Weekly Fixed Income Note

Week ending: 08th July 2022

Key Highlights:

- T-bills were oversubscribed after six straight weeks of underperformance by recording an overall subscription rate of **102.46%**, up from **37.14%** recorded in the previous week. The 91-day paper recorded the highest subscription rate at **275.99%** while the 364-day paper recorded the lowest rate at **51.15%.** The Central Bank accepted **98.44%** of the **KES 24.58Bn** worth of bids received. Current fiscal year borrowing is behind the prorated target, though we do not expect pressure on the government acceptance rate as it is still early in the fiscal year with no T-bond maturities in July. Yields on the 91-day, 182-day and 364-day papers closed the week at **8.17%**, **9.25%** and **9.98%** respectively.

- In the primary market, the **IFB1/2022/18** tap sale looking to raise **KES 20.00Bn** was undersubscribed, contrary to our expectations. The government accepted 99.97% of the **KES 6.42Bn** worth of bids received. Additionally, the government is still in the market for another **KES 40.00Bn** through reopened **FXD2/2013/15** and **FXD2/2018/15**. Auction closes on 19/07/2022. We shall provide further bidding guidance through our primary auction note, later in the week.

- In the secondary market, the value of bonds traded decreased by **31.77%** to **KES 12.76Bn** from **KES 19.01Bn** recorded last week. The yield curve largely flattened across the curve with the 14-year paper losing the most by **5.21bps** and 11-year paper gaining the most by **10.99bps**. In the international market, the yields on Kenya's Eurobonds increased by an average of **37.72bps**.

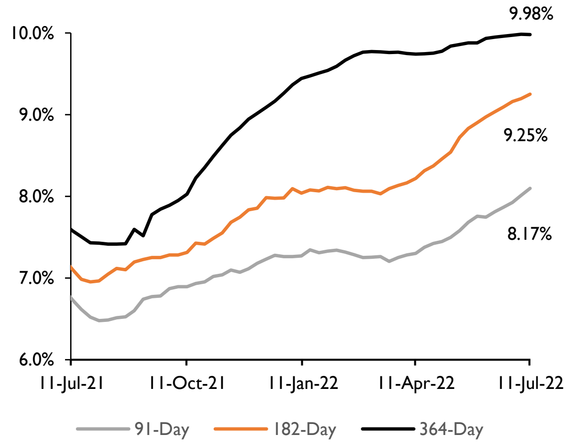
We expect activity in the secondary market to remain muted, as investors turn their attention to the fixed coupon bonds to be issued during the month. However, IFB trades are expected to continue driving the secondary market activity. We foresee a sustained preference for long-term papers from investors, factoring in greater political and post-pandemic related risks.

Macroeconomic data	Current	Previous
GDP (Q1'22 vs. Q1'21)	6.80%	2.70%
Inflation (June)	7.90%	7.10%
Private Sector Credit Growth (Apr)	11.50%	9.10%

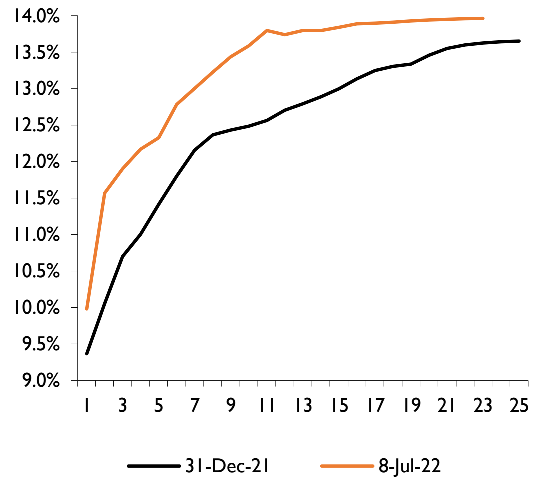
Key Indicators

	Current	Previous	bps
91- Day	8.17%	8.10%	7.00
182-Day	9.25%	9.20%	5.70
364-Day	9.98%	9.99%	0.50
Interbank Rate	5.80%	5.52%	82.00

T-Bill Rates



NSE Yield Curve



MACROECONOMIC NEWS

Currency

The Kenya shilling lost further ground against the USD, depreciating **0.87%** to trade at **KES 118.07** from **KES 117.83** at last week's close. On a YTD basis, the shilling has depreciated **4.36%** against the USD compared to **3.99%** in 2021. The CBK's usable forex reserves remained adequate at **USD 7,997Mn** (**4.61** months of import cover), a **1.02%** week-on-week decrease from **USD 7,982Mn** (**4.74** months of import cover) recorded last week. The CBK maintains that the current reserves are adequate to cover dollar demand in the market despite reports of acute dollar shortage from importers. **However, we expect the local currency to remain under pressure due to the increasing dollar demand as global oil prices remain elevated on the back of a higher import bill and reduced dollar inflows from key export earning sectors.**

Liquidity

Liquidity in the money market tightened as shown by the average interbank rate which increased to **5.80%** from **5.52%** recorded at the end of the previous week. **We expect the interbank rate to remain above the 5.00% regions given the upcoming monthly banking CRR cycle and open market operations remaining active. However, government payments, following schools reopening, could provide the necessary supply.**

Purchasing Manager's Index on the decrease

Activity in the manufacturing sector remains depressed as evidenced by the June PMI falling further to **46.80** from **48.20** in May. A PMI reading of below 50 indicates regression in the manufacturing sector and as such this is the third consecutive month of contraction and at the steepest pace since April'21. The PMI contraction was attributed to a faster decline in output and new orders, amid weaker demand due to rising price pressures. Further, cash flow shortages and the upcoming elections also contributed to the decrease**. We expect to see further pressure and increase in input costs mainly driven by rising fuel prices, prevailing global supply shortages and weaker shilling, as well as, reported dollar supply shortages. Additionally, as we enter the last 30 days to the elections, campaigns are likely to heat up delaying investment decisions and slowing activity further, at least until there is clarity on election results.**

KRA exceeds revised target

KRA released the revenue collection figures for FY21-22, where the tax man recorded an unprecedented collection figure of **KES 2.03Tn**. The FY21/22 collection was a 21.69% increase from the **KES 1.67Tn** collected the previous fiscal year. Notably, the collection was a 102.78% overperformance from the previous revised target of **KES 1.98Tn**. We attribute the good performance to increased tax base, use of technology and an improved economic environment. Recovery in key sectors led to a strong 32.70% growth in corporation taxes to **KES 242.02Bn** and an increase in PAYE to **KES 461.82Bn**. **We expect KRA to continue surpassing the revenue collection targets in the new fiscal year given the increased aggressiveness in tax evasion crackdown. Enforcement of the digital ETR machines is expected to boost domestic VAT collection. Recovery in the business operating environment is likely to be weighed down by the looming election cycle, which if not decided in the first round could drag up to May'23 (11th month of FY22/23).**

Weekly Fixed Income Calendar

This week, the Central Bank of Kenya, as the government's fiscal agent, will seek to raise **KES 24.00Bn** in Treasury Bills. EPRA is expected to release the pump prices for the period between 15th July – 14th August 2022. We expect another KES 7.00 -10.00 increase across all fuels given the elevated global prices, during the import period.

	Macro event	Date
1.	Monthly Fuel Review	14th July 2022
2.	Weekly T-Bills Auction	14th July 2022
3.	July T Bonds Auction	19th July 2022
4.	June Inflation Figures	30th July 2022

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