Weekly Fixed Income Note

Week Ending: 16th September 2022

Key Highlights:

- T-bills turned to under subscription after two straight weeks of overperformance by recording a reduced overall subscription rate of **97.02%**, from **152.99%** recorded in the previous week. Investors continued to prefer the shorter-term 91-day paper for the 12th week with a 248.80% subscription rate compared to the least preferred 364-day paper at **19.57%.** The Central Bank acceptance declined to 74.59% of the **KES 23.29Bn** amounting to **KES 17.37Bn**. The reduced acceptance rate points to the need to control the rising yields by rejecting expensive bids. We are likely to continue seeing a rejection of expensive yields and an under absorption as a way to control further rates uptick. Yields on the 91-day and, 182-day papers rose **4.00bps** and **1.60bps**, respectively while the 364-day paper reduced by **0.20bps**.

- In the Primary market, September re-opened bonds were undersubscribed, contrary to our expectations, by recording a 92.27% subscription rate. Investors preferred the shorter-dated paper, **FXD1/2022/10** with a coupon rate of 13.49% and a yield of **13.95%.** We attribute the improved interest from investors to the easing liquidity in the money markets coupled with the dissipation of uncertainty surrounding the just concluded elections. **FXD1/2022/15** with a coupon rate of 13.94% recorded a yield of **13.98%**.

- In the secondary market, the value of bonds traded decreased by **67.07%** to **KES 7.51Bn** from **KES 22.82Bn** recorded last week. The yield curve largely steepened in the longer end of the curve with flattening on the belly section. The 5-year paper gained the most by **11bps** and the **7**-year paper lost the most by **7bps**.

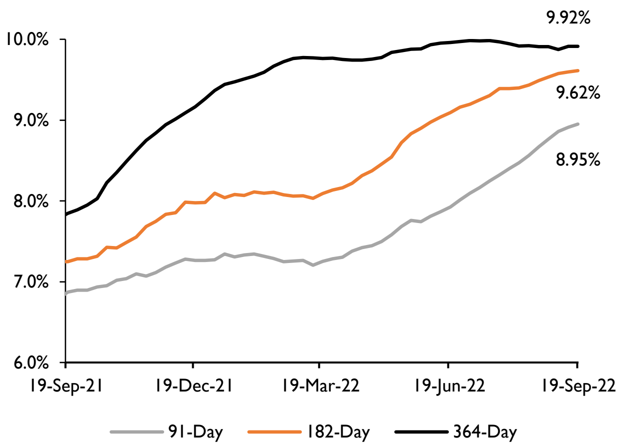
- In the international market, the yields on Kenyan Eurobond issues recorded a mixed performance largely driven by the perception of stability following the quick transition to a new government. We observed the 2024 paper reducing the most, by 70bps, highlighting the sensitivity to market sentiments given that its maturity is less than 24 months away.

We expect activity in the secondary market to be driven by investors who missed out on the recent September issue. Furthermore, we expect investors to continue preferring safer asset classes given the possibility of crystallization of the prevailing market risks.

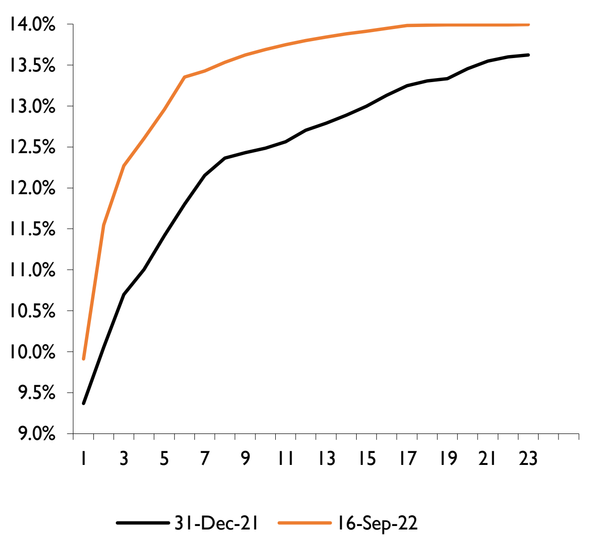
Key Indicators

	Current	Previous	w/w bps Change
91- Day	8.95%	8.91%	4.00
182-Day	9.62%	9.60%	1.60
364-Day	9.91%	9.92%	0.20
Interbank Rate	3.96%	4.33%	36.00

T-Bill Rates



NSE Implied Yield Curve



MACROECONOMIC NEWS

Currency

The Kenya shilling further lost ground against the USD, depreciating **0.09%** to trade at **KES 120.41** from **KES 120.31** the previous week. On a YTD basis, the shilling has depreciated **6.43%** against the USD compared to **4.36%** in 2021. The CBK's usable forex reserves remained adequate at **USD 7,372Mn** (**4.20** months of import cover), a **0.35%** week-on-week increase from **USD 7,346Mn** (**4.20** months of import cover) recorded last week. **We expect the local currency to continue under pressure due to the increased dollar demand from energy importers on the back of the prevailing high global oil prices, and reduced dollar inflows from key export-earning sectors. Additionally, the depreciation is driven by the continued strengthening of the dollar against other currencies as measured by the DXY index which has gained 14.25% YTD.**

Liquidity

Liquidity in the money market eased as shown by the average interbank rate falling below 4.00% for the first time in 2022. The average rate declined to 3.96% from 4.33% recorded at the end of the previous week. We attribute the increased liquidity to government payments offsetting monthly CRR requirements. Open market operations remained active. During the week, the average number of interbank deals decreased to 34 from 26 in the previous week, while the average value traded declined to **KES 21.80Bn** from **KES 13.10Bn, last week**. **We expect the interbank rate to remain below the 4.00% levels in the coming week, mainly driven by continued government payments. However, the CBK's OMO activities and monthly tax obligations, due during the week, are likely to tighten liquidity.**

Kenya Macro Economic View

The National treasury gazetted the statement of revenues and expenditures for the first two months of FY 22/23 where total revenues collected were **KES 383.37Bn** being 10.81% of the estimated collection of KES 3,544.60Bn. Tax revenues collected at **KES 280.23Bn** were 13.52% of the estimated collection of KES 2,071.92Bn and 81.72% of the prorated target of KES 345.32Bn. Going by the current tax collection rate KRA is likely to miss the FY 22/23 collection targets given the challenging economic environment. We remain concerned with the low allocation to development expenditure at KES **20.75Bn** being 5.41% of the total revenue compared to recurrent expenditure which accounted for 38.97% of total revenue.

During the week, the government announced the partial withdrawal of the prevailing fuel subsidy and we share the view that it was unsustainable given the current budgetary needs. As such, the price of petrol increased by 12.68% to **KES 179.30** as the petrol subsidy was fully withdrawn. However, a partial subsidy was retained for Diesel and kerosene whose prices increased 17.85% and 15.63% to **KES 165.00** and **KES 147.94**, respectively. The latest subsidy takes the total amount extended in the last fourteen months to KES 140.00 Bn translating to an average of KES 10.00Bn per month. However, EPRA noted that the FOB price of Murban Oil increased 7.16% to USD 117.53/barrel from USD 109.68/barrel in July'22. Meanwhile, the local currency depreciated 0.60% to trade at KES 120.64/USD in Aug'22 compared to 119.92/USD in July'22. **We expect the increased pump prices to contribute to higher overall inflation at the end of the month. Higher pump prices are negative as it increases pressure on the transport index leading to hiked bus fares. Upward adjustment of the fuel cost charge will also have additional pressure on the electricity utility index as thermal energy consumption has recently increased. Global oil prices have shown signs of retreating to pre–Russia Ukraine war levels. Additionally, there was an announcement by Saudi Arabia to increase oil supply to match increased demand and further reduce prices. However, oil prices are likely to edge higher as we approach the winter season following the energy crisis in Europe amid the Euro-Russia Nord stream pipeline tussle.**

Weekly Fixed Income Calendar

- This week, the Central Bank of Kenya, as the government's fiscal agent, is in the market for **KES 24.00Bn** in T-bills.

	Macro event	Date
1.	Weekly T-Bills Auction	15th September 2022
2.	September MPC Meeting	29th September 2022
3.	September Inflation Figures	30th September 2022

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