Indicators to Remain Divergent From Sentiment

H2'2023
Markets Outlook

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Indicators to Remain Divergent From Sentiment

H1'23 has seen the negative spillover effects from 2022 continue to hamper economic recovery with the further weakening of macro factors consequently leading higher domestic interest rates, heightened geopolitical tensions and slower global economic growth. Globally, inflation in advanced economies continued to ease during the year driven by reduced prices for basket of commodities components, easing of supply chain costs, and a decrease in commodity prices especially crude oil prices. However, core inflation has remained sticky on the higher side showing increased pressure on non-fuel non-food items. Consensus expectations have cut back on recessionary fears with expectations shifting to minor contractions in the coming quarters.

- **Macros to Remain Challenged:** Further weakening of the shilling was as a result of continued strengthening of the dollar, decreased dollar inflows and increasing import costs exacerbating the challenging business environment. We expect inflation to remain above the CBK'S target range of 2.50% - 7.50% in the short term due to increased pressure from higher local fuel prices and continued underlying inflationary pressures increasing core inflation. We expect continued easing in food inflation resulting from onset of long rains increasing food production. Globally, central banks have continued to tighten their monetary policies with the aim of combatting elevated inflation and restore inflation to within their targets. Going forward, we anticipate that economic growth will remain muted resulting from ongoing inflationary pressures, global uncertainties and an increasing risk of debt distress.
- **Fixed Income Market:** We expect investors to continue bidding aggressively in the primary market as macro factors remain challenged pushing them to demand for a premium and protect their real rate of return. The almost predictable tap sale issuance will be a huge downside to activity in the secondary market. We foresee the primary bond issuance market remaining vibrant which should be transmitted to the secondary market as investors who miss out in the initial issuance will drive demand for papers in the secondary market. We foresee the issuance of at least one more Infrastructure bond (IFB) before the end of the year. We expect investors to be dazed by the choice between higher future yields expectations in fixed income and the low current valuations in the equities market. The Eurobond redemption headache will continue paining the government due to tight fiscal space coupled with the depreciating local currency which complicates the available options.
- **Equities Market:** Activity in H1'23 slowed down compared to H1'22 with listed banks releasing mixed Q1'2023 results and listed telco Safaricom posting decline in net earnings. The higher risk-free rate and a 517bps upward movement on a YTD basis in Kenya's Equity Risk Premium is driving down valuations in the stock market. Notably, the NSE market PE has declined 19.40% to 5.4x in H1'23 from 6.7x as at the end of 2022. The NSE market PEG (PE Growth) at 0.7x has remained below 1.0x pointing to undervaluation. We foresee slowdown in capital flight and a potential turnaround. Counters whose value declined as a result of the capital flight provide an attractive entry point for foreign investors.

19th July 2023

Sovereign Credit Rating:

Moody's: B3 (Negative)

Fitch: B (Stable)

S&P: B (Negative)

GDP Est. (2023):	5.50%
Inflation (June):	7.90%
Interbank Rate (Ave):	9.24%
CBR (June 2023):	10.50%

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Global Outlook

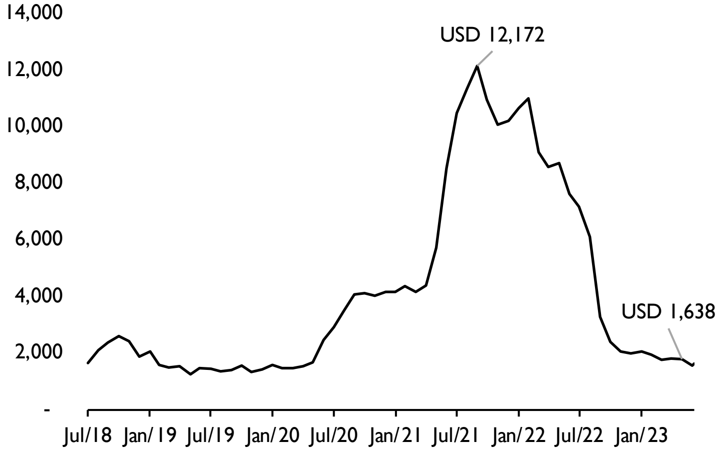
We continue to see global economy facing three major threats in H2'2023;

a) **Core Inflation to Remain as a Headache to Policy Makers :** We expect inflationary pressure to continue easing as central banks begin their cutting cycle towards the end of the year. Lower inflationary pressure will be driven by lower prices for some commodities, declining oil prices and improved logistics which has reduced freight costs. However, core inflation is likely to remain sticky leaving policy makers looking at a tradeoff between economic growth and inflationary control. We foresee monetary tightening continuing at least until Q4'23 where benchmark rate cutting cycles are likely to begin. We suspect that despite easing inflation, most central banks are still not comfortable with the lower inflation levels and are thus trying to factor any surprise inflationary shocks.

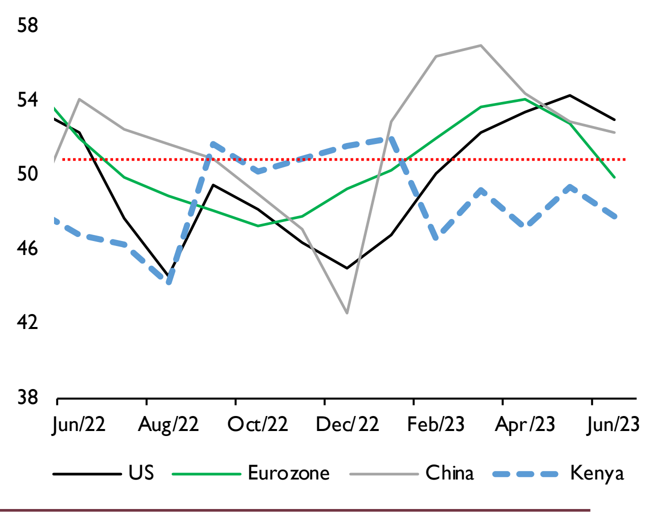
b) **Geo-Political Stability to Influence Economic Policies**: We expect that the BRICS led activities around moving trade away from the petrodollar is also likely to continue putting many countries on a collision path with the US. Even though we believe that the push to do away with the US Dollar as the benchmark/reserve currency for international trade is far fetched, the push by BRICS members will stir enough muck globally.

c) **Recessionary Fears to Cool Off:** We believe that the global markets have already priced in the earlier recessionary fears. While the fears have dwindled, they have not gone away. Global average composite PMI has remained above 50 for the better part of 2023 but we observed a bifurcation between manufacturing PMI and service PMI. With high factory input costs, reduced new orders and lower factory output manufacturing PMI has remained constrained. We expect slow growth in US, Europe, China and other emerging markets. Exports are likely to suffer and with the strengthening of the dollar this will be difficult for economies that rely heavily on exports.

Graph 1: USD Cost of Transporting a 40Ft Container Has Been Declining



Graph 2: Global Composite PMI has Remained Above 50 in H1'23



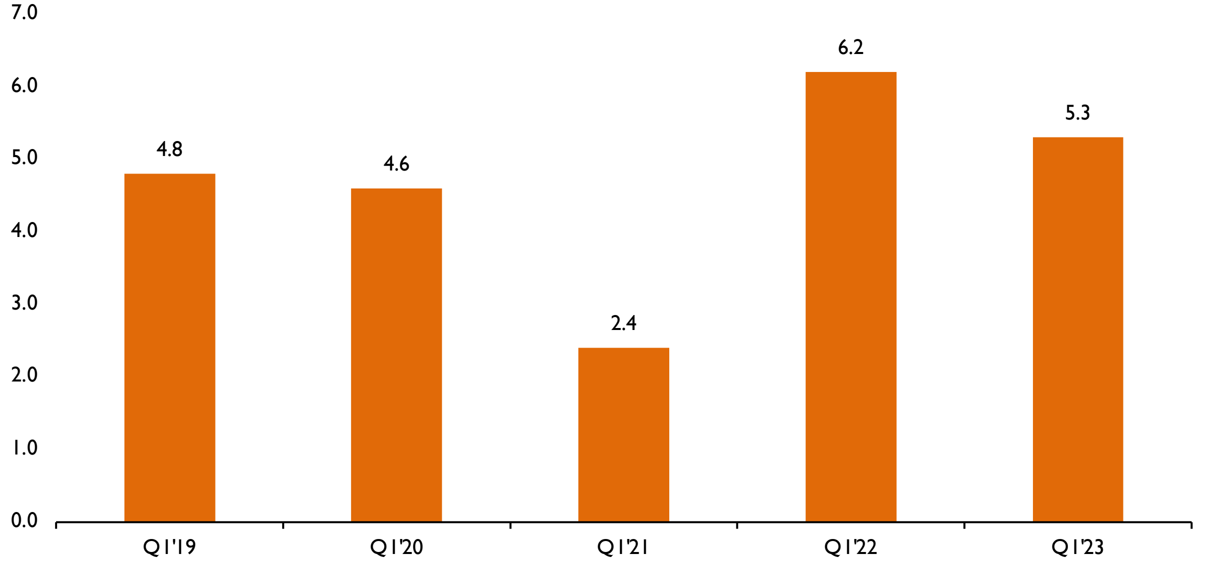
Local Economic Performance

- **Local Economic Activity:** In Q1'23 the economy expanded by 5.30% slower compared to 6.20% in Q1'22. Growth during the quarter was driven by recovery of the agricultural sector and the tourism sector and hampered by decline in manufacturing and construction sectors. Similarly, growth in Q2'23 is expected to be slower than the similar quarter in the preceding year. Local economic growth has been subdued by hiked interest rates, heightened inflationary pressures, continued depreciation of the shilling, increasing global uncertainties, slowdown in global economic growth and increased commodity prices. Additionally, high debt servicing costs, high fuel prices and continued foreign capital flight continue to slow down GDP projections.

- **Agriculture to Remain Driver for Economic Growth:** During Q1'23, the agricultural sector expanded by 5.80% from 1.70% in Q1'22 as a result of favorable weather conditions. We expect agriculture to continue to remain a significant contributor to the local economy (+20% contribution) in the coming quarters resulting from the onset of the rainy season that will see an increase in food production. However, we remain concerned with the high cost of farm inputs increasing the cost of production in the sector. We foresee almost identical factors to continue driving the deceleration witnessed in the manufacturing sector.

- **Growth Will Come from Export Driven Sectors:** We expect growth to be driven by the rebound of sectors that were worst affected by the pandemic such as accommodation and food service. Additionally, we expect the foreign exchange difficulties to continue favoring export driven sectors such as mining and agriculture.

Graph 3: Kenya's Five Year Historical Q1 GDP Growth



Source: KNBS, AIB-AXYS Research

Table 1: Q1'23 Summary Economic Performance

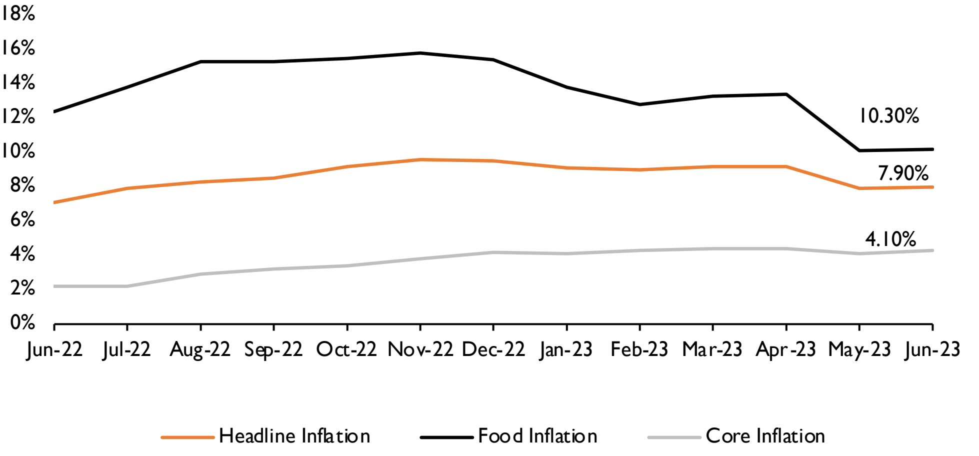
	Sector	Growth Rate Q1'22	Q1'23	Driver	Our Comments
1.	Agriculture	1.7%	5.8%	• Milk; -15.70% • Tea production; -13.00% • Coffee Exports; -5.40% • Cane Production; -0.43%	• We expect a further growth in this sector as favorable weather condition persists consequently increasing food production. However, higher input prices and inadequate rainfall will weigh down on growth. **Outlook:** Positive
2.	Manufacturing	3.8%	2.0%	<u>Food</u> • Bakery; +15.20% • Fish; +7.20% <u>Non-Food</u> • Metal products: +14.90%	• We expect muted growth driven by Fx challenges as majority of raw materials are imported. Higher input costs for raw materials, labour and energy will increase operating costs. Elevated inflation has reduced consumption power thus reducing turnover. **Outlook:** Negative
3.	Construction	6.0%	3.1%	• Cement Consum; -7.70%	• Building approvals have moderated with the sector having a huge share government pending bills. Higher inflation is likely to drive up the cost of construction materials. **Outlook:** Negative
4.	Electricity and Water Supply	3.2%	2.3%	• Geothermal; +46.80 • Wind Power; +13.50%	• We expect geothermal and wind power supply to take lead soon in the awake of the government measures of combating climate change. Talk of water sector PPPs is positive for growth. **Outlook:** Positive
5.	Transportation and Storage	7.7%	6.2%	• SGR Passengers; +15.20% • Mombasa Port Goods (Metric Tones); +1.80%	• We expect to see a decline in this sector following the current new tax laws that saw fuel VAT rise 16% from 8%. **Outlook:** Neutral
6.	Accommodation and Food Service	40.0%	21.5%	• Visitors' arrival through JKIA and MIA; +50.00%	• We expect continued steady growth in this sector given recovery of domestic and foreign tourists. **Outlook:** Positive
7.	ICT	9.0%	8.7%	<u>Domestic</u> • Voice minutes; +12.30% • SMSs ; +25.70% • Mobile Money; +7.10%	• We expect huge growth in this sector driven by government investments. However, inflationary pressure could slowdown consumers purchasing power. **Outlook:** Positive
8.	Finance and Insurance Activities	17.0%	5.8%	• CBR(March); +35.71% • Cost of Credit; 155.88% • 91-Day T-Bill yield (March) ; +34.62%	• The sector is likely to be affected by the recent CBR rate increment as borrowers may shy away from borrowing due to high cost of credit. **Outlook:** Positive

Source: KNBS, AIB-AXYS Research

Inflation

- **Inflation To Remain Elevated:** Headline inflation in H1'23 averaged 8.53% compared to 6.25% over a similar period in 2022. The May inflation print increased to 8.00% from 7.90% in April and decreased to 7.90% in June. The non-food-non-fuel inflation (core inflation) almost doubled to 4.10% from 2.20% in June 2022. The increase in core inflation's contribution to overall inflation reflects the stickiness of inflation as it entails the non-volatile element of CPI calculation. We believe that spillover effects from the high food and fuel inflation is driving the higher core inflation.

Graph 4: Core Inflation Has Remained Sticky as Headline Inflation Remained Above CBK's Upper Target



Source: KNBS, AIB-AXYS Africa Research

- We expect the onset of the short rains to positively impact food production easing of food prices. We expect the increase in VAT on petroleum products to 16.00% from 8.00% to increase pressure on headline inflation with the significant increase of fuel prices. We remain concerned with the continued increase in inflation and stickiness of core inflation and expect inflation to remain above the CBK's upper target of 7.50% in H2'23 but gradually decrease back to the CBK target range towards end of the year. **In H2'23, we anticipate that global inflationary pressures will begin to ease as a result of the effects of monetary tightening and supply chain recovery. Commodity, food and gasoline prices are anticipated to continue declining in Q3'23 as central banks are expected to continue tightening their policies or maintain them to mitigate inflation expectations.**

Table 2: Inflation Has Been Edging Down Across Markets Globally

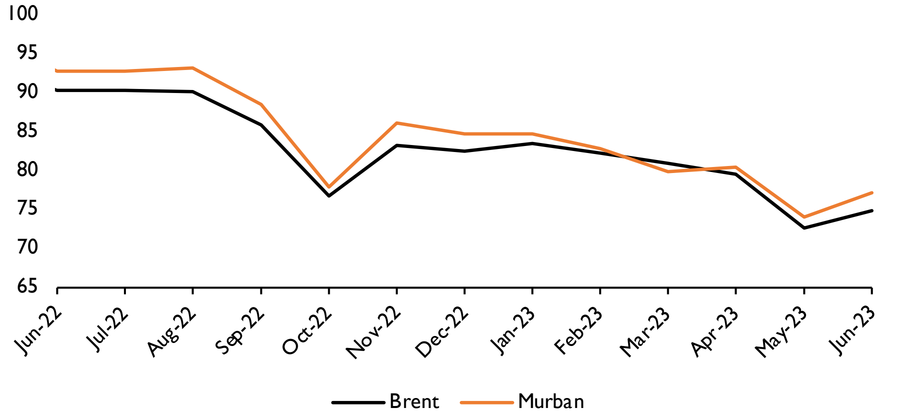
	Country	Inflation Rate			Base Lending Rate	
		April 23	May 23	June 23	Decision	Current Rate
1.	USA	4.90%	4.00%	3.00%	No Change	5.00%
2.	France	5.90%	5.10%	4.50%	25bps Hike	4.00%
3.	Ghana	41.20%	42.20%	42.50%	No Change	29.50%
4.	Rwanda	28.40%	22.40%	20.40%	No Change	7.00%
5.	Egypt	30.60%	32.70%	35.70%	No Change	18.25%
6.	Kenya	7.00%	8.00%	7.90%	100bps Hike	10.50%
7.	Uganda	8.00%	6.20%	4.90%	No Change	10.00%
8.	Tanzania	4.30%	4.00%	3.60%	No Change	5.00%

Source: National Statistics, AIB-AXYS Africa Research

Inflation – Effect from Oil Prices

- **Crude Prices to Remain Steady:** Global oil prices continued to decline during the quarter amid recessionary fears, weakened demand in China and economic uncertainties. Sanctions against Russia whose supply has nearly fully recovered will continue to affect their oil exports affecting global supply and elevating prices. Continued OPEC+ production cuts are expected to elevate global oil prices despite weaker demand resulting from global economic uncertainties. As supply of oil continues to remain constrained, it is expected that crude oil prices could increase in Q3'23.

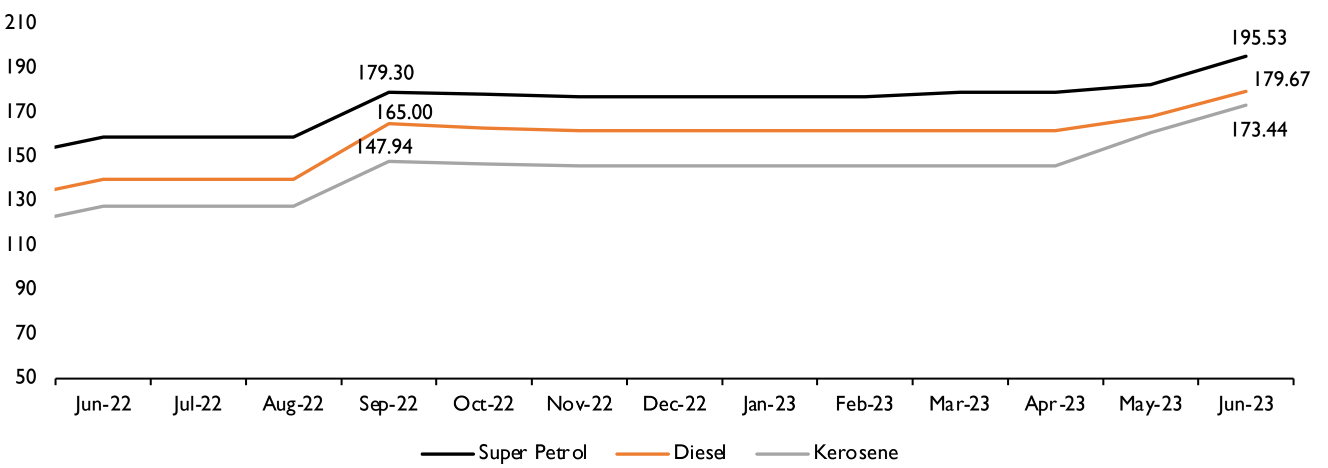
Graph 5: Global Crude Oil Prices to be Affected by Production Cuts



Source: Nasdaq, Bloomberg, AIB-AXYS Africa Research

- **Increase in VAT to Affect Local Pump Prices:** Despite the decrease of global oil prices, local pump prices were on the rise in H1'23. In June 2023, the government passed the Finance Act 2023 which saw the increase in VAT on fuel products to 16.00% from 8.00%. This led to a significant jump in the cost of fuel which we expect to increase the cost of living. **We expect the Reduction of levies (Railway Development Levy and the Import Declaration Levy) in the Finance Act 2023 to have minimal positive effects on local pump prices**.

Graph 6: Local Pump Prices Will continue Edging up



Source: EPRA, AIB-AXYS Africa Research

Fiscal Policy

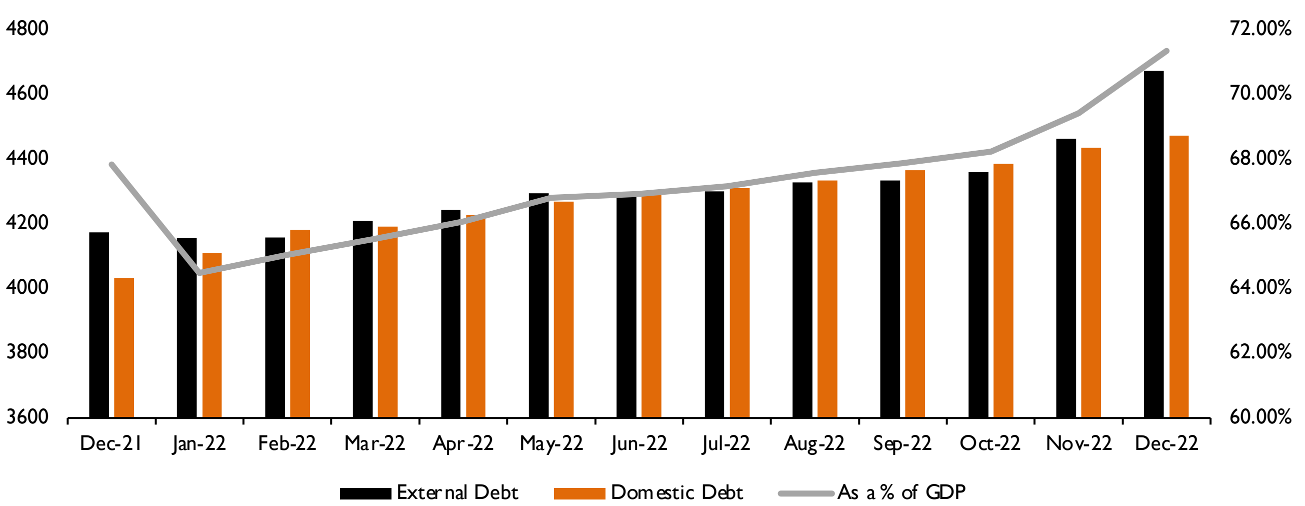
- **Budget Statement FY 23/24 :** The governments budget for FY23/24 increased to KES 3.68Tn from KES 3.38Tn with the aim of economic recovery and inclusive growth. Total revenue is expected to come in at KES 2.92Tn (17.90% of GDP). The government intends to reduce its fiscal deficit by 12.87% to KES 717.98Bn (4.4% of GDP) through enhancing revenue collections and realigning resources to key sectors. The government plans to finance the budget deficit by increasing net domestic borrowing and reduce reliance of foreign financing. **We expect the government will be keen on meeting revenue collection targets to reduce the need for additional borrowing.**

- **Revenue Collection:** Total revenue collection in eleven months of FY22/23 stood at 78.62% which is KES 2,603.51Bn of the prorated KES 3,311.30Bn. Tax revenue collection stood at 90.05% which is KES 1,1740.00Bn of the prorated KES 1,932.63Bn ,was attributable to elevated inflation having a detrimental effect on consumers purchasing power and tax collection efforts. **We expect increased pressure on KRA to meet revenue targets through widening of the tax base and reforming of tax policies in order to improve collections.**

- **Expenditure:** In the eleven months of FY22/23, reduced government expenditure coincided with low performance in revenue collection. Recurrent expenditure stood at KES 975.12Bn which was 84.03% of the prorated KES 1,160.47Bn. Development expenditure has remained low at KES 191.12Bn which was 52.94% of the prorated KES 360.99Bn. **We anticipate continued diminished development expenditure as a result of the challenging economic environment.**

- **Fiscal Deficit:** Domestic borrowing stood at **KES 464.66Bn** which is **57.18%** of the prorated **KES 812.64Bn**. With continued depreciation of the shilling against foreign currencies, the cost of servicing external debt has increased. In order to plug the budgetary deficit, the government has increased borrowing which has resulted in concerns of high debt distress.

Graph 7: Debt-to-GDP has remained Above IMFs recommended levels

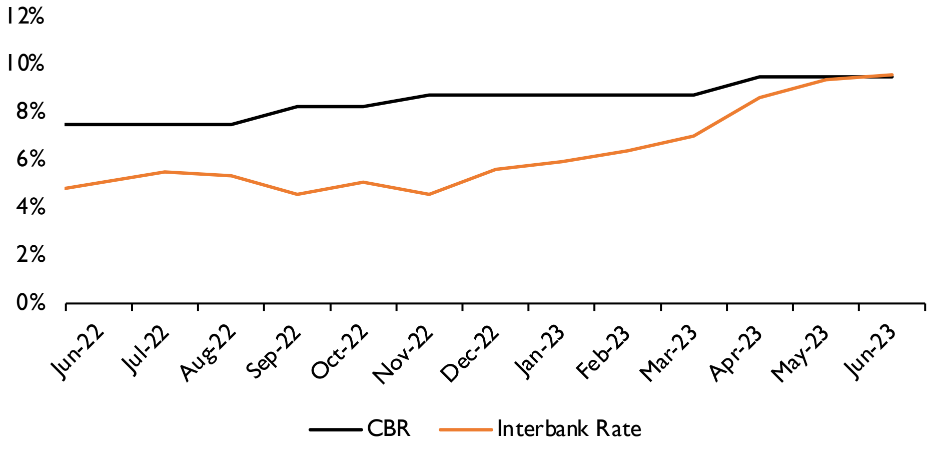


Source: CBK, AIB-AXYS Africa Research

Monetary Policy

- **Aggressive Stance:** In 2023, the Monetary Policy Committee (MPC) tightened the monetary stance by increasing the CBR by **175bps** to **10.50%** from **8.75%** as at the end of 2022 marking the fifth hike from Q1'22. Central banks globally have continued to aggressively hike their base rates in reaction to heightened inflation resulting from the ongoing global uncertainties. In raising the CBR, the MPC hopes to stabilize the economy against shocks from the rising global prices and supply chain issues. **We expect the CBR to be maintained in the short term as the effects of the hike are transmitted across the economy.**

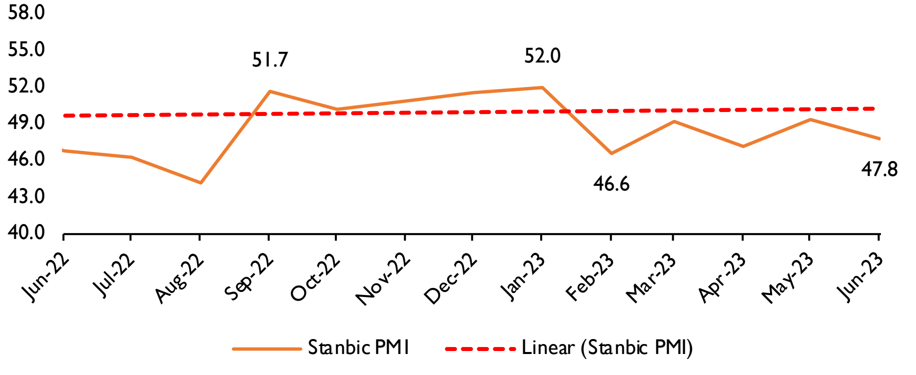
Graph 8: Central Bank Rate (CBR) and Interbank Rate (IBR)



Source: CBK, AIB-AXYS Africa Research

- **Business Environment Remains Challenged:** Following a decline in business condition in 2023, we observed a further decline in business activity as recorded by the Purchasing Managers Index (PMI) that averaged 48.70 in H1'23 from 49.25 in H1'22. We expect the PMI to remain below the 50-point threshold in the short-term on the back of high input costs and depreciation of the shilling, but gradually improve in the long-term. Near-term concerns are driven by elevated inflationary pressures, elevated input costs and the continued depreciation of the shilling. **We foresee business activity improving driven by better private sector credit growth, better agricultural production following the onset of short rains and benefits of the monetary tightening.**

Graph 9: Stanbic Kenya PMI



Source: Stanbic PMI, AIB-AXYS Africa Research

Currency

- **Shilling To Continue Declining Against The USD:** In H1'23, the shilling further depreciated by 13.94% against the US Dollar to close at KES 140.52 compared to a 4.16% decline in H1'22 (Closed at KES 117.83). This is attributable to the strengthening of the dollar against emerging market currencies, the rise in global commodity prices leading to higher demand for dollars and the reduction of dollar receipts from agricultural produce.

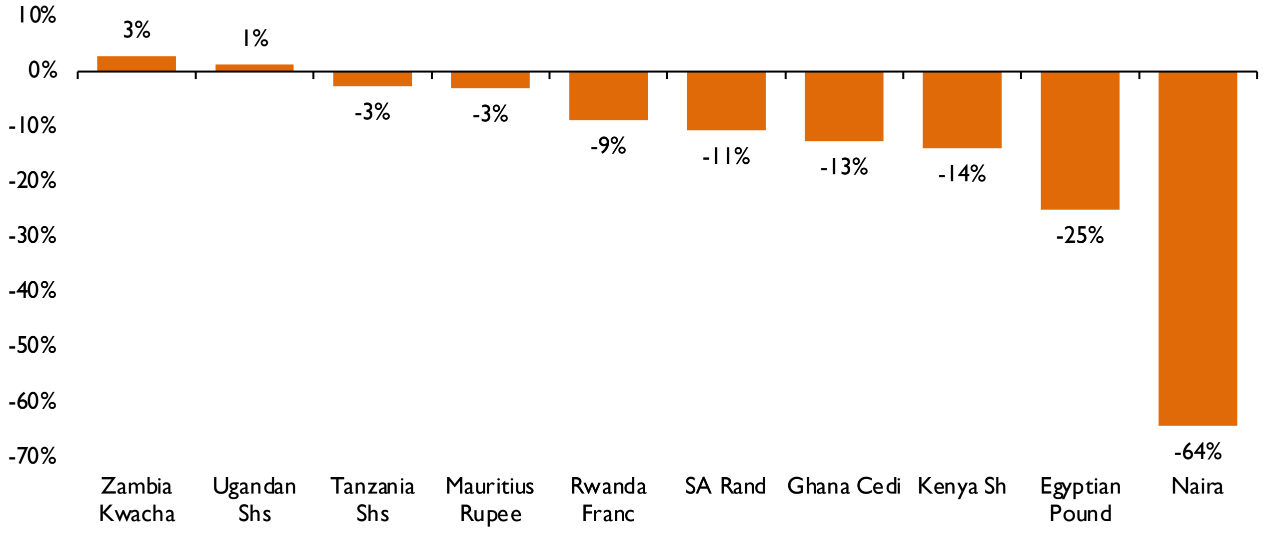
Table 3: KES Has Depreciated Against Majority of the Comparative Currencies

	USD	EUR	GBP	RAND/KES	KES/UGX	KES/TZS
3Q22	-2.46%	-5.55%	-9.07%	-8.08%	0.19%	-2.40%
4Q22	-2.19%	-12.06%	-13.62%	-7.22%	-5.82%	-2.06%
1Q23	-7.26%	-9.98%	-10.24%	-1.89%	-5.14%	-6.53%
2Q23	-6.19%	-5.97%	-8.31%	-3.46%	-8.69%	-2.81%

Source: CBK, AIB-AXYS Africa Research

- Foreign exchange reserves dipped in 2023 averaging USD 6,826 equivalent to 3.81 months of import cover which is below CBK's statutory requirement of at least 4 months of import cover. This was on the back of increased dollar outflows in debt servicing. **We anticipate that the shilling will continue the losing streak against the dollar having already depreciated higher than the 9.04% recorded in 2022. The dollars continued strengthening against Frontier currencies coupled with foreign denominated debt repayment will further weaken the forex reserves. Additionally, dividend repatriation in Q3'23 in the equities market will further increase demand for the dollar. The inflow of dollar investments through FDI's, NSE Market and other capital inflows will be a key source of dollar supply helping KES sustain resistance.**

Graph 10: Performance of select African Currencies vs USD



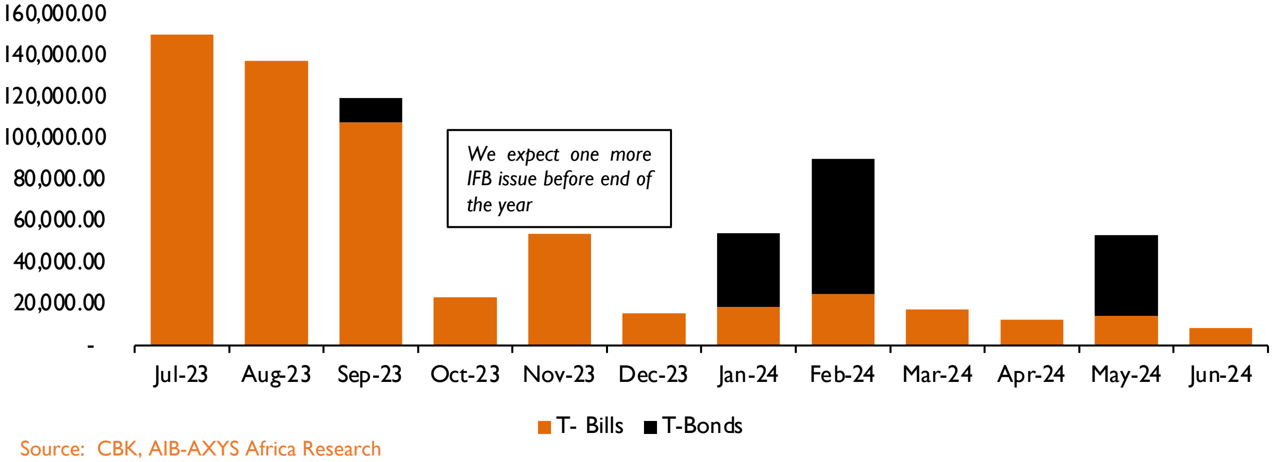
Source: Bloomberg

Interest Rates Outlook

➢ **Appetite for Fixed Income:** Activity in the Fixed Income market increased as investors continued to prefer the higher yield on short-term government papers and higher risk adjusted returns. Treasury bond issuances were generally oversubscribed at an average rate of 94.28%. Treasury bills were oversubscribed with investors continuing to see short term risks in the market and favoring their risk-adjusted returns. During the quarter, we observed an increase in yields on all papers to firmly above the 12.00% level.

➢ In the secondary market, bond turnover decreased in H1'23 by **12.96%** to **KES 331.52Bn** from **KES 380.88Bn** in H1'22, as investors place bids in the primary market due to increased short term risks. **We anticipate increased activity in the fixed income market as investors continue to chase after papers they missed out on in the primary market.**

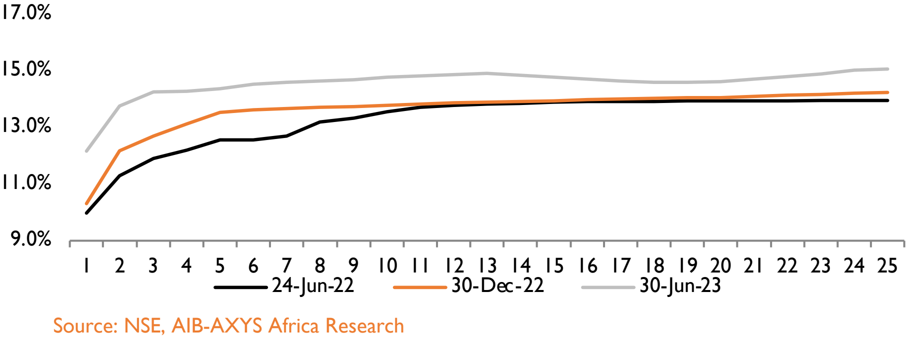
Graph 11: Upcoming Maturities for the Next 12 Months



Source: CBK, AIB-AXYS Africa Research

➢ **Yield curve steepening persists:** In line with our earlier outlook, investors have persisted in testing the governments resolve by pushing T-Bill rates above 11.00% and T-Bond rates to higher than 14.50%. The one-year paper gained the most by 1.36x in Q2'23 driven by investors demand for higher returns in response to rising local and domestic economic instability. **We expect investors to continue pushing for a 17.00% bond likely in Q3'22 as compensation for taking up additional risks and protection of their real rate of return.**

Graph 12: NSE Yield Curve Has Continued to Steepen with a Possible Inversion in the Belly Section



Source: NSE, AIB-AXYS Africa Research

Kenya Eurobond Performance

- **GOK Fiscal Position Concerns Linger -** The debt to GDP ratio remained near the 70.00% level in Q1'23, higher than the IMF recommended level of 50.00% for a 'B' rated country. In Q2'23, we saw a downgrade from Moody's rating to a B3 from B2 with a negative outlook. The rating agency observed that Kenya is facing an increase in government liquidity risks and deteriorating government financing conditions. Additionally, the external debt amortizations will rise to 2.90% of GDP in FY23/24 from 1.50% in FY22/23 increasing external debt service costs amid weaker foreign reserves and constrained external financing options.

- **External Eurobond Issuance Difficult in Hostile Environment -**Yields on all the KENINT Eurobonds increased 2.0x in 2022 driven by heightened risk perception on frontier markets and credit incidents in frontier markets like Ghana that eroded investor confidence. Currency depreciation has been negative as per our estimates a 1.00% KES depreciation increases the KES equivalent value of total Eurobond debt by KES 10.00Bn meaning the debt has ballooned by KES 140.00Bn in 2023.

- In H1'23, yields on all KENINT Eurobonds recorded a mixed performance (See table) with a downward trend mostly in last two months of the half. The improved outlook on Kenya's prospects were driven partly by IMF'S favorable outlook in the medium-term and the rebound in domestic government issuances. However, persisting concerns about Kenya's debt sustainability and political protests could erode investor confidence and create a negative outlook on Kenya's macro prospects which could lead to a rise in KENINT yields. For the upcoming Eurobond maturity, the government has three options; (1) Settle the full redemption e.g. Rwanda and Nigeria (2) Restructure e.g. Ghana (3) Outright Default.

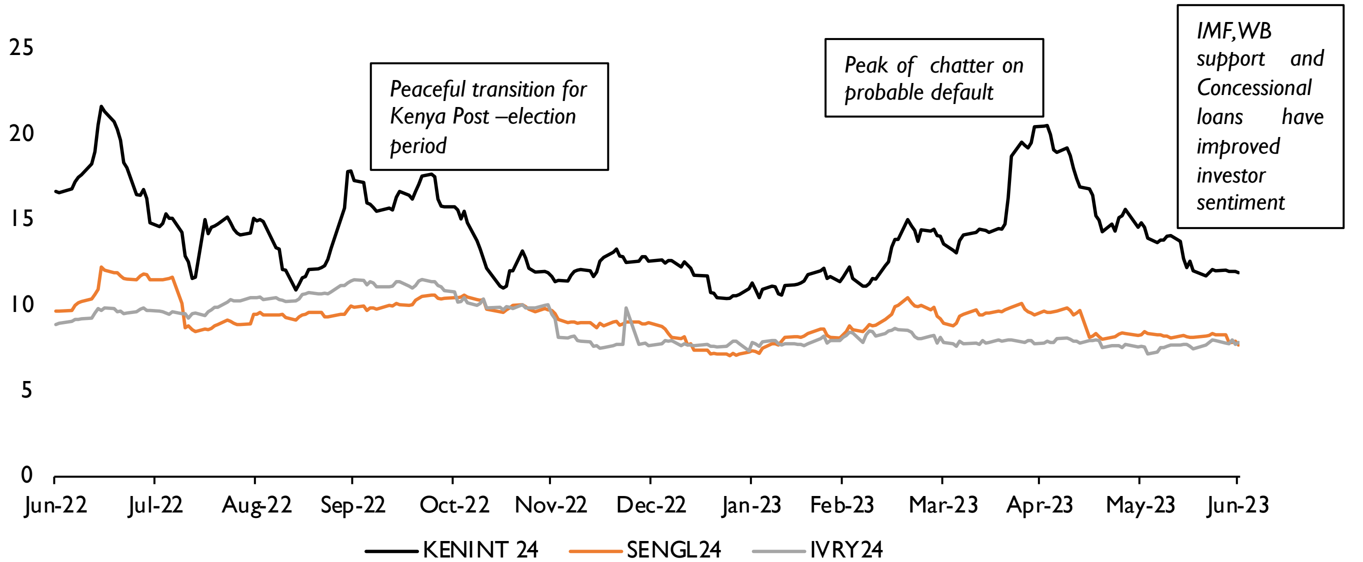
- **We believe that the Eurobond issuance environment is hostile for any new issuances as the high yields would make debt more costly for the issuer. We foresee yields will rise in 2023 primarily due to questions surrounding GOK'S debt sustainability. We do not expect KENINT yields to decline rapidly enough to enable Kenya issue Eurobonds at single-digit interest rates.**

Table 4: Kenya Eurobond Performance (H1'2023)

Kenya Eurobond	H1'23 Change (bps)
KENINT 2024	-40bps
KENINT 2027	+26bps
KENINT 2028	+62bps
KENINT 2032	+31bps
KENINT 2034	+46bps
KENINT 2048	+19bps

Source: Bloomberg

Graph 13: Kenya Eurobond Performance Against Select SSA Sovereigns (10 Year paper Maturing in 2024)

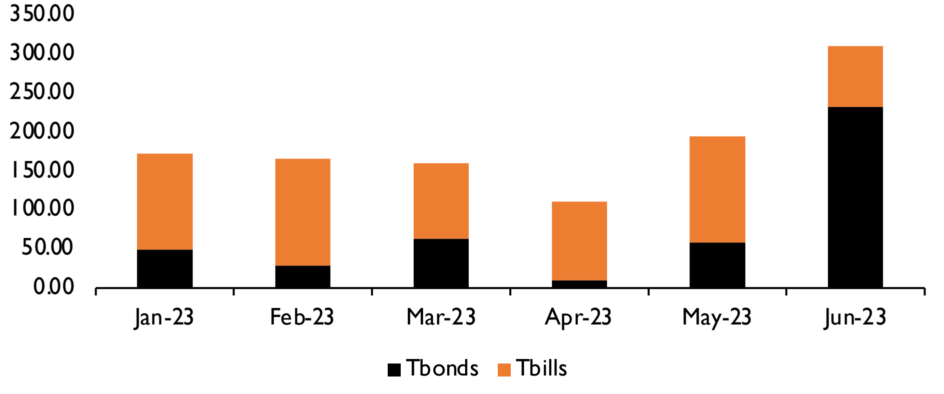


Source: Bloomberg

Fixed Income

- **Market Activity Picks Up:** Activity in the fixed income market in Q2'23 increased compared to Q1'23 with the government raising **KES 616.29Bn** compared to **KES 497.81Bn** in the preceding quarter. Increased activity was driven by investors preference for higher risk adjusted yields. We observed that all T-bill papers crossed the 11.00% level with continued preference for the 91-day paper. We observed an average T-bond oversubscription rate of 116.31% in Q2'23 and increase from an average undersubscription rate of 76.66% in Q1'23. Similarly, there was increased frequency in tap sales of shorter-dated bonds with the government taking advantage of positive investor sentiment to raise additional funds to meet fiscal obligations, further bolstering market activity during the quarter. Notably, we witnessed a 3.67x oversubscription in the 7-year IFB bond, the highest domestic bond oversubscription with the yield crossing the 15.00% level , indicating investors willingness to test the CBK's resolve against higher yields.

Graph 14: Fixed Income Performance



Source: NSE, AIB-AXYS Africa Research

We expect continued increased activity in the fixed income market as investors continue to push for higher yields and continue seeking refuge from volatility in other asset classes.

Key Fixed Income expectations in H2'23 include;

i. **T-bills to edge higher** - T-bills to remain firmly above the 12.00% level with continued preference towards the 91-day paper.

ii. **Primary market Investors to Continue Demanding a Premium** - Investors to continue demanding a premium by placing aggressive bids in the T-Bonds Primary market. We expect T-Bonds to touch a near 20% especially on issuance of longer tenures.

iii. **Government to Remain Conservative in Primary Auctions** - Government to manage further yield rise through a conservative acceptance rate. Due to a tighter macro environment investors will continue protecting their real rate of return by demanding higher compensatory rates.

iv. **Secondary Market to Remain active** – Investors who missed out in the primary issuance have been driving demand for papers in the secondary market more so the IFB papers. We expect this to continue in H2'23 on the back of lower expected acceptance levels.

Equity Market

- **Market Activity Remains Subdued :** Activity in the equities market in Q2'2023 worsened with the equity turnover decreasing by 34.75% to **KES 14.39Bn** from **KES 22.05Bn** in the preceding quarter. Benchmark indices recorded losses with the NASI and NSE-20 declining 5.11% and 2.91% to close at **KES107.00** and **KES 1,574.92** respectively. The YTD loss for the NASI and NSE-20 stood at **(16.06%)** and **(6.04%)** respectively. The bourse's market capitalization declined by 2.91% to **KES 1.94Bn** from **KES 2.34Bn** in Q1'23 indicating decrease in overall value of listed companies. We believe the subdued market activity was brought about by continued foreign investor outflow during the quarter impacting market confidence.

Table 5: NSE Indices Performance

	Q3'22	Q4'22	Q1'23	Q2'23
NSE 20	-9.72%	-11.90%	-3.22%	-6.04%
NASI	-22.86%	-23.42%	-11.54%	-16.06%

Source: NSE, AIB-AXYS Africa Research

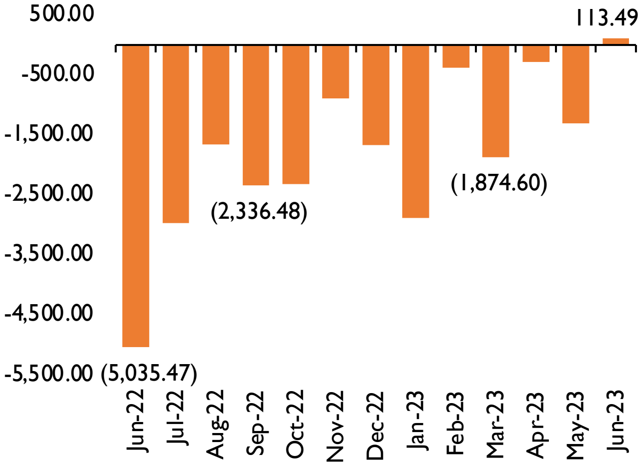
We expect further foreign investor selloffs in H2'2023, albeit at a slower rate, driven by continued negative investor sentiment on emerging and frontier market as well as a negative local currency outlook. The continued hiking of benchmark rates in developed markets has made returns more attractive and this likely to drive further foreign exits. Performance is anticipated to be sluggish as a result of scarcity of the dollar and low returns compared to other asset classes. Upcoming settlement of dividend payments during the quarter is expected to cause little to no action on the corresponding counters.

Table 6: Our Top Picks for H2'23

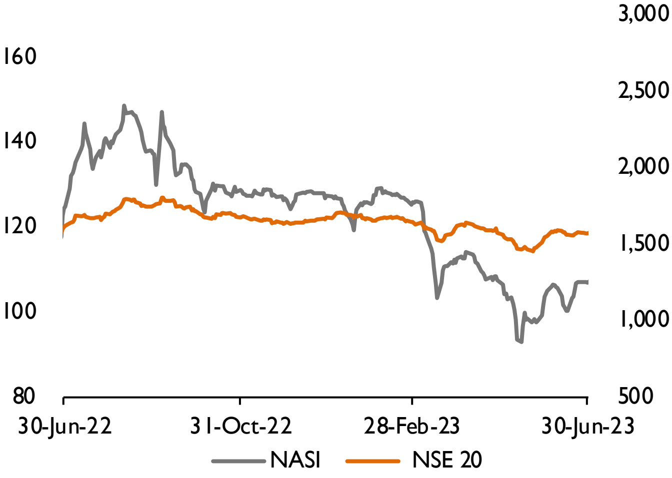
	Stock	Returns YTD (%)	Div Yield (%)	Trailing P/E (x)	Our Comments
1.	Safaricom	-20.08%	6.22%	11.87x	• We expect Mpesa and Data to be the key growth drivers. Voice business will remain challenged by regulatory measures i.e higher excise duty and reduced MTR likely leading to defensive pricing, especially in the Kenyan market. We remain positive on Ethiopia growth prospects following IFC funding.
2.	KCB	-17.06%	6.33%	2.41x	• Future growth in the bank's earnings will be driven by digital channels, loan book growth and regional subsidiaries consolidation. We are concerned with the historically above-industry average NPL numbers. We expect an interim dividend in H1'2023.
3.	Equity	-17.06%	9.20%	3.65x	• We expect regional subsidiaries, use of digital channels and Forex trading revenue to drive Non-Interest Income. The bank's lending will be supported by the focus on more SME credit and sector specific initiatives such as trade finance and infrastructure funding in subsidiary markets in Rwanda, Uganda and DR Congo. We expect an interim dividend in Q3'2023.
4.	NCBA	1.27%	10.66%	4.09x	• Expected continued growth of Digital loan product business Fuliza and M-shwari, robust digital channels and Expected approval of the risk-based pricing model will drive future growth. We expect an interim dividend in H1'2023 or Q3'2023.
5.	BAT	-4.08%	12.92%	6.59x	• We expect BAT to keep the pricing benefit advantage though it has proven to be negative with consumers down grading to less premium brands. Additional taxes and inflationary pressure are eating into the profits. We expect the total FY'23 DPS at similar levels to FY'22.
6.	EABL	-1.19%	6.65%	11.00x	• Mainstream spirit and new frontiers such as Senator keg are expected to be key revenue drivers supported by beer and premium brands. Tanzania and Ugandan consistent and strong growth is a huge positive. We expect a final dividend of KES 3-5.00
7.	Jubilee	-6.54%	6.46%	2.04x	• We view the diversified portfolio, merger with Allianz and continued digital investments as an advantages over other competitors. However, the continued consumer pressure will hurt the insurance sectors with lower premiums uptake and increased claims. However, we expect JUB to remain resilient with a DPS of >KES 10.00 going forward.

Source: KNBS, AIB-AXYS Research

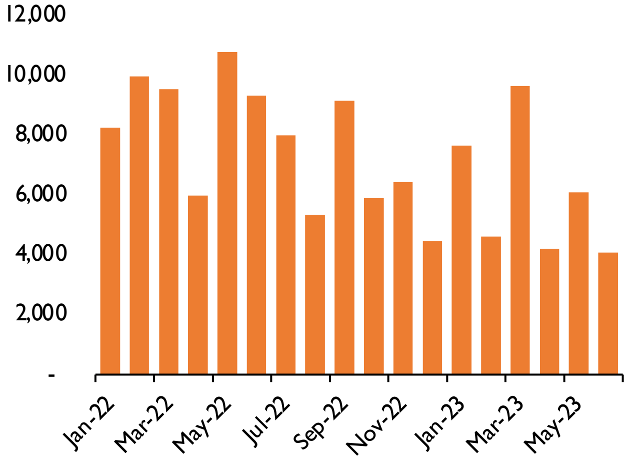
Graph 15: NSE Net Foreign Activity Turned Positive in June'23



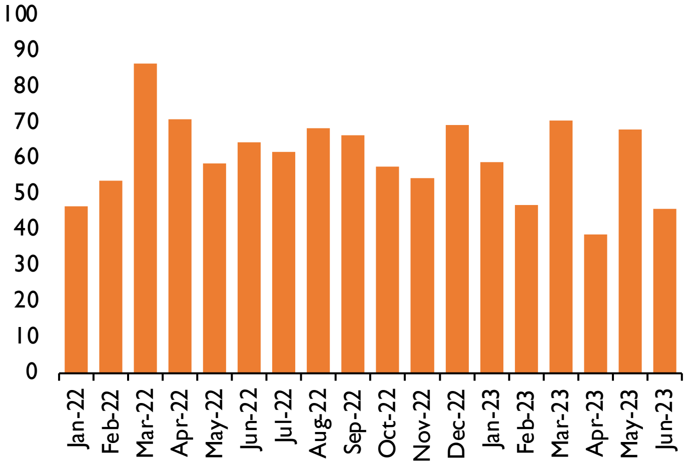
Graph 16: NSE Indices Have Been Declining in 2023



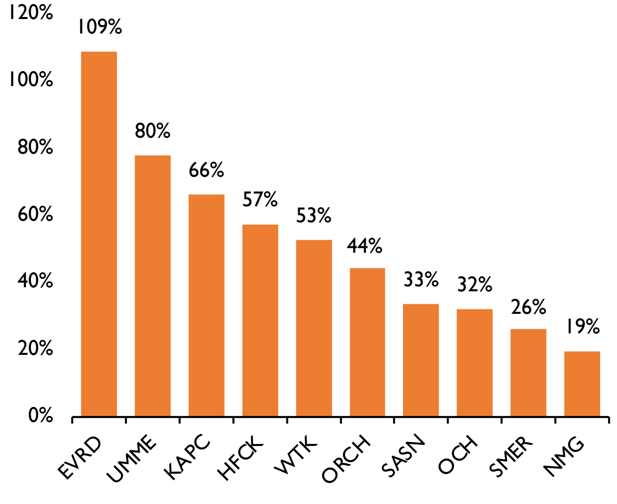
Graph 17: Equity Turnover



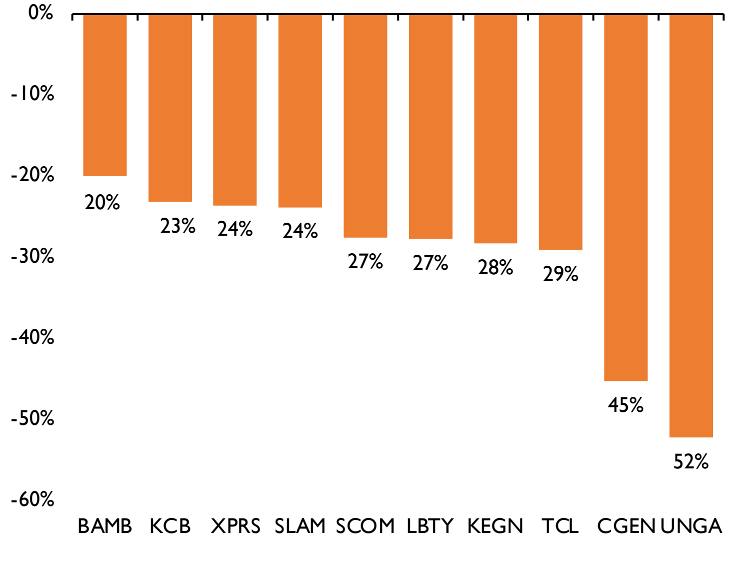
Graph 18: Secondary Market Bond Turnover



Graph 19: Top 10 Gainers H1'23



Graph 20: Top 10 Losers H1'23



Source: CBK, AIB-AXYS Africa Research

Table 7: Scenario Proposition for Key Market Drivers in H2'2023

	Best Case	Base Case	Worst Case
GDP Growth	• Economic growth rate will be above the Government's projection of 6% (4.5% in Q1'23)	• We foresee economic growth maintaining at similar levels to Q1'23	• Economic growth will trend 100 bps lower than the Q1'23 print.
Inflation	• Better food production benefits will outweigh any negative impact leading to inflation treading to lower than the target range mid point	• Ample food production to keep inflation within CBK target. New G-to-G oil deal to be +ve to fuel prices	• Low rainfall, high pump prices negative effects across the economy and government subsidies not bearing enough fruit
Currency	• Higher export earning sectors (Agriculture, tourism and diaspora remittances) will boost currency performance	• Fx volatility to persist with minimal benefits from the G-to-G oil deal. Import to drive fx demand	• KES depreciation to hit >150/USD levels. With interbank forex market remaining challenged
Interest Rates	• CBR to remain at current levels thus preventing further rates increase. The government to reject expensive bids thus taming investors' demand for a premium.	• MPC to maintain CBR until end of year and monitoring any effects. Investors to continue hunt for higher yields edging the yield curve higher	• Further CBR hikes to signal a higher rates possibility. Yield curve to edge higher as investors protect their real rate of return
Business Environment	• Business owners outlook to improve with the PMI staying above 50. Businesses to be elastic to prevailing challenges as they adapt correspondingly	• PMI reading to remain at around 50 on the back of tough operating dynamics	• Damp business outlook with PMI at <50. Higher input costs to weigh down on factory output, jobs and sale orders
Political Risk	• With the conclusion of 2022 elections the political temperatures have cooled off. We foresee minimal interruptions from the opposition driven weekly protest if the government agrees to a truce	• Weekly protests to continue with effect on business operations limited to the day of the protest	• Weekly protests to be negative on business climate in major cities. Political rumblings to negatively affect investor sentiment
Fiscal Policy	• Government spending including settlement of pending bills in H1 of FY 23/24 will drive economic growth. However, new taxes will weigh down on economic performance due to higher cost of doing business	• Fiscal consolidation to remain on track with KRA being aggressive tax measures while government spending remaining on track as per budget estimates	• Challenging business climate and the challenges facing Finance Act 2023 to lead lower tax collection which is likely to limit government spending
Equities	• Positive outlook driven by banking sector interim dividends, recovery in blue chip counters and reduced foreigner net selling position	• Foreign exits to continue but better performance by blue chips to support overall market outcome. Interim dividends from banks will be a positive	• Foreign exits with limited local support, lack of interim dividends and profit warnings to negatively affect the shares market

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