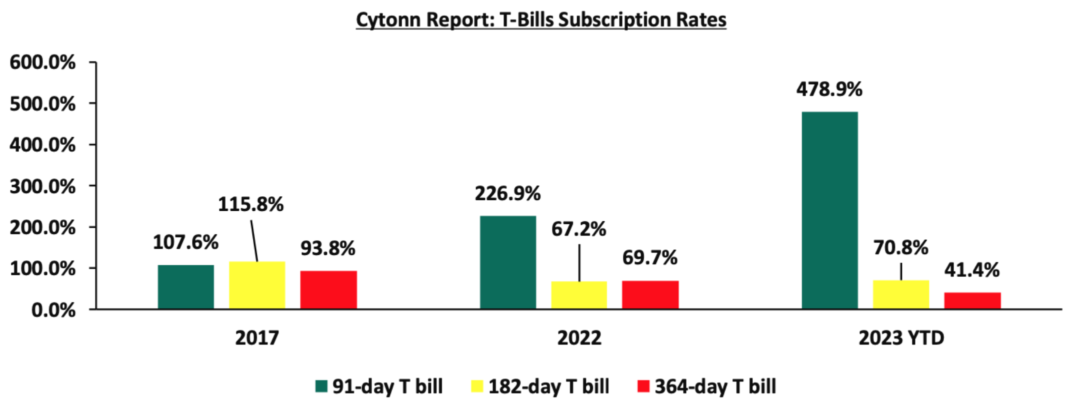
Off-Plan Real Estate, & Cytonn Weekly #21/2023

Fixed Income

Money Markets, T-Bills Primary Auction:

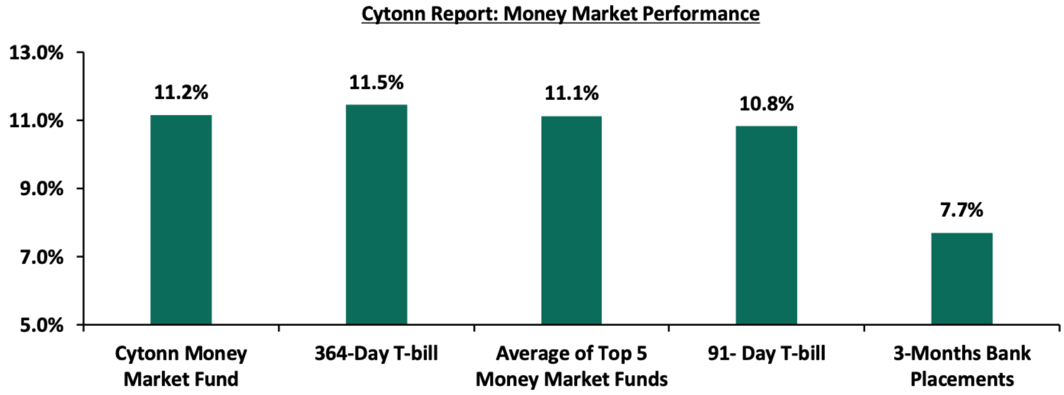
During the week, T-bills were undersubscribed for first time in four weeks, with the overall subscription rate coming in at 91.9%, down from an oversubscription rate of 150.1% recorded the previous week. Investor's preference for the shorter 91-day paper persisted as they sought to avoid duration risk, with the paper receiving bids worth Kshs 14.2 bn against the offered Kshs 4.0 bn, translating to an oversubscription rate of 356.1%, lower than the 602.3% recorded the previous week. The subscription rates for the 182-day and 364-day paper declined to 40.4% and 37.6%, from the 42.2% and 77.1% recorded the previous week, respectively. The government accepted bids worth Kshs 21.0 bn out of the Kshs 22.0 bn total bids received, translating to an acceptance rate of 95.4%. 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 6.7 bps, 13.5 bps and 31.4 bps to 11.5%, 11.1% and 10.8%, 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 bond market, the Central Bank of Kenya released the tap sale results for the Treasury bond FXD1/2023/003 with tenor to maturity of 3 years. In line with our expectations, the bond recorded an oversubscription rate of 136.0%, partly attributable to investors' preference for shorter dated bonds as they seek to avoid duration risk. The government issued the bond seeking to raise Kshs 20.0 bn for budgetary support. The tap sale of the bond received bids worth Kshs 27.2 bn, with government accepting bids worth Kshs 27.2 bn, translating to an acceptance rate of 100.0%. Key to note, both the weighted average yield of accepted bids and the coupon rate came at 14.2%.

Money Market Performance:

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 yields on the 364-day and 91-day paper increased by 6.7 bps and 31.4 bps to 11.5% and 10.8% respectively. The yield of Cytonn Money Market Fund increased by 2.0 bps to 11.2%, up from 11.1% recorded in the previous week, while the average yields of Top 5 Money Market Funds increased by 18.0 bps to 11.1%, up from 11.0% recorded the previous week.



The table below shows the Money Market Fund Yields for Kenyan Fund Managers as published on 26 May 2023:

Cytonn Report: Money Market Fund Yield for Fund Managers as published on 26 May 2023

Rank	Fund Manager	Effective Annual Rate
1	Etica Money Market Fund	11.6%
2	Cytonn Money Market Fund (dial *809# or download the Cytonn app)	11.2%
3	Madison Money Market Fund	11.0%
4	Dry Associates Money Market Fund	11.0%
5	Enwealth Money Market Fund	10.9%
6	GenAfrica Money Market Fund	10.9%
7	Apollo Money Market Fund	10.8%
8	Jubilee Money Market Fund	10.8%
9	AA Kenya Shillings Fund	10.5%
10	Old Mutual Money Market Fund	10.3%
11	Co-op Money Market Fund	10.1%
12	NCBA Money Market Fund	10.1%
13	Sanlam Money Market Fund	10.1%
14	Kuza Money Market fund	10.1%
15	Nabo Africa Money Market Fund	10.0%
16	Zimele Money Market Fund	9.9%
17	GenCap Hela Imara Money Market Fund	9.7%
18	British-American Money Market Fund	9.6%
19	CIC Money Market Fund	9.6%
20	ICEA Lion Money Market Fund	9.6%
21	Orient Kasha Money Market Fund	9.4%

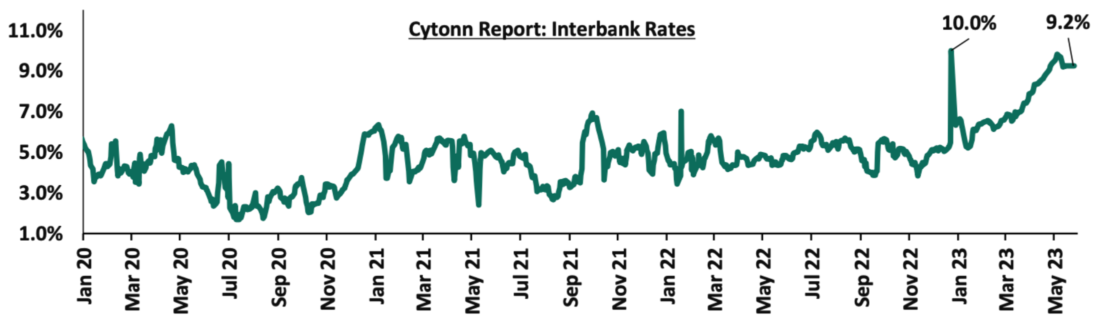
Cytonn Report: Money Market Fund Yield for Fund Managers as published on 26 May 2023

Rank	Fund Manager	Effective Annual Rate
22	KCB Money Market Fund	9.2%
23	Absa Shilling Money Market Fund	8.9%
24	Mali Money Market Fund	8.3%
25	Equity Money Market Fund	7.5%

Source: Business Daily

Liquidity:

During the week, liquidity in the money markets remained tightened, with the average interbank rate remaining relatively unchanged at 9.2% similar to what was recorded the previous week, partly attributable to tax remittances that offset government payments. The average interbank volumes traded increased by 13.7% to Kshs 25.7 bn, from Kshs 22.6 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 on the 10-year Eurobond issued in 2014 gaining by 0.3% points to 15.7%, from 15.4%, recorded the previous week, while the yield on the 7-year Eurobond issued in 2019 declining the most by 1.0% points to 13.3%, from 14.3% recorded the previous week. The table below shows the summary of the performance of the Kenyan Eurobonds as of 18 May 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	**1.1**	**4.8**	**24.8**	**4.0**	**9.0**	**11.1**
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%

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	**1.1**	**4.8**	**24.8**	**4.0**	**9.0**	**11.1**
Yields at Issue	**6.6%**	**7.3%**	**8.3%**	**7.0%**	**7.9%**	**6.2%**
1-May-23	20.6%	14.1%	12.7%	15.5%	13.2%	12.4%
18-May-23	15.4%	12.6%	12.0%	14.3%	12.4%	11.7%
19-May-23	14.7%	12.3%	11.8%	13.5%	12.2%	11.4%
22-May-23	15.3%	12.3%	11.8%	13.5%	12.2%	11.3%
23-May-23	15.0%	12.1%	11.6%	13.2%	12.0%	11.2%
24-May-23	15.5%	12.1%	11.7%	13.4%	12.1%	11.2%
25-May-23	15.7%	12.1%	11.6%	13.3%	12.1%	11.2%
Weekly Change	**0.3%**	**(0.5%)**	**(0.4%)**	**(1.0%)**	**(0.3%)**	**(0.5%)**
MTD change	**(4.9%)**	**(2.0%)**	**(1.1%)**	**(2.2%)**	**(1.1%)**	**(1.2%)**
YTD Change	**2.8%**	**1.7%**	**0.7%**	**2.4%**	**1.3%**	**1.3%**

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

Kenya Shilling:

During the week, the Kenya Shilling depreciated by 0.6% against the US dollar to close the week at Kshs 138.3, from Kshs 137.5 recorded the previous week, partly attributable to the persistent dollar demand from importers, especially oil and energy sectors against a slower supply of hard currency. On a year to date basis, the shilling has depreciated by 12.0% 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,
ii. An ever-present current account deficit estimated at 4.9% of GDP in twelve months to January 2023, from 5.6% recorded in a similar period last year,
iii. The need for Government debt servicing which continues to put pressure on forex reserves given that 63.0% of Kenya's External debt was US Dollar denominated as of December 2022, and,

The shilling is however expected to be supported by:

i. Diaspora remittances standing at a cumulative USD 1,335.9 mn in 2023 as of April 2023, albeit 3.1% lower than the USD 1,378.9 mn recorded over the same period in 2022, and,
ii. The tourism inflow receipts that came in at USD 268.1 bn in 2022, a significant 82.9% increase from USD 146.5 bn inflow receipts recorded in 2021.

Key to note, Kenya's forex reserves increased by 2.9% to USD 6.5 bn as of 25 May 2023, from USD

6.3 bn as of 18 May 2023. As such, it represented a 3.6 months of import cover, a notable increase from the 3.5 months of import cover recorded the previous week. However, the forex reserves remained below the statutory requirement of maintaining at least 4.0-months of import cover. Key to note, should the government receive the USD 410.0 mn from International Monetary Fund (IMF), upon completion of the fifth reviews of Kenya's economic programme under the Extended Fund Facility (EFF) and Extended Credit Facility (ECF) arrangements, the forex reserve months of import cover is expected to increase to 3.8 months from the current 3.6 months. The chart below summarizes the evolution of Kenya months of import cover over the last 10 years:

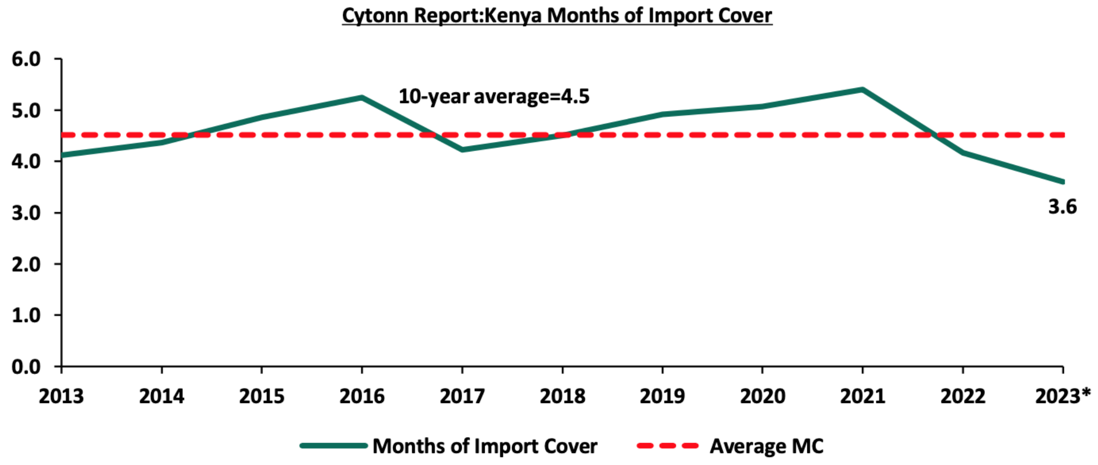


Figure as at 25 May 2023

Weekly Highlights:

I. **Kenya's International Monetary Fund (IMF) Loan facility**

During the week, the International Monetary Fund (IMF) announced that it had reached a staff level agreement with Kenyan authorities on the following;

i. To conclude the fifth reviews of Kenya's economic program under the Extended Fund Facility (EFF) and Extended Credit Facility (ECF) arrangements,
ii. An argumentation of access under the EFF/ECF totaling 75.0% of quota of USD 544.3 mn (Kshs 75.3 bn) given challenging global financing conditions,
iii. Extension of the duration of the EFF/ECF arrangements by 10 months to April 2025 to allow sufficient time for meeting the programme objectives, and,
iv. A new 20-month Resilience and Sustainability Facility (RSF) arrangement with access also of 75.0% of the quota that will run in parallel with the EFF/ECF arrangements until April 2025.

Upon the expected completion of the fifth reviews by July 2023, Kenya will have immediate access of USD 410.0 mn (Kshs 56.7 bn) of the approved loan facility totaling to USD 2.3 bn that was announced in April 2021 including from augmentation of access under the ECF/EFF. This will bring total IMF financial support disbursed under the EFF/ECF to USD 2,051.2 mn (Kshs 283.7 bn). Additionally, with the EFF/ECF augmentations and the RSF support, the total IMF commitment under these arrangements would be USD 3.5 bn (Kshs 486.7 bn)

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 138.3)
Apr-21	307.5	42.5
Jun-21	407.0	56.3

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

Date	Amount Received (USD mn)	Amount Received (Kshs bn, 1 USD = Kshs 138.3)
Dec-21	258.1	35.7
Jul-22	235.6	32.6
Nov-22	433.0	59.9
Jul-23	*410.0	56.7
Total Amount Received	**2,051.2**	**283.7**
Amount Pending	**1,470.0**	**204.2**

**Expected funds upon IMF management and executive board approval*

The government budget has been under pressure on the back of low revenue collection as well as tight financing conditions, evidenced by the total revenue collected as at the end of April 2023 amounting to Kshs 1,639.8 bn, equivalent to 78.4% of the revised estimates of Kshs 2,192.0 bn for FY'2022/2023 and was 89.8% of the prorated estimates of Kshs 1,826.7 bn. As such, the funding is expected to support the economy amid backdrop of the country's economic growth as evidenced by the GDP of 4.8% in 2022, which was lower than the 7.6% growth recorded in 2021. Additionally, upon disbursement, the financing is expected to boost the country's dwindling foreign exchange reserves which currently stand at USD 6.5 mn representing 3.6 months of import cover, below the minimum statutory requirement of 4.0 months of import cover. The Resilience and Sustainability Facility (RSF) is also expected to aid in addressing challenges posed by climate change, while also strengthening the macroeconomic stability.

Notably, the IMF commended the government move to bring back liquidity to the interbank market for foreign exchange which is expected to support exchange rate flexibility and backstop the external position. Going forward, the IMF noted the need for the government to fast track reforms in State Owned Enterprises (SOEs) which continues to drain on budget resources, among the SOEs include, Kenya Airways and Kenya Power and Lighting Company.

II. **May 2023 Inflation Projection**

We are projecting the y/y inflation rate for May 2023 to come in at a range of 7.9%-8.3%, despite inflation easing to 7.9% in April 2023 from 9.2% in March 2023. Our projection is mainly on the back of:

i. **Increased Fuel Prices -Fuel prices increased by 1.9%, 4.0% and 10.4% to Kshs 182.7, Kshs 168.4 and Kshs 161.1 per litre of Super Petrol, Diesel and Kerosene, respectively, for the period between 15th May 2023 to 14th June 2023. The increase was attributed to the government's decision to completely fuel subsidy which was cushioning the citizens from high fuel prices. As such, given that fuel is major input to most sectors, we expect the cost of production to increase and consequently lead to high consumer prices, and,**

ii. **Elevated food prices - Food prices have remained elevated mainly on the back of uneven weather patterns as well as supply chain bottleneck experienced globally. The elevated prices were evidenced by the 10.1% y/y increase in the prices of food and non-alcoholic beverages in April 2023. Given that the food is a major input in inflation index, we expect the resulting high prices to underpin inflationary pressures.**

Notably, the high commodity prices in the country are also attributed to the sustained depreciation of the Kenya Shilling which has inflated import bill. As a result, manufactures pass on the cost to consumers through hike in commodity prices. Going forward, we expect inflationary pressures to persist in the short term, however to ease in the medium term to CBK's target range of 2.5% to 7.5% aided by easing in global commodity prices and easing of domestic food prices on account of favorable weather conditions. We also 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

III. **May 2023 MPC Meeting**

The Monetary Policy Committee (MPC) is set to meet on Monday, 29 th May 2023, to review the outcome of its previous policy decisions and recent economic developments, and to decide on the direction of the Central Bank Rate (CBR). We expect the MPC to maintain the CBR at 9.50% with their decision mainly being supported by;

i. The ease on y/y inflation in April 2023 to 7.9%, from 9.2% recorded in March 2023, despite remaining above the CBK's target range of 2.5%-7.5%. Additionally, food inflationary pressures are expected to slow in the near term, aided by continued rains as well as importation of duty-free staples such as maize, rice, cooking oil and sugar. However, elevated inflation is expected to endure in the short to medium following the increase in fuel prices after the government completely removed the fuel subsidies which was aimed at cushioning consumers from high fuel prices. As such, we expect the MPC to maintain the CBR as the current monetary stance still transmits in the economy,
ii. The continued deprecation of the shilling does not provide room for any easing, hence MPC has to maintain the elevated rates to protect the shilling, and,
iii. The need to support the economy by adopting an accommodative policy that will ease financing activities. Additional hike in the CBR rate might slow down economic activities given the current macro and business environment fundamentals cannot accommodate further hikes.

Notably, despite the macroeconomic indicators being inclined towards an increase in the Central Bank Rate with focus on easing inflation to the CBK target range while supporting the Kenyan shilling, the committee must be cautious as the country's economic growth has been declining. This is evidenced by Kenya's economy recording a 4.8% growth in 2022 compared to the 7.6% expansion in 2022. Therefore, we expect the MPC to maintain the CBR at 9.50% as they monitor the impact of the policy measures, as well as developments in the global and domestic economy.

For a more detailed analysis, please see our May 2023 MPC note.

Rates in the Fixed Income market have been on upward trend given the continued government's demand for cash as well as tight liquidity in the money market. The government is on target with its prorated borrowing target of Kshs 387.7 bn having borrowed Kshs 387.8 bn of the revised domestic borrowing target of Kshs 425.1 bn 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 April 2023 coming in at Kshs 1.6 tn in the FY'2022/2023, equivalent to 74.8% of its revised target of Kshs 2.2 tn and 89.8% of the prorated target of Kshs 1.8 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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