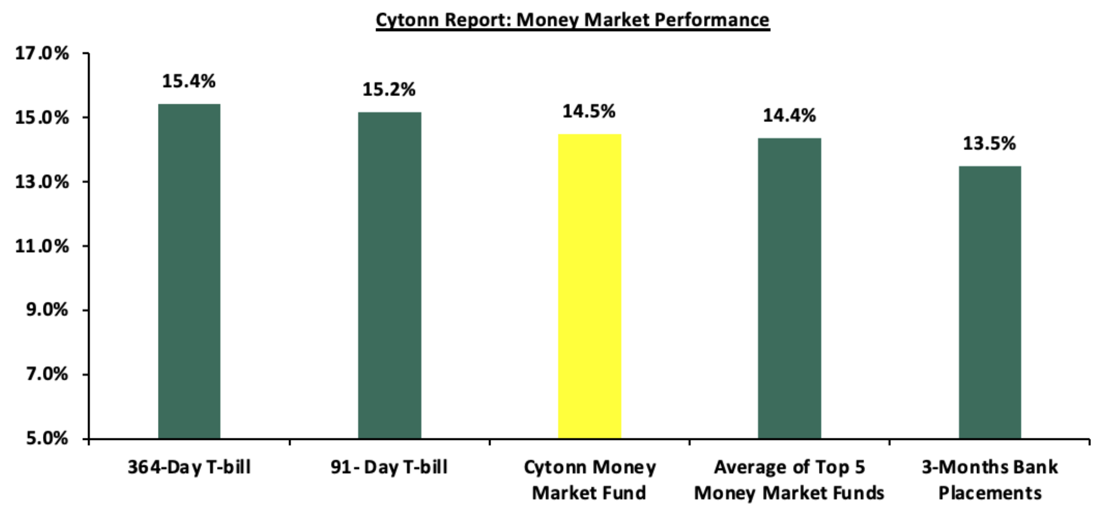
The yields on the government securities were on an upward trajectory during the month compared to the same period in 2022. Notably, the yields on short to medium-term government bonds continue to rise faster than the yield on the long-term bonds as investors avoid long-term duration risk, and attaching higher yields as they seek to cushion themselves against future losses on the back of the government's debt sustainability concerns, ahead of the upcoming USD 2.0 bn Eurobond maturity in June,2024. The chart below shows the yield curve movement during the period:



The secondary bond turnover decreased by 33.3% to Kshs 64.2 bn, from Kshs 96.2 bn recorded in September 2023, pointing towards decreased activities by commercial banks in the secondary bonds market. On a year on year basis, the bonds turnover increased by 11.5% from Kshs 57.6 bn worth of treasury bonds transacted over a similar period last year.

Money Market Performance:

In the money markets, 3-month bank placements ended the week at 13.5% (based on what we have been offered by various banks), The yield on the 364-day paper increased by 5.2 bps to 15.4%, while that of 91-day paper increased by 7.5 bps to 15.2%. The yield of Cytonn Money Market Fund decreased by 1.0 bps to stay relatively unchanged at 14.5% and the average yields on the Top 5 Money Market Funds increased by 22.8 bps to 14.4% from 14.1% recorded the previous week.



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

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

Rank	Fund Manager	Effective Annual
1	GenAfrica Money Market Fund	14.9%

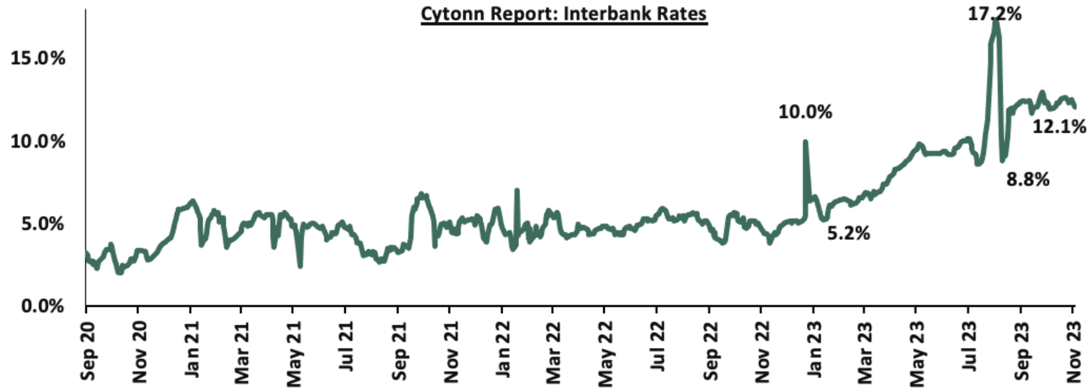
Cytonn Report: Money Market Fund Yield for Fund Managers as published on 3rd November 2023

Rank	Fund Manager	Effective Annual
2	Cytonn Money Market Fund	14.5%
3	Enwealth Money Market Fund	14.4%
4	Etica Money Market Fund	14.0%
5	Apollo Money Market Fund	14.0%
6	Lofty-Corban Money Market Fund	14.0%
7	Madison Money Market Fund	13.8%
8	Jubilee Money Market Fund	13.2%
9	Nabo Africa Money Market Fund	13.2%
10	Sanlam Money Market Fund	13.2%
11	Co-op Money Market Fund	13.1%
12	Kuza Money Market fund	12.8%
13	GenCap Hela Imara Money Market Fund	12.8%
14	AA Kenya Shillings Fund	12.6%
15	Old Mutual Money Market Fund	12.5%
16	Absa Shilling Money Market Fund	12.1%
17	KCB Money Market Fund	12.0%
18	ICEA Lion Money Market Fund	11.5%
19	Equity Money Market Fund	11.5%
20	Dry Associates Money Market Fund	11.5%
21	CIC Money Market Fund	11.2%
22	Orient Kasha Money Market Fund	11.0%
23	Mali Money Market Fund	10.3%
24	British-American Money Market Fund	9.4%

Source: Business Daily

Liquidity:

Liquidity in the money markets marginally eased in the month of October 2023, with the average interbank rate remaining relatively unchanged at 12.3%. During the month of October, the average interbank volumes traded decreased by 22.2% to Kshs 21.0 bn, from Kshs 27.0 bn recorded in September. Also, during the week, liquidity in the money markets eased, with the average interbank rate decreasing to 12.3%, from 12.5% recorded the previous week, partly attributable to government payments that offset tax remittances. The average interbank volumes traded increased by 2.0% to Kshs 14.3 bn, from Kshs 14.1 bn recorded the previous week. The chart below shows the interbank rates in the market over the years:



Kenya Eurobonds:

During the month, the yields on the Eurobonds were on a downward trajectory with the yield on the 10-year Eurobond issued in 2014 declining the most by 3.7% points to 14.6% from 18.3% recorded in end of September 2023. Also, during the week, the yields on Eurobonds were on a downward trajectory with the yield on the 10-year Eurobond issued in 2014 recording the largest decline of 1.1% points to 14.1%, from 15.2%, recorded the previous week. The table below shows the summary of the performance of the Kenyan Eurobonds as of 2nd November 2023;

Cytonn Report: Kenya Eurobonds Performance

	2014	**2018**		**2019**		**2021**
Tenor	**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	**0.6**	**4.3**	**24.3**	**3.6**	**8.6**	**10.6**
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%
29-Sep-23	18.3%	13.3%	12.5%	14.3%	12.7%	12.3%
26-Oct-23	15.2%	13.6%	12.4%	14.1%	12.9%	12.4%
27-Oct-23	14.5%	13.4%	12.3%	13.8%	12.7%	12.2%
30-Oct-23	14.6%	13.3%	12.2%	13.6%	12.7%	12.1%
31-Oct-23	14.6%	13.1%	12.1%	13.6%	12.6%	12.0%
1-Nov-23	14.6%	13.1%	12.0%	13.5%	12.5%	11.8%
2-Nov-23	14.1%	12.8%	11.7%	13.1%	12.1%	11.5%
Weekly Change	**(1.1%)**	**(0.8%)**	**(0.7%)**	**(1.0%)**	**(0.8%)**	**(1.0%)**
MoM Change	**(3.7%)**	**(0.1%)**	**(0.4%)**	**(0.7%)**	**(0.1%)**	**(0.3%)**
YTD Change	**1.2%**	**2.3%**	**0.9%**	**2.2%**	**1.3%**	**1.6%**

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

Kenya Shilling:

During the month, the Kenya Shilling depreciated by 1.7% against the US Dollar, to close the month at Kshs 150.6, from Kshs 148.1 recorded at the end of September 2023, partly attributable to the increased dollar demand from importers, especially oil and energy sectors.

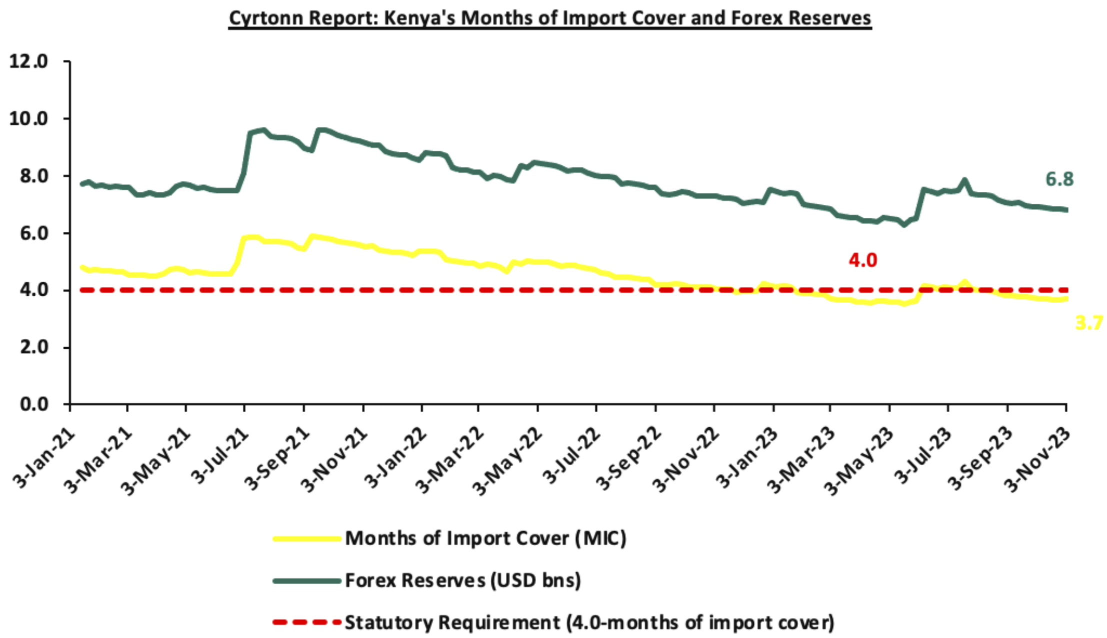
Also, during the week, the Kenya Shilling depreciated by 0.5% against the US dollar to close at Kshs 151.1, from Kshs 150.4 recorded the previous week. On a year to date basis, the shilling has depreciated by 22.4% against the dollar, adding to the 9.0% depreciation recorded in 2022. We expect the shilling to remain under pressure in 2023 as a result of:

i. An ever-present current account deficit, which came at 3.7% of GDP in Q2'2023 from 6.0% recorded in a similar period last year,
ii. The need for government debt servicing, continues to put pressure on forex reserves given that 67.1% of Kenya's external debt is US Dollar denominated as of June 2023, and,
iii. Dwindling forex reserves currently at USD 6.8 bn (equivalent to 3.7-months of import cover), which is below the statutory requirement of maintaining at least 4.0-months of import cover.

The shilling is however expected to be supported by:

i. Diaspora remittances standing at a cumulative USD 3106.7 mn in 2023 as of September 2023, 3.8% higher than the USD 2,992.5 mn recorded over the same period in 2022, which has continued to cushion the shilling against further depreciation. In the September 2023 diaspora remittances figures, North America remained the largest source of remittances to Kenya accounting for 57.0% in the period, and,
ii. The tourism inflow receipts which came in at USD 268.1 bn in 2022, a significant 82.9% increase from USD 146.5 bn inflow receipts recorded in 2021.

The chart below summarizes the evolution of Kenya's months of import cover (MIC) over the years:



Notably, the MIC has been on a downward trajectory, to close October at 3.7 months, from the 3.8 months recorded at end of September. Likewise, Forex Reserves declined to USD 6.8 bn in October, from USD 6.9 bn recorded in September.

Weekly Highlights:

I. **October 2023 Inflation**

The y/y inflation in October 2023 increased marginally by 0.1% points to 6.9%, from the 6.8% recorded in September 2023. This was in line with our projections of an increase to within a range of

6.8% to 7.0%. The headline inflation in October 2023 was majorly driven by increase in prices of commodities in the following categories; transport, food and non-alcoholic beverages and housing, water, electricity, gas and other fuels by 13.6%, 7.8% and 7.8% respectively. The table below shows a summary of both the year on year and month on month commodity indices performance:

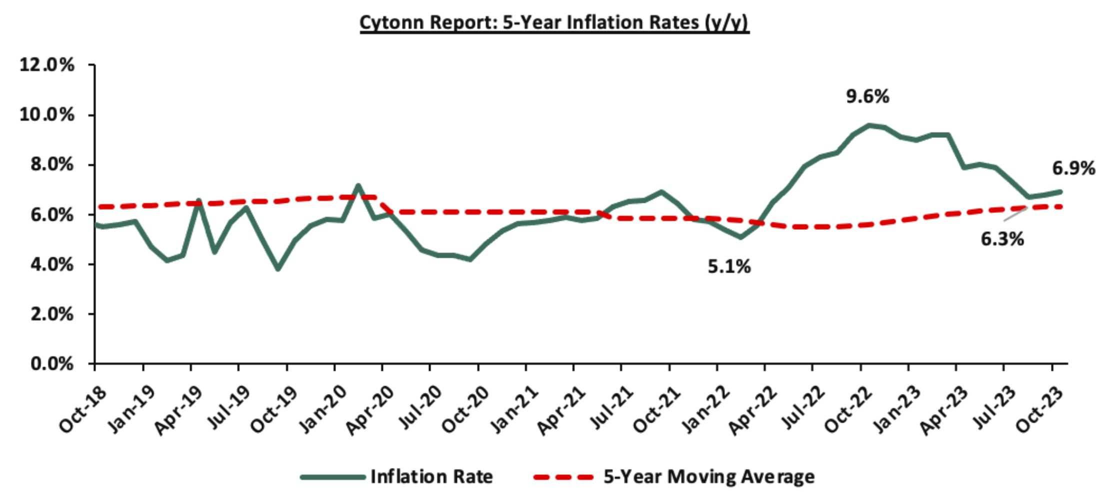
Cytonn Report: Major Inflation Changes – 2023

Broad Commodity Group	Price change m/m (October-2023/September-2023)	Price change y/y (October-2022/October-2023)	Reason
Food and Non-Alcoholic Beverages	1.3%	7.8%	The m/m increase was mainly driven by the increase in prices of commodities such as potatoes, tomatoes and Oranges of 9.6%, 5.4% and 2.8%, respectively. However, the increase was weighed down by decrease in prices of Maize flour-sifted, maize flour-fortified, and wheat flour-white by 4.1%, 3.2%, and 0.8%, respectively.
Housing, Water, Electricity, Gas and Other Fuel	1.9%	7.8%	The m/m performance was mainly driven by the increase in prices of 13.0kg gas/LPG by 7.3%. However, there was a decrease in prices of Electricity of 200KWH and 50KWH by 5.0% and 3.3% respectively.

Cytonn Report: Major Inflation Changes – 2023

Broad Commodity Group	Price change m/m (October-2023/September-2023)	Price change y/y (October-2022/October-2023)	Reason
Transport cost	1.5%	13.6%	The m/m increase in transport Index was mainly due to increase in prices of country bus fares on the back of the rise in the prices of petrol and diesel by 2.7% and 2.2%, respectively.
Overall Inflation	**1.0%**	**6.9%**	**The m/m increase was mainly driven by 1.9% increase in Housing, Water, Electricity, Gas and Other Fuel.**

Notably, the overall headline inflation remained within the Central Bank of Kenya (CBK) target range of 2.5% to 7.5% for the fourth consecutive month. The increase in headline inflation in October 2023 comes amid the recent rise in fuel prices which increased by 2.7%, 2.2% and 1.2% to Kshs 217.4, Kshs 205.5 and Kshs 205.1 per litre of Super Petrol, Diesel and Kerosene, respectively, for the period between 15th October 2023 to 14th November 2023. The chart below shows the inflation rates for the past 5 year;



Source: KNBS

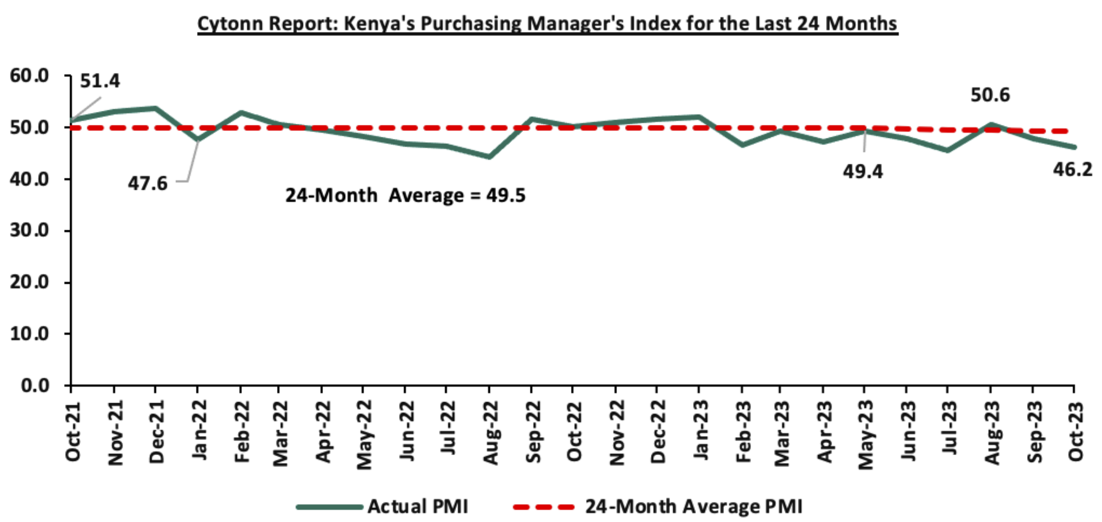
Going forward, we expect inflationary pressures to persist in the short to medium term partly on the back increased government spending following the provisions in proposed supplementary budget which saw the government revise its expenditure upwards by 5.0% to Kshs 3.9 tn, from Kshs 3.7 tn at the beginning of the FY'2023/2024. Key to note, the high commodity prices in the country is also attributed to the sustained depreciation of the Kenya Shilling which has inflated the import bills. As a result, manufacturers pass on the cost to consumers through hike in consumer prices. However, we expect the measures taken by the government to subsidize major inputs of agricultural production such as fertilizers to lower the cost of farm inputs and support the easing of inflation in the long term.

II. **October 2023 Purchasing Managers Index (PMI)**

During the week, Stanbic Bank released its Monthly Purchasing Manager's Index (PMI), highlighting that the index for the month of October 2023 deteriorated further, coming in at 46.2, down from 47.8 in September 2023, signaling a stronger downturn of the business environment for the first month of Q4'2023. On a year to year basis, the index recorded an 8.0% deterioration from the 50.2 recorded in October 2022. The strong downturn of the general business environment is mainly attributable to the elevated inflationary pressure experienced in the country, albeit within the Central Bank of Kenya (CBK) target range of 2.5%–7.5% with the inflation rate in October 2023 slightly tightening to 6.9%, from 6.8% recorded in September 2023. This was on the back of further increase in fuel prices by an average of Kshs 4.3 per litre, as well as the aggressive depreciation of the Kenyan shilling, having depreciated against the dollar by 1.7% in the month of October. As such, input costs rose at the quickest pace in history, resulting from the deterioration of the Shilling against the dollar, which led to price pressures. Consequently, demand worsened as heightened prices resulted to erosion of spending power, leading to a decline in new businesses.

Additionally, the manufacturing output declined at a faster rate compared to September, as firms adjusted to reduced demand by cutting their workforce, resulting to the highest rate of workforce cut since June 2022. Construction, wholesale and retail sectors recorded the highest decline in new business activities.

Notably, exports remained high during the month, attributable to the weak shilling, which made Kenyan exports more affordable in the global market. Key to note, a PMI reading of above 50.0 indicates an improvement in the business conditions, while readings below 50.0 indicate a deterioration. The chart below summarizes the evolution of PMI over the last 24 months:



Going forward, we project that the business environment will continue to be restrained in the short to medium term on the back of the persistent depreciation of the Kenyan Shilling, consequently raising the importation and production costs, thus raising inflation. Additionally, fuel prices remain high and on an upward trajectory as well as food prices, which continue to put inflationary pressures in the private sector. Further, the increased taxation, with likelihood of more upward tax revisions is set to continue restraining the business environment in the country. As a result, the volume of new businesses is expected to remain stifled as consumers cut back on spending owing to a lack of purchasing power. Notably, the general improvement in business conditions is largely dependent on the stability of the Kenya shilling, given that the country's high cost of production is mostly attributable to the high import cost of goods owing to the poor performance of the shilling.

Monthly Highlights:

1. The National Treasury gazetted the revenue and net expenditures for the first quarter of FY’2022/2023, indicating that the total revenue collected as at the end of September 2023 amounted to Kshs 540.0 bn, equivalent to 21.0% of the original estimates of Kshs 2,571.2 bn for FY’2023/2024 and is 84.0% of the prorated estimates of Kshs 642.8 bn. Please see our Cytonn weekly #41/2023,
2. The Energy and Petroleum Regulatory Authority (EPRA) released their monthly statement on the maximum retail fuel prices in Kenya, effective 15th October 2023 to 14th November 2023. Notably, fuel prices for super petrol, Diesel and Kerosene increased by 2.7%, 2.2% and 1.2% to Kshs 217.4, Kshs 205.5 and Kshs 205.1, respectively, from Kshs 211.6, Kshs 200.9 and Kshs 202.6 per litre for super petrol, Diesel and Kerosene respectively. Please see our Cytonn Weekly #41/2023,
3. The Kenya National Bureau of Statistics (KNBS) released the Q2'2023 Quarterly Gross Domestic Product Report, highlighting that the Kenyan economy recorded a 5.4% growth in Q2’2023, marginally faster than the 5.2% growth recorded in Q2’2022. Please see our Cytonn Q3'2023 Markets Review,
4. The monetary policy committee met on October 3, 2023 to review the outcome of its previous policy decisions amidst a backdrop of continued global uncertainties, high inflationary pressures, a weak global growth outlook as well as measures taken by other economies around the world in response to these developments. The MPC retained the CBR Rate at 10.50%, which was in line with our expectations of the MPC to maintain the CBR rate at the current rate. Please see our Cytonn Q3'2023 Markets Review, and,
5. Stanbic Bank released its monthly Purchasing Manager's Index (PMI), highlighting that the index for the month of September 2023 slid back into the negatives, coming in at 47.8, down from 50.6 in August 2023, signaling a stronger downturn of the business environment at the end of Q3’2023. Please see our Cytonn Q3'2023 Markets Review.

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 25.7% behind its prorated net domestic borrowing target of Kshs 91.2 bn, having a net borrowing position of Kshs 67.7 bn of the domestic net borrowing target of Kshs 316.0 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.