Primary Auction Note – November 2022

November 7th 2022

The Central Bank of Kenya is in the market looking to raise **KES 60.00Bn** for funding of Infrastructure projects in the FY 2022/2023 budget estimates through the issuance of **IFB1/2022/14.** The coupon rate will be market-determined with bidding closing on the 8th of November 2022. The minimum investment is KES 100,000 with an effective duration of 11 Years.

We expect the issue to be oversubscribed due to the tax-free nature of IFB issues and high yields currently being offered by government papers. We anticipate a resurgence of interest from foreign investors, who we also suspect have been avoiding the local primary market due to election-related risks. However, the participation of international investors is likely to be constrained by the ongoing depreciation of the shilling.

We expect aggressive bidding driven by;

I. **Investors' increased preference for higher risk-adjusted returns** – From the performance of recent FXD issues and T-Bills investors bidding trends have shown a risk vs duration mismatch. The recent 25-year paper successfully crossed the elusive 14.00% level and we also expect investors to test CBK's resolve in this issue

II. **High inflation levels** - Given the risks associated with the current high levels of local and global inflation, we anticipate that investors will make aggressive bids on this paper trying to compensate for a higher real rate of return. Local inflation for the month of October hit a 65-month high of 9.59% with fears of this edging up even further

Given the upcoming T-Bond maturities and coupon payments in the month of November coupled with budgetary needs, we foresee increased pressure on the government to accept expensive bids. The lack of transparency on the specific infrastructure projects to be financed by the IFB leads us to believe that some proceeds from the paper could be used for other budgetary needs.

Indications of upcoming budget cuts may result in a reduction in the demand for borrowing later in the fiscal year. As a result, there will be less pressure on the government to borrow and accept high-interest rates, which will cause yields to decrease. Additionally, the historically low subscription rate in Q4 of the calendar year is likely to be also reflected in this issue and could contribute to poor performance.

Summary Bidding Guidance:

Issue No	Amount Offered	Next Coupon Payment	Coupon Rate	Bidding Range
IFB1/2022/14	KES 60.00Bn	15/05/ 2023	TBD	13.64% -13.89%

RECOMMENDATIONS:

IFB1/2022/14

Bid: 13.64%– 13.89%

Period of Sale: 26/10/2022 to 8/11/2022

Sovereign Credit Rating:

Moody's: B2 (negative)

Fitch: B+ (negative)

S&P:B (stable)

October CPI: (2019=100): 127.86

October Inflation: 9.59%

Interbank Rate (31st October 2022): 4.80%

C.B.R (Oct '2022): 8.25%

Analysts

Solomon Kariuki

Faith Sang

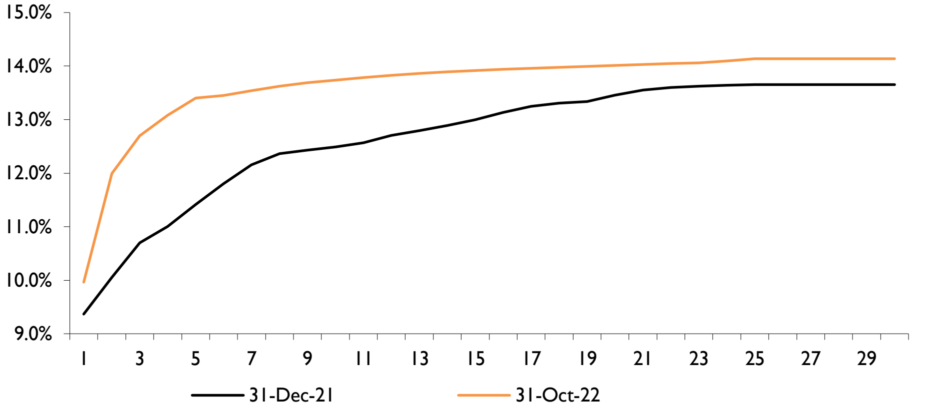
Tel: +254114842208

Email: research@aib-axysafrica.com

Liquidity

During the month of October, the money markets largely remained liquid supported by government payments. Mostly, interbank rates remained sub 5.00% levels having recorded **4.68%** on 31st October a 100bps decline from 5.68% recorded on 30th September 2022.

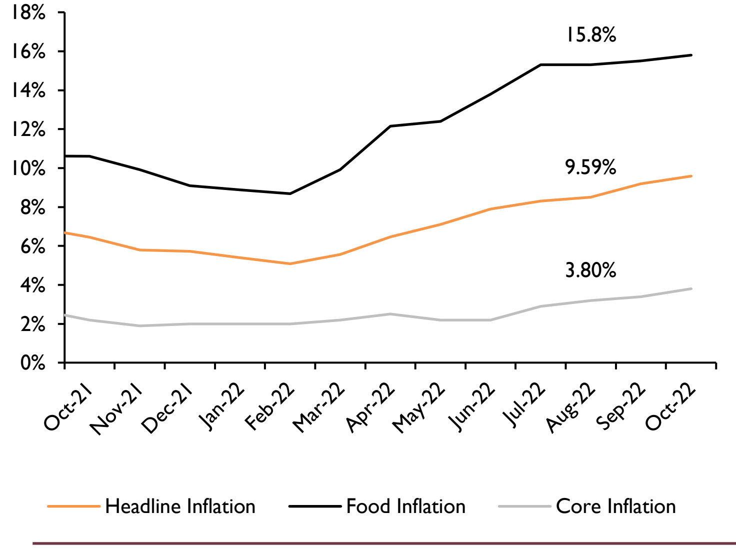
NSE Implied Yield Curve



In the month of October, yields increased across the curve. 4-year papers increased the most by 375bps while the 17-year papers decreased the most by 90bps. The 2 and 5-year papers increased by 363bps and 360 bps m/m, respectively. We expect the yield curve to experience upward pressure across medium and long-term tenors, with a slight easing in the short-term, as investors seek higher premiums on prevailing high inflation.

During the month of October, the overall subscription rate for Treasury bills declined to 91.85% from 106.34% recorded in September. The yields on the 91-day, 182-day and 364-day papers were 9.05%, 9.65% and 9.92% respectively.

October Inflation:



- The headline inflation increased for the eighth month in a row to **9.59%** in October from **9.20%** recorded in September. The CPI increased 0.89% to **127.86** in October 2022 from **126.73** in September 2022.
- Meanwhile, the food and non-alcoholic beverages index increased by **15.80%** y/y. While the housing utilities and the transport indices increased by **7.10%** and **11.6%,** respectively y-o-y**.**
- Headline inflation remained above CBK's upper target of 7.50% driven by the 0.5% increase In the Housing, Water, Electricity, Gas and Other Fuels' Index. We anticipate continued pressure on the CPI, at least until localized effects of the global oil price slowdown, cost of electricity declines and relief from the ongoing severe drought in the nation is experienced.

CONTACTS:

Research Desk

Solomon Kariuki
Research Analyst

Faith Sang
Research Analyst

Email: research@aib-axysafrica.com

Equities Dealing

Bernard Kung'u

Benard Gichuru

Brian Tanui

Samuel Githinji

Sheema Shah

Samuel Wachira

Email: trading@aib-axysafrica.com

Bond Dealing

Crispus Otieno

Titus Marenye

Email: trading@aib-axysafrica.com