Kingdom Securities Limited

Pre-Auction Fixed Income Note – May 2021

A Call for Debt Restructure

Re-open FXD2/2019/15Yr – 12.734% Coupon - 13 Years

New FXD1/2021/25Yr – Market Determined Coupon - 25 Years

May 3, 2021

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KINGDOM SECURITIES

Fixed Income Pre-Auction Note

May 2021

The government issued two bonds for a total of KES 30Bn by reopening FXD2/2019/15Yr with a coupon of 12.734% and a new bond FXD1/2021/25Yr market determined.

This is the fourth issue of the FXD2/2019/15Yr. It was first issued on May 2019 with subscription of KES 21.54Bn and KES 19.32BN accepted. The bond was reopened on September of the same year receiving KES 17.37Bn and 100% acceptance. The third offer was December 2020 with KES 22.51Bn received and 17.10Bn (76.0%) accepted.

We forecast an under subscription on the two bonds on low interest on the tenure of the bonds. Investors have seen to shun long term bonds preferring short term papers while the FXD2/2019/15Yr continues to see low appetite even in the secondary market.

Below is our bidding guidance:

Bond	FXD2/2019/15Yr	FXD1/2021/25Yr
Tenure	13 years	25 years
Coupon	12.734%	MDA
Conservative Bid	**12.75% - 12.95%**	**13.50% - 13.70%**
Aggressive Bid	**13.00% - 13.25%**	**13.80% - 14.10%**

Table1: Bidding Guidance **Source: CBK, KSL**

Central Bank: The next meeting of the Monetary Policy Committee (MPC) will be held on Wednesday, May 26, 2021.

Fiscal Budget 2021-2022: Treasury Secretary submitted a KES 3.64Tr budget to parliament. The focus will be on restructuring country's external debt to reduce cost and lengthen tenure. Below is the summary. Read our Budget analysis for additional information.

Fiscal Framework KES Bn	2020/21		2021/22	2020/21 vs 2021/22	2021/22 Budget to Nominal GDP	Final Budget to Nominal GDP
	Budget	Final Budget	Budget			
Total Revenue	**1,892.6**	**1,848.0**	**2,038.6**	**10.3%**	**16.5%**	**15.2%**
Ordinary Revenues	1,633.8	1,594.0	1,775.6	11.4%	14.3%	13.3%
Expenditure and Net Lending	**2,790.6**	**2,892.0**	**3,053.5**	**5.6%**	**25.9%**	**22.8%**
Recurrent Expenditure	1,826.7	1,853.1	2,019.2	9.0%	16.6%	15.1%
Development and Net Lending	589.7	653.0	619.5	-5.1%	5.8%	4.6%
County Transfer	362.2	398.9	409.8	2.7%	3.6%	3.1%
Fiscal Deficit exc Grants	**(898.0)**	**(1,044.0)**	**(1,014.9)**	**-2.8%**	**-9.3%**	**-7.6%**
Fiscal Deficit incl Grants	**(841.1)**	**(970.9)**	**(952.9)**	**-1.9%**	**-8.7%**	**-7.1%**
Net Foreign Financing	346.8	427.0	291.3	-31.8%	3.8%	2.2%
Net Domestic Financing	494.30	543.90	661.60	21.6%	4.9%	4.9%
Nominal GDP	**11,275.8**	**11,168.5**	**13,393.1**	**19.9%**		
Fiscal Deficit	7.5%	8.7%	7.1%			

Table2: Fiscal Framework **Source: Treasury, KSL**

KINGDOM SECURITIES

Fixed Income Pre-Auction Note

May 2021

CPI and Inflation: April inflation overshot our upper range focus of 5.60% to 5.76%. this was 14bps lower compared to 5.90% March inflation. The decline was caused by a Food and Non-Alcoholic Beverages and transport index to 2.11% and 1.66% while non-core inflation increased to 1.99% from 1.96%. The rate was higher compared to our upper range prediction of 5.6%.

With rainfall underperforming and the reprieve on pump prices viewed as a one off, we forecast May inflation to range 5.66% - 6.08%. Our view assumes that petroleum regulator will not retain prices on the same levels forcing an upward pricing and with cessation of movement coming to an end, demand will increase. Food index will be affected by pressure on lagged maturity impairing harvest.

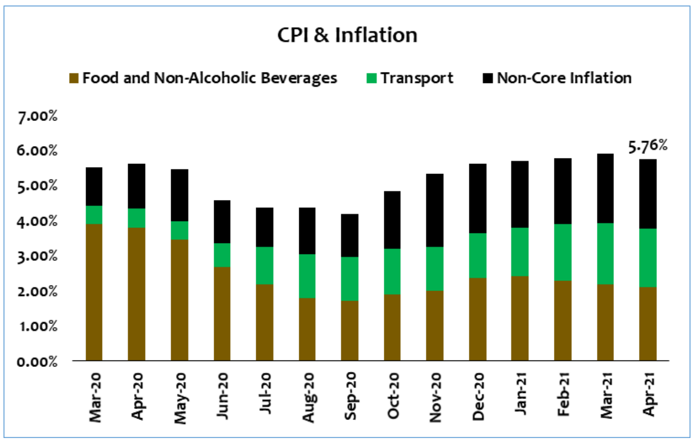

Figure 1: CPI and Inflation Source: KNBS, KSL

Interbank Rate: April average interbank rage was 5.14%, 8.2bps lower compare to March average of 5.22%. demand was lower at KES 10.56Bn against 13.02Bn over the period.

Mid-month had tight liquidity which pushed the rate to a high of 5.771%. improved market environment saw the rate close the month at 4.8289% (March 31st – 5.5484%) with bank reserves increasing to close at KES 13.0Bn above the regulatory requirement.

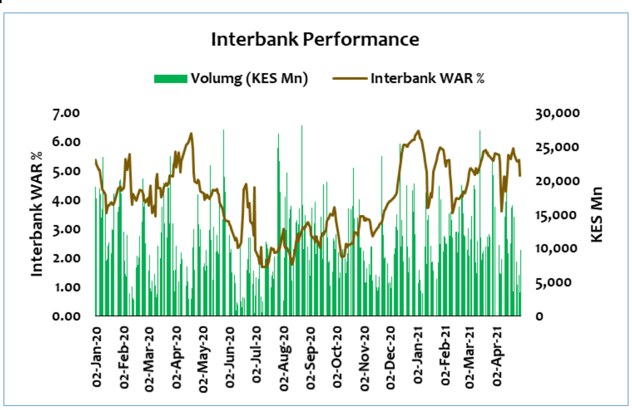

Figure 2: Interbank Rates and Volumes Source: CBK, KSL

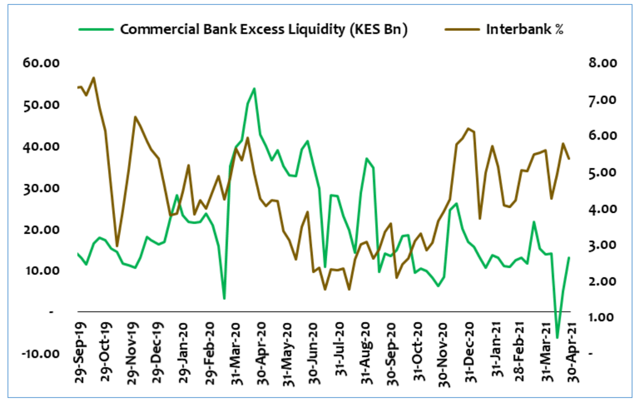

Figure 3: Interbank Rates and Commercial Bank Excess Liquidity Source: CBK, KSL

Treasury Bills: T-Bill auction received KES 62.78Bn, a 65.4% acceptance on an offer of KES 96Bn. This was lower to KES 139.64Bn (116.4% subscription). Acceptance levels improved to KES 58.90Bn, 93.8% compared to 87.2% in March.

Tenure	Offer (KES Bn)	Subscription	Acceptance	WAR % 03-May-21
364-Day	**40.00**	102.0%	90.9%	9.474%
182-Day	**40.00**	22.5%	98.5%	7.989%
91-Day	**16.00**	81.1%	99.7%	6.897%
Total	**96.00**	65.4%	93.8%	

Table 3: Monthly T-Bill Performance Source: CBK, KSL

Performance was due dependency on reinvestments which stood at KES 73.24Bn which was lower than the borrowing target of KES 96Bn coupled by high demand from the issue infrastructure bond.

Subscriptions was skewed towards the 364-day paper with a 108.0% performance. Yield on the paper stood at 9.474% which was lower compared to out target of 9.635% - 6.660%. Yield on the paper has increased faster compared to the peers with the range widening to 233.5bps compared to the 91-day paper from 144.2bps at the beginning of the year.

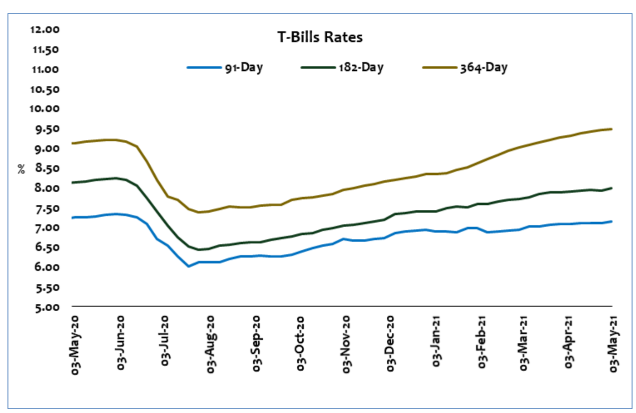

Figure 4: T-Bills Rates Source: CBK, KSL

KINGDOM SECURITIES

Fixed Income Pre-Auction Note

May 2021

The month of May, the government expect to borrow KES 96.0Bn. maturities stands at KES 95.37Bn with KES 73.82Bn on 364-day paper. We foresee average subscription with acceptance remaining >90% with government targeting to maintain low borrowing profile as we had towards the end of the fiscal year.

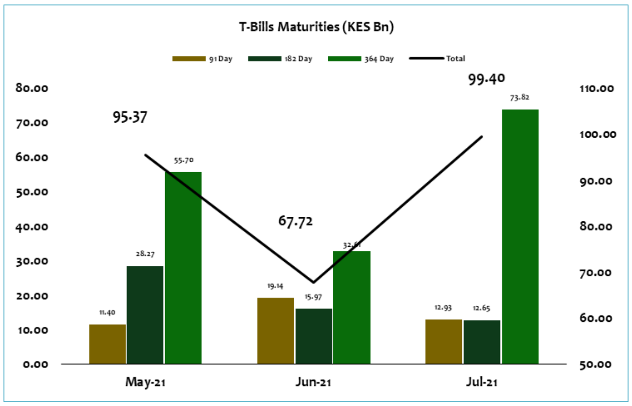

Figure 5: T-Bills Maturities Source: CBK, KSL

We advise or client to maintain investment on the 364-day paper with a range of 9.625% - 9.675%. Our forecast is based on the upcoming maturities with investors opting to reinvest while the government cost management plan which has seen rejection of expensive cash.

Treasury Bonds: April primary saw government issue KES 60Bn 18-year infrastructure bond. The bond received KES 88.58Bn (147.6% performance) while it accepted KES 81.94Bn for a 92.5% acceptance levels. This was in-line with our prediction on heavy interest from foreign investors.

Secondary Bonds Market: In the month of April, secondary bond market saw 1.8% improve in value traded to KES 65.65Bn from KES 64.51Bn in March. This was despite deals increasing by 226%. The performance was boosted by last minute traded before close of the month.

Trade focused on the issued 18-year infrastructure bond which managed 35.6% of total monthly traded with y-t-m shifting 57.9bps lower to an average of 12.083%.

May will see a coupon payment of KES 28.75Bn with payment spread evenly through the month. Heavy payout is expected in the month of July with a total of KES 54.95Bn expected from KES 30.56Bn in coupons and KES 24.40Bn in maturities.

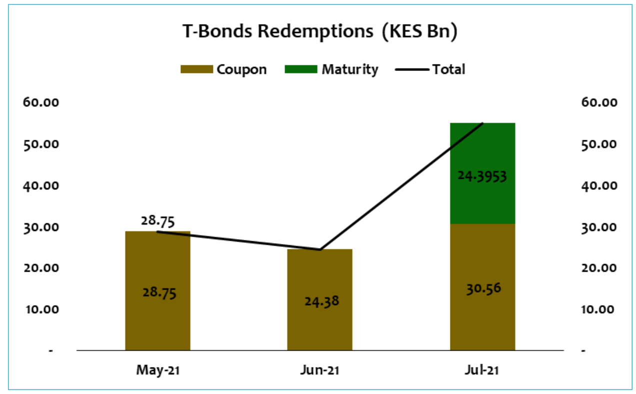

Figure 6: T-Bonds Maturities Source: CBK, KSL

Yield Curve: The demand for on-the-run bond left long end of the yield curve stable with the short end shifting upwards. We expect activity to remain on the short end with the long end remaining stable on little activities on that front.

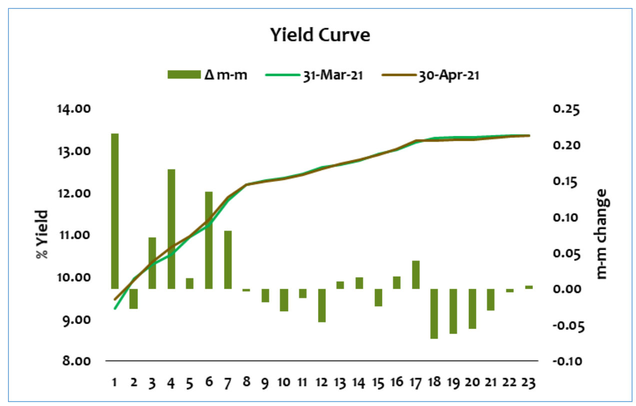

Figure 7: Yield Curve Source: NSE, KSL

Total Public Debt: Total government debt stood at KES 7,339.71Bn with KES 3,569.84Bn (48.3%) in domestic debt and KES 3,769.87Bn in Public & Publicly Guaranteed External debt 34.74.

As end nf march, domestic borrowing stood at KES 640.39Bn, 75.9% of revised target 853.85Bn for the fiscal year.

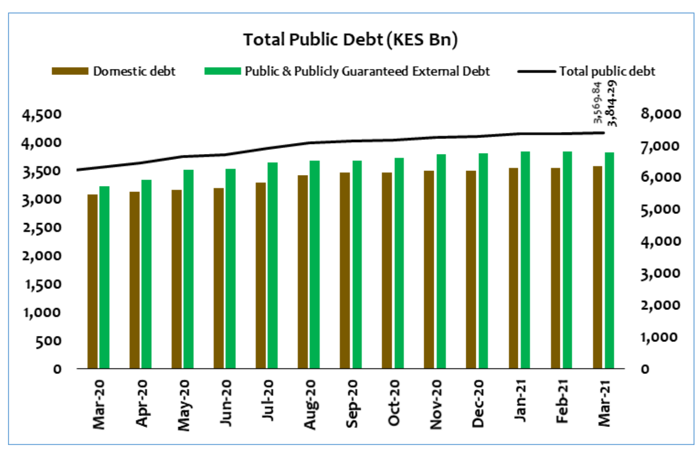

Figure 8: Total Public Debt Source: CBK, KSL

KINGDOM SECURITIES

Fixed Income Pre-Auction Note

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