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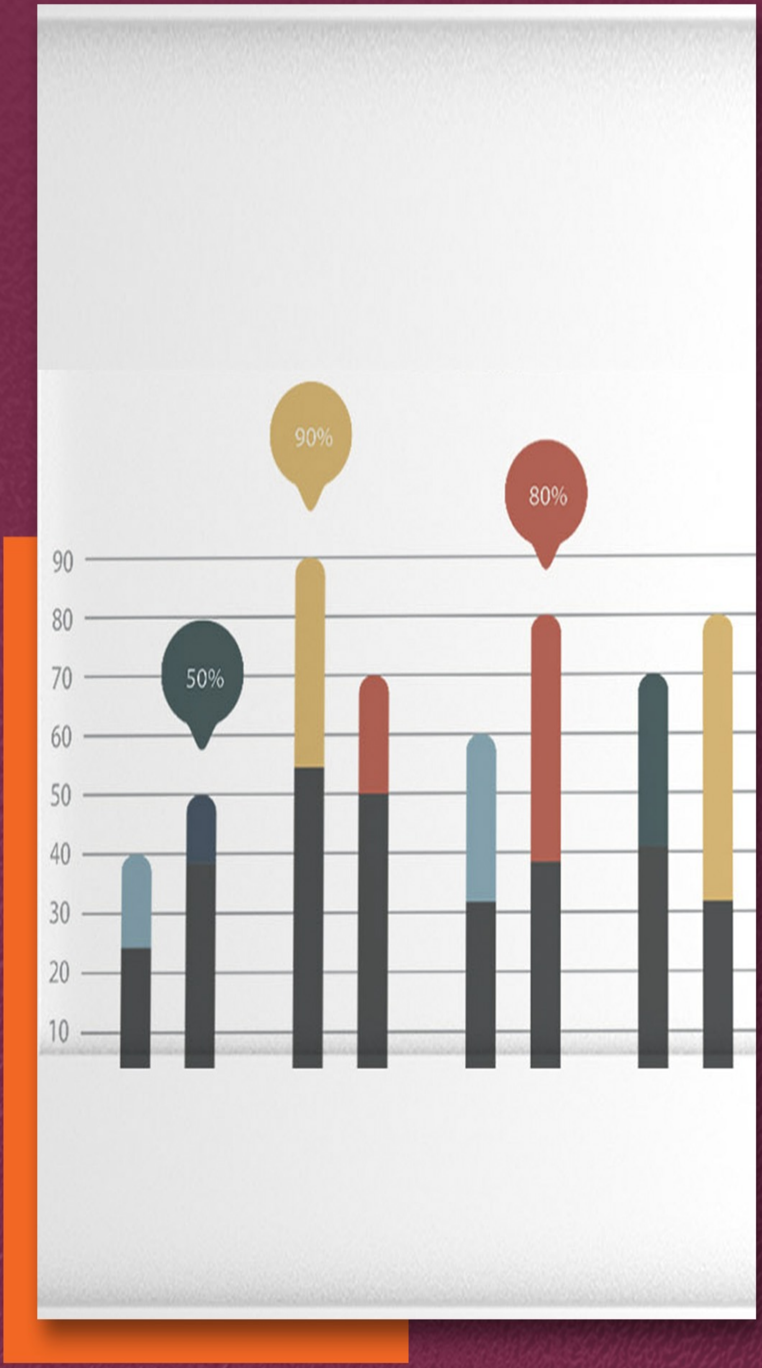


# Primary Auction Guide

# Primary Auction Guide – IFB1/2023/6.5

06th November 2023

**RECOMMENDATIONS:**

IFB1/2023/6.5

Bid: 17.80% - 18.49%

Period of Sale: 20/10/2023 to 08/11/2023

Sovereign Credit Rating:

Moody's: B3 (Negative)

Fitch: B (Negative)

S&P: B (Negative)

October CPI: (2019=100): 136.71

October Inflation: 6.90%

Interbank Rate ( 3rd November 2023): 12.09%

C.B.R (October '2023): 10.50%

The Central Bank of Kenya is in the market looking to raise KES 50.00Bn for budgetary support through the issuance of an amortized infrastructure bond, IFB1/2023/6.5. The coupon rate of the newly issued bond will be market determined with bidding closing on 08th November 2023. The minimum investment is KES 50,000 with an effective tenor of 5.1 years.

We foresee this bond issue will be oversubscribed driven by factors such as;

i. **Tax free nature of the bond -** Infrastructure bonds are tax free in nature hence attractive to investors compared to other government bonds that have a 10%-15% withholding tax.

ii. **Expected high yield -** Yields currently offered on government papers have been on the rise in recent past driven by deteriorating macro factors. Concerns about government debt sustainability and depreciation of the shilling has led to investors seeking higher returns to safeguard their real return. Given the uncertain macroeconomic outlook in Kenya, it is anticipated that yields will continue to edge higher.

iii. **High demand in the secondary market -** Activity in the secondary market is driven by investors who missed out on the primary market auction and hence we anticipate significant interest from investors who will miss out on the primary market. As such, holders of the bond can cash out at a higher price making the paper attractive for the primary market.

The recent low acceptance levels points to the governments need to control yields from rising further. We anticipate the government will reject expensive bids to control yields from rising higher and to remain within the lower domestic borrowing target. Mid-range bidding could position investors within the acceptance zone with the expectation that the government is aiming to stabilize upward movement of the yield curve.

We expect aggressive bidding driven by :

i. **Investors increased preference for higher risk-adjusted returns-** From the performance of recent FXD and T-Bill issues, investors bidding trends have shown a risk vs duration mismatch. The yield on the recent FXD1/2023/005 came in at 17.99% level and we expect investors to bid higher in this issue.

ii. **Debt sustainability concerns -** Growing concerns about the governments' debt sustainability given the current debt burden in the aftermath of downgrading by credit rating agencies has led to investors pursuing higher returns. We expect investors awaken their risk feelers and demand a premium by placing aggressive bids.

## Summary Bidding Guidance:

| Issue No | Amount Offered | Next Coupon Payment | Coupon Rate | Bidding Range |
|---|---|---|---|---|
| IFB1/2023/6.5 | KES 50.00Bn | 13/05/2024 | Market determined | 17.80% -18.49% |

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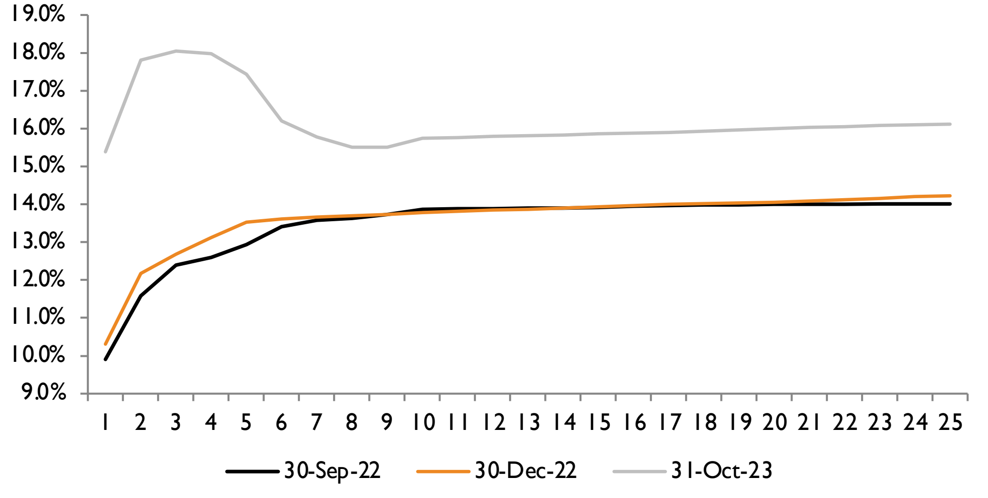
### Liquidity

During the month of October, liquidity in the money markets tightened marginally. Higher liquidity was partly attributable to government spending outpacing statutory deductions and tax remittances. Additionally, we opine the introduction of interbank pricing system has had a favorable impact in the interbank trading. Mostly, interbank rates remained largely above 11.00% levels having recorded **12.52%** on 31st October reflecting a 9bps increase form **12.44%** recorded on 29th September 2023.

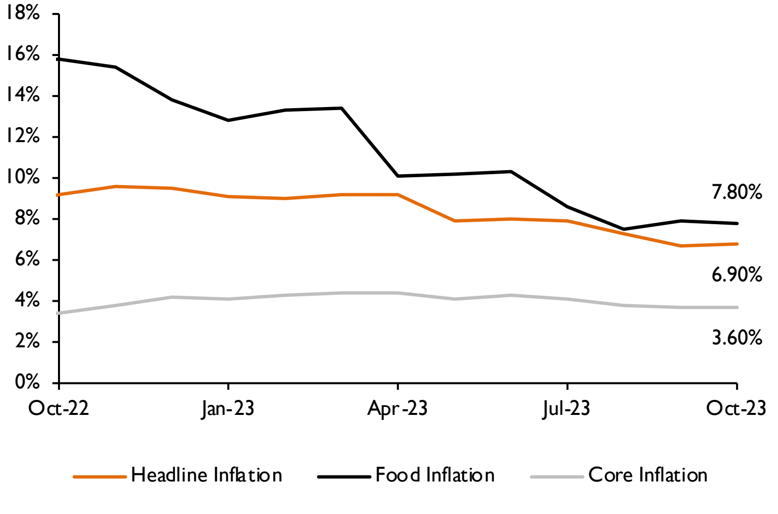
### NSE Implied Yield Curve




In the month of October, there was a mixed yield movement across the curve. We continued to see investors pricing risk on the short end with the 1-year papers increasing the most by 33bps. The 6-year papers lost the most by 60bps.

We expect the yield curve to experience upward pressure across all tenors with a concentration on the shorter end as compensation for prevailing market risks. The yields on the 91-day, 182-day, and 364-day papers closed October at 15.11% (32bps), 15.13% (+19bps), and 15.39% (+17bps) respectively.

### October Inflation




- The headline inflation increased for the month of October to **6.90%** from **6.80%** in September. Inflation remains within CBK'S target range of 2.50%-7.50%. The CPI increased by 103bps to **136.71** from **135.32** in September 2023.
- Meanwhile, the food and non-alcoholic beverages index decreased 10bps to 7.80% y/y in October from 7.90% recorded in September. Housing utilities increased to 7.8% y/y while transport increased to 13.60% y/y.
- We expect headline inflation to remain under pressure but within CBK's upper target in the short-term. We foresee that the CPI will remain under pressure, at least until localized effects of the global oil price decrease, cost of electricity declines, and relief from expected rainfall increases food production.

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