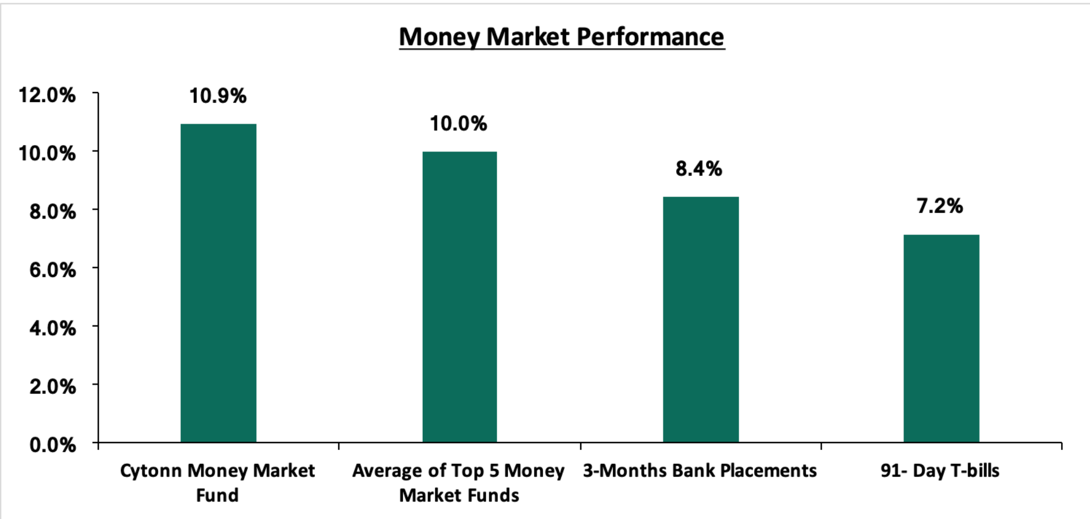
Real Estate Investment Trusts, REITS, as an Investment Alternative, & Cytonn Weekly #52

Fixed Income

Money Markets, T-Bills & T-Bonds Primary Auction:

During the week, T-bills remained undersubscribed, with the subscription rate coming in at 17.0%, the lowest recorded in the last two years, down from 64.1% the previous week. This is down from an average of 125.4% from January 2019 to November 7th 2019 before the repeal of the rate cap; and 98.2% points lower than the YTD average of 115.2%. The undersubscription is partly attributable to declined investor activity associated with the festive season, coupled with the reduced participation by banks since the repeal of the interest rate cap, with their focus now shifting to private sector lending. The yield on the 91-day and 364-day paper remained unchanged at 7.2% and 9.8%, respectively. The yield on the 182-day paper increased to 8.2% from the 8.1% recorded the previous week. The acceptance rate increased to 100.0%, from 99.4% recorded the previous week, with the government accepting Kshs 4.1 bn of the Kshs 4.1 bn worth of bids received.



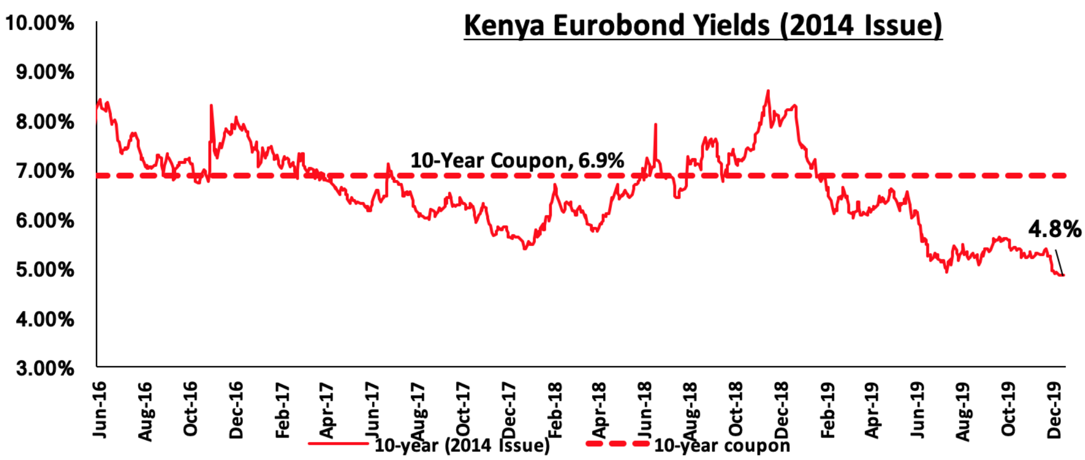
In the money markets, 3-month bank placements ended the week at 8.4% (based on what we have been offered by various banks), the 91-day T-bill came in at 7.2%, while the average of Top 5 Money Market Funds came in at 10.0%, unchanged from the previous week. The yield on the Cytonn Money Market remained unchanged at 10.9% recorded the previous week.

Liquidity:

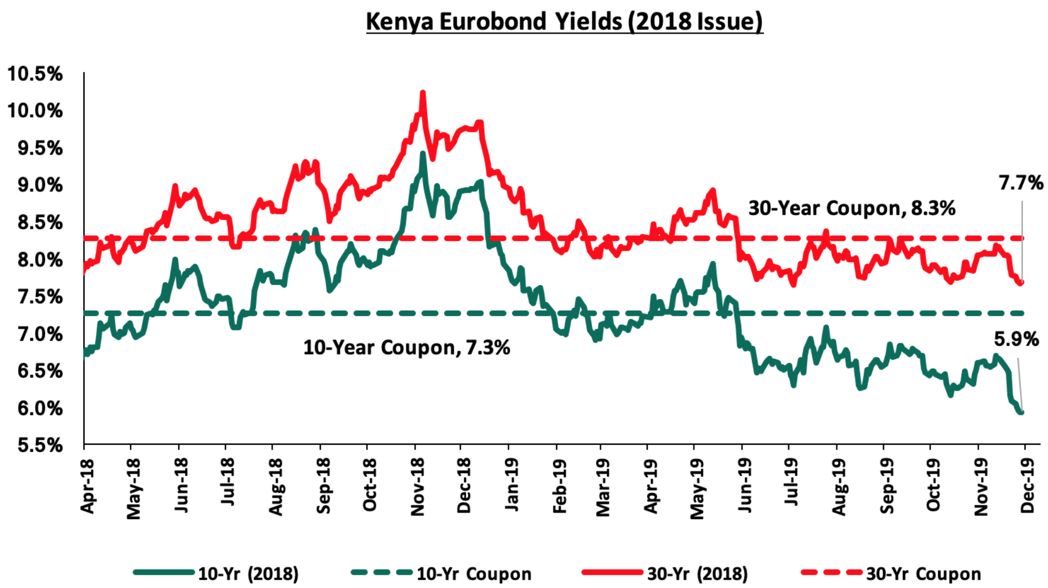
During the week, the average interbank rate increased marginally to 5.6%, from 5.5% recorded the previous week, pointing to tightening of liquidity in the money markets. Commercial banks' excess reserves came in at Kshs 17.2 bn in relation to the 5.25% cash reserves requirement (CRR). The average interbank volumes increased by 14.8% to Kshs 21.3 bn, from Kshs 18.5 bn recorded the previous week.

Kenya Eurobonds:

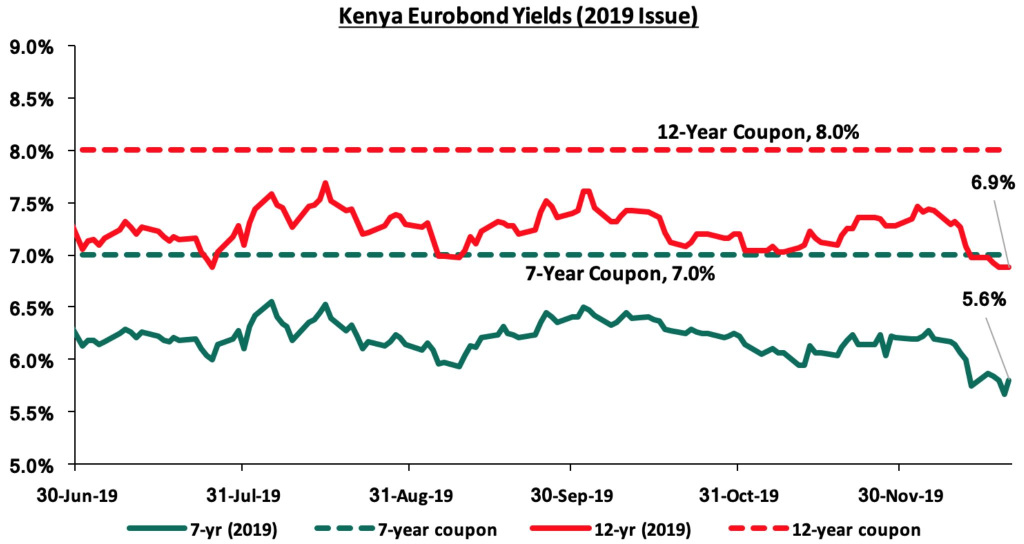
According to Reuters, the yield on the 10-year Eurobond issued in June 2014 declined by 0.1% points to 4.8%, from 4.9% recorded the previous week, an indication that investors are attaching lower risk premium on the country, attributed to the release of the country's credit rating by Fitch Ratings, which was "B+", highlighting the country's stable outlook.



During the week, the yields on the 10-year Eurobond and the 30-year Eurobond both remained unchanged at 5.9% and 7.7%, respectively.



During the week, the yield on the 7-year Eurobond decreased by 0.2% points to 5.6%, from 5.8% recorded the previous week, while the yield on the 12-year Eurobond remained unchanged at 6.9%.



Kenya Shilling:

During the week, the Kenya Shilling appreciated by 0.1% against the US Dollar to close at Kshs 100.8, from 100.7 recorded the previous week, mostly supported by inflows from tourism and diaspora remittances amid slow demand from importers. On a YTD basis, the shilling has appreciated by 1.1% against the dollar, in comparison to the 1.3% appreciation in 2018. In our view, the shilling should remain relatively stable against the dollar in the short term, supported by:

i. The narrowing of the current account deficit, with preliminary data indicating that Kenya's current account deficit in Q2'2018 was equivalent to 6.2% of GDP, from 7.6% recorded in Q2'2018. This was mainly driven by the narrowing of the country's merchandise trade deficit balance (a scenario where imports are greater than exports) by 1.7% and a rise in secondary income transfers (transfers recorded in the balance of payments whenever an economy provides or receives goods, services, income or financial items) by 5.1%,
ii. Improving diaspora remittances, which have increased cumulatively by 5.0% in the 12-months to November 2019 to USD 2.8 bn, from USD 2.7 bn recorded in a similar period of review in 2018,
iii. Foreign capital inflows, with investors looking to participate in the equities market,
iv. CBK's supportive activities in the money market, such as repurchase agreements and selling of dollars, and,
v. High levels of forex reserves, currently at USD 8.8 bn (equivalent to 5.4-months of import cover), above the statutory requirement of maintaining at least 4.0-months of import cover, and the EAC region's convergence criteria of 4.5-months of import cover.

Rates in the fixed income market have remained relatively stable as the government rejects expensive bids. The government is 5.6% ahead of its domestic borrowing target, having borrowed Kshs 164.6 bn against a pro-rated target of Kshs 155.9 bn. We expect an improvement in private sector credit growth considering the repeal of the interest rate cap. This will result in increased competition for bank funds from both the private and public sectors, resulting in upward pressure on interest rates. Owing to this, our view is that investors should be biased towards short-term fixed-income securities to reduce duration risk.