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WEEKLY FIXED INCOME NOTE

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Weekly Fixed Income Note

Week Ending: 05th May 2023

Key Highlights:

- T-bills were oversubscribed last week recording an increased overall subscription rate of 110.72% from 37.52% recorded in the previous week. Investors continued to prefer the shorter-term 91-day paper for the 12th month. We attribute the performance to investors continuing to see short-term risks in the market. We expect continued preference towards the 91-day paper given the rising yields which as expected have crossed the 10% level. Additionally, CBK's announcement of easier access to opening treasury securities trading accounts is likely to see increased retail and diaspora investors' interest. The Central Bank acceptance rate decreased to 96.13% of the **KES 26.57Bn** amounting to **KES 25.54Bn.** Yields on all the papers are now firmly above 10.00% with the 91, 182, and 364-day papers moving **4.30bps, 16.70bps,** and **4.60bps,** respectively.

- In the primary market for the month of May, the government is looking to raise KES 20.00 Bn for budgetary support through the issuance of a three-year bond. FXD1/2023/03 has a time to maturity of 3.0 years and the coupon rate will be market determined with bidding to close on 09th May 2023. For further bidding guidance please see our Primaery Auction Note.

- In the secondary market, the value of bonds traded increased by 12.05% to **KES 13.88Bn** from **KES 12.39Bn** recorded a week prior. We observed a further yield curve steepening across the curve highlighting investors' demand for higher rates. As such, the 2-year paper gained the most by **77bps.** We continue to see a yield curve inversion in the mid section which is likely to spread towards the long end depending on the maturity profile of the upcoming primary issues.

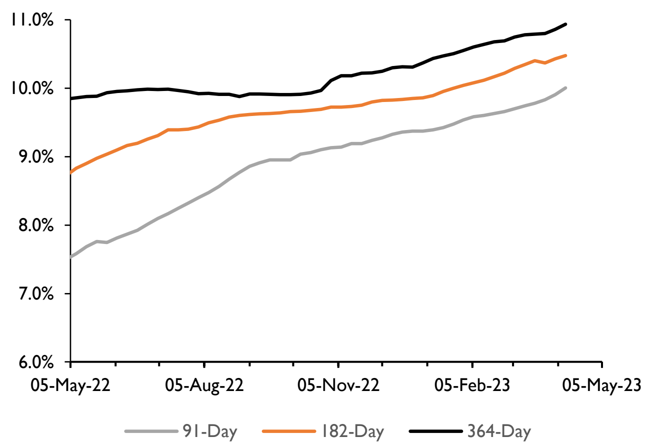
- In the international market, yields on Kenya's Eurobonds decreased by an average of 15bps indicating improved investor sentiment on the long end. We expect another week of higher yields on the 2024 paper (likely to be higher than 20% level) given the announcement of return of the weekly protests led by members of the opposition.

We expect activity in the secondary market to be driven by IFB trading with minimal negative effect from the ongoing May T-bond primary auction. We believe that the high frequency of tap sales is likely to have a negative impact on the secondary market especially for IFBs. Several transactions in the secondary market are driven by investors who missed out in the primary market. In the coming T-Bond bidding sessions, we foresee investors testing CBK's resolve on accepting rates higher than 14.50%.

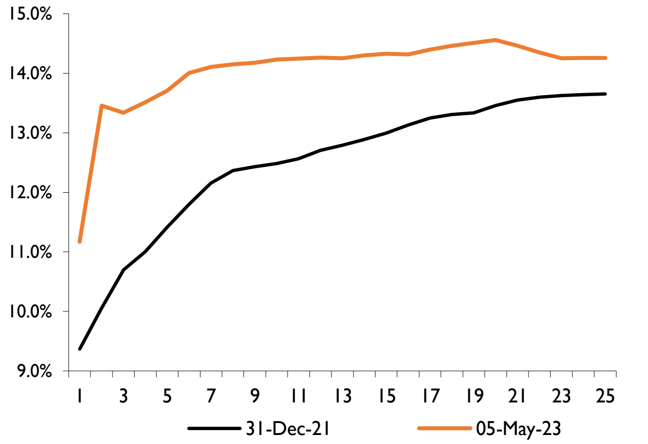
Key Indicators

	Current	Previous	w/w bps Change
91- Day	10.32%	10.28%	4.30
182-Day	10.68%	10.51%	16.70
364-Day	11.17%	11.12%	4.60
Interbank Rate	9.66%	9.18%	(47.95)

T-Bill Rates



NSE Implied Yield Curve



MACROECONOMIC NEWS

Currency

The Kenya shilling further lost ground against the USD, depreciating **36bps** to **KES 136.40** from **KES 135.91** the previous week. On a YTD basis, the shilling has depreciated **10.60%** against the USD ,depreciation exceeded the 9.04% depreciation recorded in 2022. The CBK's usable forex reserves declined marginally remaining below the 4.00 months level to close last week at **USD 6,492Mn** (**3.61 Months** of Import Cover), a 25bps week-on-week decrease from **USD 6,508Mn** (**3.62 Months** of Import Cover), recorded last week. The current reserves remain below the CBK's statutory requirement (4 Months) & EAC Convergence requirement (4.5 Months) of import cover. **We expect the local currency to continue coming under pressure due to the increased dollar demand from importers on the back of the prevailing high global commodities prices, and reduced dollar inflows from key export-earning sectors. Additionally, the depreciation is driven by the continued strengthening of the dollar against emerging and frontier markets currencies.**

Liquidity

Liquidity in the money market tightened as shown by the average interbank rate increasing 47bps to 9.66% from 9.18% recorded a week prior. We partly attribute the tightening to the statutory deductions and tax remittances outpacing government payments. **We expect the interbank rate to remain above 9.00% levels in the coming week, mainly driven by the remittance of monthly obligations, delayed government payments and CBK's open market operations.**

Macro-economic News Roundup

The private sector's economic outlook measured by the Purchasing Managers Index (PMI) decreased to 47.2 in April from 49.2 in March 2023. A PMI reading of below 50.00 indicates declining business conditions while a reading of above 50.00 shows an improvement. The most recent estimate indicates that the private sector has continued contracting, mostly as a result of political unrest and a significant decline in consumer demand resulting from cost-of-living constraints. At the same time input costs remained elevated.

During the week, the National Treasury put forward the Finance Bill 2023 in which a number of modifications were introduced with the aim to increase revenue and bring tax law into compliance with government development aims. The Act proposes the amendment of the annual inflation adjustment provision to exempt specified products in an effort to protect consumers from price increases brought on by annual inflation adjustments. Additionally, the act proposes an increase in personal income tax rates, introduction of tax on digital assets, an increase in capital gains tax , an introduction on investment deduction claims on capital expenditure among others.

We expect that the economy will continue to be constrained by the prolonged high commodity prices and prevailing inflationary pressures. In the near term, we foresee business activity improving driven by better agricultural production from the onset of short rains and benefits from the effects of the monetary tightening. However, we foresee global challenges including inflationary pressures, recessionary fears and geopolitical events likely to slow down economic growth and dampen the general business environment.

Weekly Fixed Income Calendar

- **Treasury issues -** This week, the Central Bank of Kenya, as the government's fiscal agent, is in the market for **KES 24.00Bn** in T-bills. Additionally, the April T-Bond issue is looking to raise KES 20.00Bn with bidding ending on 09th May 2023.
- **Monthly Pump Prices Review-** We expect minimal movement in the local pump prices announcement this week as cross-subsidization continues. The global crude oil prices have edged up since the announcement of additional production cut by OPEC members and this is likely to be seen in a higher fuel landing costs.

	Macro event	Date
1.	May T-Bond Auction	09th May 2023
2.	Weekly T-Bills Auction	11th May 2023
3.	May Pump Prices Review	14th May 2023
4.	May MPC Meeting	31st May 2023

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