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WEEKLY FIXED INCOME NOTE

research@aib-axysafrica.com

Weekly Fixed Income Note

Week Ending: 19th May 2023

Key Highlights:

- T-bills were oversubscribed for the third week recording a decreased overall subscription rate of 150.09% from 188.91% recorded in the previous week. Investors continued to prefer the shorter-term 91-day paper for the 13th 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 99.85% of the **KES 36.02Bn** amounting to **KES 35.97Bn.** Yields on all the papers are now firmly above 10.00% with the 91, 182, and 364-day papers moving **10.80bps, 12.50bps,** and **12.00bps,** respectively.

- In the primary market, the tap sale of the May FXD1/2023/03 was oversubscribed recording a 106.02% subscription with the CBK accepting KES 10.60Bn. We attribute the overperformance to investors continuing to see the market's short-term risks, hence the high appetite for shorter dates papers.

- In the secondary market, the value of bonds traded increased by 30.72% to **KES 18.21Bn** from **KES 13.93Bn** recorded a week prior. Higher trading was driven by investors who missed out on the recently issued high yielding T-Bond issue. We observed a further yield curve steepening across the curve highlighting investors' demand for higher rates. As such, the 3-year paper gained the most by **29bps.** 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.

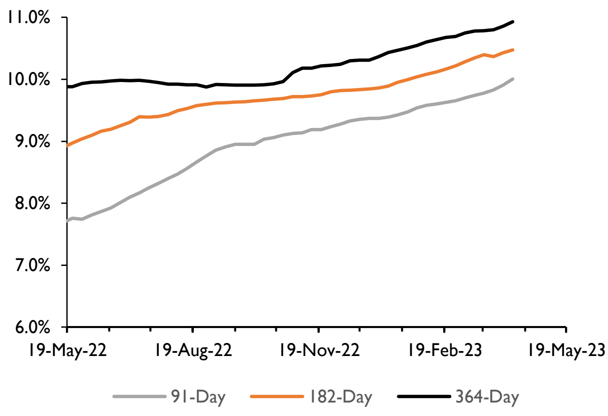
- In the international market, yields on Kenya's Eurobonds decreased by an average of 83bps indicating improved investor sentiment on the long end. We observed the 2024 Eurobond paper decreased by 218bps, highlighting the paper's sensitivity to market sentiments given that its maturity is less than 13 months away. We expect further declines in the 2024 paper following positive domestic subscriptions that could point to improved sentiments. However, the Moody's ratings downgrade could sway yields upwards.

We expect activity in the secondary market to be driven by investors who missed out on the May T-Bond issue. 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.

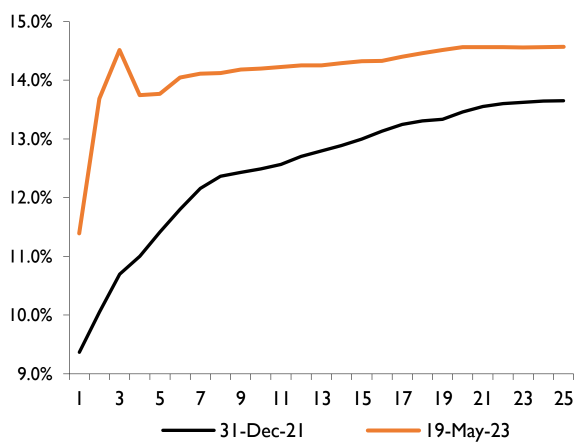
Key Indicators

	Current	Previous	w/w bps Change
91- Day	10.52%	10.41%	10.80
182-Day	10.98%	10.85%	12.50
364-Day	11.39%	11.27%	12.00
Interbank Rate	9.25%	9.50%	24.68

T-Bill Rates



NSE Implied Yield Curve



MACROECONOMIC NEWS

Currency

The Kenya shilling further lost ground against the USD, depreciating **45bps** to **KES 137.49** from **KES 136.88** the previous week. On a YTD basis, the shilling has depreciated **11.48%** 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 6,297Mn** (**3.50 Months** of Import Cover), a 264bps week-on-week decrease from **USD 6,468Mn** (**3.60 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 eased as shown by the average interbank rate decreasing 25bps to 9.25% from 9.50% recorded a week prior. We partly attribute the easing to government payments outpacing statutory deductions and tax remittances. **We expect the interbank rate to remain above 9.00% levels in the coming week, mainly driven by the remittance monthly obligations, delayed government payments and CBK's open market operations.**

Macro-economic News Roundup

In the international front, the US dollar strengthened 0.49%, against other major currencies during the week taking the YTD performance to -0.33%. We attribute this to the Federal Reserve's aggressive monetary policy stance by raising interest rates to combat the high inflation with anticipation that the Federal Reserve could hike interest rates once more in June. Following the release of GDP figures and expectations for a debts ceiling increment agreement, the yield on the 10-year treasury paper climbed further. Similarly, yields of short-term paper rates have been increasing indicating growing optimism about the US economy. Kenya's supplier UAE Murban increased closing the week at USD 75.58/barrel while Brent Crude oil price increased closing the week at USD 77.22/barrel.

We expect the shilling to come under more pressure as the dollar gains strength which will lead to the widening of the current account deficit as import costs rise. We anticipate that the rise in interest rates in developed markets will accelerate the current withdrawal of foreign investors from developing countries like Kenya, which will keep the shilling under pressure. With Murban crude prices increasing at last week's close, we expect local pump costs to continue to be impacted by worldwide prices which will continue to put pressure on headline inflation. As earlier highlighted, we do not foresee any local pump pricing benefits for consumers from the new oil import method as the inventory settlement currency remains as the dollar. In our view, lower pump prices can only be achieved by a reduction in landing costs and lower taxes/levies on fuels.

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.

	Macro event	Date
1.	Weekly T-Bills Auction	25th May 2023
2.	May MPC Meeting	29th May 2023
3.	May Inflation Figures	31st May 2023

CONTACTS:

Research Desk

Solomon Kariuki
Research Analyst

Stacy Makau
Research Analyst

Email: research@aib-axysafrica.com

Equities Dealing

Nina Goswami

Bernard Kung'u

Benard Gichuru

Brian Tanui

Samuel Githinji

Sheema Shah

Samuel Wachira

Benson Ngugi

Email: trading@aib-axysafrica.com

Bond Dealing

Crispus Otieno

Titus Marenye

Aundrina Musyoka

Kenneth Minjire

Email: trading@aib-axysafrica.com

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