Kenya’s FY’2024/2025 Budget Review, & Cytonn Weekly #27/2024

Fixed Income

Money Markets, T-Bills Primary Auction:

During the week, T-bills were oversubscribed for the first time in four weeks, with the overall oversubscription rate coming in at 124.4%, a reversal from the undersubscription rate of 32.0% recorded the previous week. Investors’ preference for the shorter 91-day paper persisted, with the paper receiving bids worth Kshs 14.8 bn against the offered Kshs 4.0 bn, translating to an oversubscription rate of 370.1%, higher than the oversubscription rate of 109.0% recorded the previous week. The subscription rates for the 182-day and 364-day papers increased significantly to 94.2% and 56.3% respectively from the 14.9% and 18.3% respectively recorded the previous week. The government accepted a total of Kshs 27.9 bn worth of bids out of Kshs 29.9 bn bids received, translating to an acceptance rate of 93.4%. 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 3.9 bps, 3.1 bps and 1.0 bps to 16.83%, 16.80% and 15.99% respectively from 16.79%, 16.76% and 15.98% respectively recorded the previous week; The chart below shows the yield growth rate for the 91-day paper over the period:

The chart below compares the overall average T-bill subscription rates obtained in 2018, 2022, 2023, and 2024 Year-to-date (YTD):

Also, during the week, the Central Bank of Kenya released the auction results for the tap sale issue for the FXD1/2023/002 bond with a tenor to maturity of 1.2 years, and a fixed coupon rate of 17.0%. The bond was undersubscribed with the overall subscription rate coming in at 2.4%, receiving bids worth Kshs 0.5 bn against the offered Kshs 20.0 bn. The government accepted bids worth Kshs 0.5 bn, translating to an acceptance rate of 99.8%. The weighted average yield of accepted bids for the FXD1/2023/002 came in at 17.1%, remaining unchanged from the last issue. With the Inflation rate at 4.6% as of June 2024, the real return of the FXD1/2023/002 is 12.5%;

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), and the yields on the government papers were on an upward trajectory, with the yields on the 364-day and 91-day papers increasing by 3.9 bps and 1.0 bps to 16.83% and 15.99% respectively from 16.79% and 15.98% respectively recorded the previous week. The yields on the Cytonn Money Market Fund increased by 75.0 bps to close the week at 18.3% from the 17.6% recorded the previous week, while the average yields on the Top 5 Money Market Funds increased by 16.8 bps to 17.9% from the 17.7% recorded the previous week.

The table below shows the Money Market Fund Yields for Kenyan Fund Managers as published on 5th

July 2024:

Cytonn Report: Money Market Fund Yield for Fund Managers as published on 5th July 2024

Rank	Fund Manager	Effective Annual Rate
1	Cytonn Money Market Fund *(Dial *809# or download the Cytonn App)*	18.3%
2	Lofty-Corban Money Market Fund	18.3%
3	Etica Money Market Fund	18.3%
4	Kuza Money Market fund	17.2%
5	Arvocap Money Market Fund	17.1%
6	GenAfrica Money Market Fund	16.7%
7	Nabo Africa Money Market Fund	16.5%
8	Enwealth Money Market Fund	15.9%
9	GenCap Hela Imara Money Market Fund	15.8%
10	Apollo Money Market Fund	15.7%
11	Jubilee Money Market Fund	15.7%
12	KCB Money Market Fund	15.6%
13	Co-op Money Market Fund	15.4%
14	Mayfair Money Market Fund	15.4%
15	Madison Money Market Fund	15.3%
16	Sanlam Money Market Fund	15.2%
17	Mali Money Market Fund	15.2%
18	Absa Shilling Money Market Fund	15.1%
19	AA Kenya Shillings Fund	15.0%
20	Dry Associates Money Market Fund	14.1%
21	Equity Money Market Fund	14.0%
22	Old Mutual Money Market Fund	13.7%
23	Orient Kasha Money Market Fund	13.6%
24	CIC Money Market Fund	13.5%
25	British-American Money Market Fund	13.5%
26	ICEA Lion Money Market Fund	12.4%

Source: Business Daily

Liquidity:

During the week, liquidity in the money markets marginally tightened, with the average interbank rate increasing by 2.4 bps, to remain relatively unchanged at 13.3% recorded the previous week, partly attributable to tax remittances that offset government payments. The average interbank volumes traded decreased by 2.3% to Kshs 20.0 bn from Kshs 20.4 bn recorded the previous week. The chart below shows the interbank rates in the market over the years:

Kenya Eurobonds:

During the week, the yields on Eurobonds recorded a mixed performance, with the yields on the 7-year Eurobond issued in 2024 increasing the most by 19.1 bps to 10.9% from 10.7% recorded the previous week, while the yields on the 30-year Eurobond issued in 2018 decreasing marginally 1.7 bps to remain relatively unchanged from the 10.9% recorded the previous week. The table below shows the summary of the performance of the Kenyan Eurobonds as of 4th July 2024;

Cytonn Report: Kenya Eurobonds Performance

	2018		2019		2021	2024
Tenor	**10-year issue**	**30-year issue**	**7-year issue**	**12-year issue**	**13-year issue**	**7-year issue**
Amount Issued (USD)	**1.0 bn**	**1.0 bn**	**0.9 bn**	**1.2 bn**	**1.0 bn**	**1.5 bn**
Years to Maturity	**3.7**	**23.7**	**2.9**	**7.9**	**10.0**	**6.7**
Yields at Issue	**7.3%**	**8.3%**	**7.0%**	**7.9%**	**6.2%**	**10.4%**
1-Jan-24	9.8%	10.2%	10.1%	9.9%	9.5%	
1-Jul-24	10.6%	11.1%	10.3%	11.0%	11.0%	11.1%
27-Jun-24	10.3%	10.9%	9.9%	10.8%	10.8%	10.7%
28-Jun-24	10.4%	11.0%	10.1%	10.8%	10.8%	10.8%
1-Jul-24	10.6%	11.1%	10.3%	11.0%	11.0%	11.1%
2-Jul-24	10.5%	11.1%	10.3%	11.0%	11.0%	11.1%
3-Jul-24	10.4%	10.9%	10.0%	10.9%	10.9%	10.9%
4-Jul-24	10.4%	10.9%	10.0%	10.9%	10.9%	10.9%
Weekly Change	**0.0%**	**(0.0%)**	**0.1%**	**0.1%**	**0.1%**	**0.2%**
MTD Change	**(0.2%)**	**(0.2%)**	**(0.3%)**	**(0.2%)**	**(0.1%)**	**(0.1%)**
YTD Change	**0.5%**	**0.7%**	**(0.1%)**	**1.0%**	**1.4%**	**-**

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

Kenya Shilling:

During the week, the Kenya Shilling appreciated against the US Dollar by 0.8%, to close at Kshs 128.5, from Kshs 129.5 recorded the previous week. On a year-to-date basis, the shilling has appreciated by 18.2% against the dollar, a contrast to the 26.8% depreciation recorded in 2023.

We expect the shilling to be supported by:

i. Diaspora remittances standing at a cumulative USD 4,509.8 mn in the 12 months to May 2024, 12.8% higher than the USD 3,997.3 mn recorded over the same period in 2023, which has continued to cushion the shilling against further depreciation. In the May 2024 diaspora remittances figures, North America remained the largest source of remittances to Kenya accounting for 56.0% in the period, and,
ii. The tourism inflow receipts which came in at USD 352.5 bn in 2023, a 31.5% increase from USD 268.1 bn inflow receipts recorded in 2022, and owing to tourist arrivals that improved by 27.2% to 2.1 mn in the 12 months to March 2024, from 1.6 mn recorded during a similar period in 2023.

The shilling is however expected to remain under pressure in 2024 as a result of:

i. An ever-present current account deficit which came at 3.2% of GDP in Q1’2024 from 3.0% recorded in Q1’2023,
ii. The need for government debt servicing, continues to put pressure on forex reserves given that 67.3% of Kenya’s external debt is US Dollar denominated, and,
iii. Dwindling forex reserves, currently at USD 7.8 mn (equivalent to 4.0 months of import cover), which is at par with the statutory requirement of maintaining at least 4.0 months of import cover.

Key to note, Kenya’s forex reserves decreased marginally by 0.3% during the week to remain relatively unchanged from the USD 7.8 bn recorded the previous week, equivalent to 4.0 months of import cover, a decrease from the 4.1 months recorded the previous week, and at par with the statutory requirement of maintaining at least 4.0-months of import cover. The chart below summarizes the evolution of Kenya's months of import cover over the years:

Weekly Highlights

I. **Kenya Q1’2024 GDP Growth Highlight**

During the week, the Kenya National Bureau of Statistics (KNBS) released the Q1’2024 Quarterly Gross Domestic Product Report, highlighting that the Kenyan economy recorded a 5.0% growth in Q1’2024, slower than the 5.5% growth recorded in Q1’2023. The main contributor to Kenyan GDP remains to be the Agriculture, Fishing and Forestry sector which grew by 6.1% in Q1’2024, lower than the 6.4% expansion recorded in Q1’2023. All sectors in Q1’2024, except Mining and Quarrying, recorded positive growths, though the rate of growth was slower than that recorded the same time last year. Accommodation and Food Services, Mining & Quarrying and Construction Sectors growth declined by 19.1%, 3.8%, and 2.9% points, respectively. Other sectors that recorded a slower growth rate, from what was recorded in Q1’2023 were Transport and Storage, Other Services, and Public Administration sectors whose growth slowed by 2.8%, 2.1%, and 1.8% points respectively.

The key take-outs from the report include;

- **Sectoral Contribution to Growth** - The biggest gainer in terms of sectoral contribution to GDP was the Accommodation and Food Services sector, increasing by 0.3% points to 1.5% in Q1’2024 from 1.2% in Q1’2023, while the Manufacturing sector was the biggest loser, declining by 0.3% points to 7.8% in Q1’2024, from 8.1% in Q1’2023. Real Estate was the second largest contributor to GDP at 10.2% in Q1’2024, up from 10.1% recorded in Q1’2023, indicating sustained growth. The Accommodation and Food Services sector recorded the highest growth rate in Q1’2024 growing by 28.0%, slower than the 47.1% growth recorded in Q1’2023. The chart below shows the top contributors to GDP by sector in Q1’2024:

Source: KNBS Q1’2023 and Q1’2024 GDP Report

- **Slowed growth in the Agricultural Sector**– Agriculture and Forestry recorded a growth of 6.1% in Q1’2024. The performance was a decrease of 0.3% points, from the expansion of 6.4% recorded in Q1’2023. The slower growth recorded during the quarter was mainly attributable to decline in exports of coffee, fruit and cut flowers. Coffee exports declined by 13.8% to stand at 9,722.3 metric tonnes in Q1’2024 from the 11,284.9 metric tonnes recorded in Q1’2023.
- **Increased growth in the Financial and Insurance Sector:** The Financial and Insurance sector registered a growth increase of 1.1% points to 7.0% in Q1’2024 compared to the 5.9% in Q1’2023. Similarly, the contribution to GDP increased to 8.9%, from 8.7% in Q1’2023. In line with the prevailing monetary policy stance, the Central Bank Rate was raised to 13.0% in March 2024 from 9.5% in March 2023. The cost of credit rose Q1’2024, with average interest rates on loans and other advances by commercial banks increasing to 16.3% in March 2024 from 13.1% in March

2023.

- **Decelerated growth in the Manufacturing sector** - The manufacturing sector recorded a decelerated growth of 1.3% in Q1'2024 compared to a 1.7% growth in a similar period in 2023. Additionally, the sectoral contribution to GDP decreased to 7.8% in Q1'2024, from 8.1% recorded in Q1'2023.
- **Significant growth in the Accommodation and Food Service sector**: Accommodation and Food Services sector is the only sector that recorded double digit growth in Q1'2024, having expanded by 28.0%, albeit slower than the 47.1% recorded in Q1'2023. Additionally, the contribution to GDP increased by 0.3% points, to 1.5% in Q1'2024, compared to 1.2% recorded in Q1'2023

The chart below shows the different sectoral GDP growth rates for Q1'2024

Source: KNBS Q1'2024 GDP Report

In the near-term, we expect the economy to grow at a slower pace given the restrained business as a result of the difficult economic environment caused by increasing taxes, and an overall rise in the cost of living. Additionally, the Central Bank of Kenya's Monetary Policy Committee's (MPC) decision on 5th June 2024 to maintain the Central Bank Rate (CBR) at 13.0% in a bid to curb inflation and maintain price stability is expected to curtail economic growth. The higher CBR is set to maintain the cost of credit issued by lenders high, hence discouraging borrowing, which will in turn lead to reduced investment spending in the economy by both individuals and businesses. Additionally, the inflation in the country remains within the Central Bank's range of 2.5%-7.5%, and risks going high mainly on the back of a possible increase in fuel prices due to an increase in international fuel prices resulting from geo-political tensions, as well as the proposed road maintenance levy which will push the fuel prices up if approved. Thus, consumer purchasing power remains restrained despite an ease in inflation, resulting in reduced demand for goods and services and consequentially slowed economic growth. However, we expect the agricultural sector to continue backing economic growth in the country, as the country continues to experience sufficient rain during the year. The sector remains Kenya's largest contributor to GDP, as well as food prices being a major contributor to headline inflation. Additionally, we expect we expect the economy to benefit from the strengthening Shilling and the ease in inflationary pressures.

II. Kenya Q1'2024 Balance of Payments

Kenya's balance of payment (BoP) position improved by 126.4% in Q1'2024, with a surplus of Kshs 33.8 bn, from a deficit of Kshs 127.8 bn in Q1'2023, and a significant improvement from the deficit of Kshs 134.8 bn recorded in FY'2023. The y/y positive performance in BoP was mainly driven by a 246.1% improvement in the financial account balance to a surplus of Kshs 121.6 bn in Q1'2024, from a deficit of Kshs 83.2 bn in Q1'2023, and a 22.2% increase in capital account balance to Kshs 8.5 bn from Kshs 6.9 bn recorded in a similar period in 2023. The performance was however weighed down by an 18.8% deterioration in the current account balance to a deficit of Kshs 131.2 bn from a deficit of Kshs 110.5 bn in Q1'2023. The table below shows the breakdown of the various balance of payments components, comparing Q1'2023 and Q1'2024;

Cytonn Report: Kenya's Balance of Payments

Item	Q1'2023	Q1'2024	Y/Y % Change
Current Account Balance	(110.5)	(131.2)	18.8%
Capital Account Balance	6.9	8.5	22.2%
Financial Account Balance	(83.2)	121.6	(246.1%)

Cytonn Report: Kenya’s Balance of Payments

Item	Q1'2023	Q1'2024	Y/Y % Change
Net Errors and Omissions	59.0	34.9	(40.8%)
Balance of Payments	**(127.8)**	**33.8**	**126.4%**

All values in Kshs bns

Key take-outs from the table include;

i. The current account deficit (value of goods and services imported exceeds the value of those exported) widened by 18.8% to Kshs 131.2 bn from the Kshs 110.5 bn deficit in Q1’2023. The y/y widening of the current account was brought about by the 10.3% widening in Merchandise trade deficit to Kshs 341.6 bn in Q1’2024, from Kshs 309.6 bn recorded in Q1’2023. This is attributable to the 28.1% growth in merchandise exports to Kshs 298.1 bn, from Kshs 233.0 bn in Q1’2023 compared to the 19.3% growth in merchandise imports to Kshs 640.0 bn from Kshs 536.6 bn recorded in a similar period in 2023,
ii. The capital account balance (shows capital transfers receivable and payable between residents and non-residents, including the acquisition and disposal of non-produced non-financial items), which includes foreign direct investments (FDIs), increased by 22.2% to a surplus of Kshs 8.5 bn in Q1’2024 up from a surplus of Kshs 6.9 bn in Q1’2023,
iii. The financial account balance (the difference between the foreign assets purchased by domestic buyers and the domestic assets purchased by foreign buyers) recorded a surplus of Kshs 121.6 bn in Q1’2024, An increase of 246.1% from the deficit of Kshs 83.2 bn recorded in Q1’2023. During the review period, reserve assets were depleted by Kshs 90.8 bn, and the government received Kshs 74.0 bn from the International Monetary Fund (IMF), a 35.8% increase from Kshs 54.5 bn in 2023, and,
iv. Consequently, the Balance of Payments (BoP) position improved to a surplus of Kshs 33.8 bn in Q1’2024, from a deficit of Kshs 127.8 bn recorded in Q1’2023.

Current Account Balance

Kenya’s current account deficit widened by 18.8% to Kshs 131.2 bn in Q1’2024 from the Kshs 110.5 bn deficit recorded in Q1’2023. The y/y expansion registered was driven by:

i. The widening of the merchandise trade account deficit (the value of import goods exceeds the value of export goods, resulting in a negative net foreign investment) by 10.3% to Kshs 341.6 bn in Q1’2024, from Kshs 309.6 bn recorded in Q1’2023, and,
ii. A 35.3% deterioration in the services trade balance (transfer) balance to a deficit of Kshs 26.4 bn from a deficit of Kshs 40.7 bn in Q1’2023.

The table below shows the breakdown of the various current account components on a year-on-year basis, comparing Q1’2023 and Q1’2024:

Cytonn Report: Kenya’s Current Account Balance

Item	Q1'2023	Q1'2024	Y/Y % Change
Merchandise Trade Balance	(309.6)	(341.6)	10.3%
Services Trade Balance	40.7	26.4	(35.3%)
Primary Income Balance	(62.0)	(90.8)	46.6%
Secondary Income (transfer) Balance	220.3	274.9	24.7%
Current Account Balance	**(110.5)**	**(131.2)**	**18.8%**

All values in Kshs bns

Kenya's balance of payments improved in Q1'2024, mainly on the back of a 246.1% improvement in the financial account to a surplus of Kshs 121.6 bn in Q1’2024, from a deficit of Kshs 83.2 bn in Q1’2023 reflecting significant inflows of financing into the country. This follows depletion of reserve assets by Kshs 90.8 bn, as the government received Kshs 74.0 bn from the International Monetary Fund (IMF), a 35.8% increase from Kshs 54.5 bn in 2022. The current account deficit (value of goods and services imported exceeds the value of those exported) widened by 18.8% to Kshs 131.2 bn from the Kshs 110.5 bn deficit in Q1’2023. The y/y widening of the current account was brought about by the 10.3% widening in Merchandise trade deficit to Kshs 341.6 bn in Q1’2024, from Kshs 309.6 bn in Q1’2023 driven by the 28.1% growth in merchandise exports to Kshs 298.4 bn, from Kshs 233.0 bn in Q1’2023 which outpaced the 19.3% increase in merchandise imports to Kshs 640.0 bn from Kshs 536.6 bn recorded in a similar period in 2023. Additionally, the secondary income balance saw a substantial increase, bolstered by strong growth in diaspora remittances. Looking ahead, the outlook for Kenya's current account is optimistic, as continued growth in key export sectors and sustained diaspora remittances are expected to further improve the current account balance. Efforts to diversify exports and enhance value addition in agricultural products, along with prudent fiscal and monetary policies, will be crucial in sustaining this positive trajectory. Furthermore, the ongoing strengthening of Kenyan Shilling against most trading currencies is expected to lower the import bill hence narrowing the current account deficit. We expect that the current administration’s renewed focus on fiscal consolidation will improve the balance of payments performance by minimizing the costs of servicing external debts. Additionally, the favorable weather conditions and government intervention through subsidy programs are set to boost agricultural production in the country, thereby increasing the export of agricultural products, and supporting the current account. We anticipate that the balance of payments will continue being stable with the help of multiple trade agreements, such as the one between Kenya and the EU and the one among the EAC, SADC and COMESA, as the agreements will boost the amount and variety of exports that are needed and offer more opportunities to sell them.

III. **Stanbic Bank’s June 2024 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 May 2024 sharply deteriorated, coming in at 47.2, above the 50.0 neutral, down from 51.8 in May 2024, signaling a deterioration in the operating conditions across Kenya. This was the sharpest decline recorded in seven months. Private sector output dropped markedly in the month of June, reflecting a renewed and steep fall in new business intakes. On a year-to-year basis, the index recorded a 5.2% decline from the 49.8 recorded in January 2024. This sharp decline in the general business environment is mainly attributable to the cost of living crisis, as well as protests surrounding the country’s finance bill which hurt sales volumes. This downturn was partially softened by a rise in new orders across manufacturing, which was the only monitored sector to register growth in June. In addition to the easing inflation, which came in at 4.6%, from 5.1% in June 2024, well below the CBK’s preferred target of 5.0%, and remaining within the Central Bank of Kenya (CBK) target range of 2.5% to 7.5% for the twelfth consecutive month, and a decrease of 0.4% points from 5.1% in May. Notably, the prices for Super Petrol, Diesel and Kerosene decreased by Kshs 3.0, Kshs 6.1 and Kshs 5.7 each respectively, and will retail at Kshs 192.8, Kshs 179.2 and Kshs 168.7 per litre respectively from the May 2024 prices of Kshs 189.8, Kshs 173.1 and Kshs 163.1 respectively.

The average input charges rose for the first time in three months in June, attributable to higher taxation on products was commonly noted by respondents as driving up costs. Meanwhile, output prices recorded a mild increase in anticipation of the increased taxes proposed in the Finance Bill 2024. The sector data showed an increase in output, for the first time since February, with expansions recorded in the services, manufacturing and wholesale & retail segments. Agriculture, services, wholesale and retail sectors were the ones that recorded increases during the month, as manufacturing and construction sectors registered declines. Similarly, the employment levels improved for the sixth consecutive month in June, though mildly, with a rise in staff costs, increased inventories and prospects of new business driven by an uptick in customer demand.

Supplier performance also improved in June , attributable to greater availability of raw materials and competition between various vendors. Notably, overall sentiment towards future activity of the Kenyan business environment slipped for the first time in a while, recording a four-month low. The firms cited economic challenges as the reason for the reduced optimism. 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 expect the business climate to be restrained in the short to medium term as a result of the difficult economic environment and the recent unrest following the anti-finance bill protests in addition to the high interest rates from tightening monetary policy and an overall rise in the cost of living. However, we expect firms to benefit from reduced inflationary pressures and an appreciating Shilling, which will lower input prices.

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 154.4% ahead of its prorated net domestic borrowing target of Kshs 5.1 bn, and 95.1% behind the total domestic net borrowing target of Kshs 263.2 bn for FY'2024/2025, having a net borrowing position of Kshs 12.9 bn. However, we expect a downward readjustment of the yield curve in the short and medium term, with the government looking to increase its external borrowing to maintain the fiscal surplus, hence alleviating pressure in the domestic market. As such, we expect the yield curve to normalize in the medium to long-term and hence investors are expected to shift towards the long-term papers to lock in the high returns.