Kingdom Securities Limited

Pre-Auction Fixed Income Note – December 2021

November – 2021

December – 2021

January - 2022

Re-open FXD4/2019/10Yr – Coupon 12.28% - Term 8.0 Years

Re-open FXD1/2018/20Yr - Coupon 13.30% - Term 16.4 Years

December 6, 2021

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KINGDOM SECURITIES

Fixed Income Pre-Auction Note

December 2021

December Bonds Primary Issue: Reopened FXD4/2019/10 and FXD1/2018/20 for KES 40.00Bn

For December, treasury opted to reopen FXD4/2019/10 and FXD1/2018/20 for KES 40.00Bn for budgetary support. The two bonds have not been much in the investors focus as FXD4/2019/10 has traded KES 13.99Bn or 1.8% of total trades y-t-d while FXD1/2018/20 has moved KES 7.06Bn or 0.8% on total turnover over the same period.

Overall market has been affected by low liquidity leading to an upward shift on the short end while a stale mate in the secondary market where supply is not matched by demand has forced a downward shift on the long end.

We expect low reception on the two bonds with clients preferring the FXD4/2019/10 due to the duration and activity levels on the two papers. Acceptance rate to remain >85%.

Below is our bidding guidance.

Bond	FXD4/2019/10	FXD1/2018/20
Tenure	8.0 year	16.4 years
Coupon	12.28%	13.20%
Issued	**Nov-19**	**Mar-18**
Conservative Bid	**12.50% - 12.75%**	**13.00% - 13.25%**
Aggressive Bid	**12.85% - 12.95%**	**13.30% - 13.50%**

Table 1: Bidding Guidance Source: CBK, KSL

CBK

The general bonds market remains as with CBK MPC retaining the central bank rate (CBR) at 7.0% stating a stable macroeconomic environment.

We forecast MPC to retain the CBR at 7.0% during the next sitting due to due to:

- **Inflation expected to remain within the government range of 5.0±2.5% boosted by stable food prices, mild or non-movement on local petroleum pump prices. November inflation eased to 5.8% from 6.45% in October 2021.**
- **Banking sector to remain stable with adequate liquidity. The industry saw positive profit trajectory Q3-21 on declining provisions which led to CBK relaxing dividend pay-out restrictions imposed in 2020. We expect private credit growth to remain at an average of 7.7% while NPL to average 13.9% for the remaining of the fiscal year.**
- **Growing economic output led by growth in exports. October current account deficit stood at 5.4% compared to 4.8% in October 2020 and 5.6% in September. The CBK governor forecasted the Kenyan economy to recover at a faster rate of 6.4% in 2021 compared to government projection of 6.2%. The Purchasing Managers' Index (PMI) has remained above 50.0 for six months running. This is a positive indicator for the economic performance.**
- **At the beginning of December, Forex reserves stood at USD 8,737Mn or 5.34 months of import cover which is above 4.0 months of import cover. This is expected to thin further with the payment of USD 100.25Mn in Eurobond interest due this December. This will put further pressure on the local currency which has shed 3.1% y-t-d and 1.8% y-y against the USD.**
- **International economies to slowdown in December on uncertainty of Omicron Covid-19 variant on the global economy. We expect the economies to adjust fast compared to recovery on the delta variant.**

Inflation:

- The inflation eased to 5.8% in November, 65bps from 6.45% as CPI increased by 0.45% to 117.20. the rate declined on lower vegetable prices and stable petroleum prices which led to decline on cost of public transport.
- We expect December inflation to inch further downward on lower base to range 5.20% to 5.60%. Pressure will come from;
  1. higher food prices due to holiday season demand and
  2. higher public transport as Kenyans travel upcountry the same time as school closure for December break.
- On November 26th, 2021, international oil futures prices plunged by 11.6% and 12.0% to USD 72.72 pb and USD 68.15pb from USD 82.22pb and 77.41pb on the Brent and WTI respectively after the detection of the first Omicron Covid-19 variant. This is due to the anticipated negative effect of the variant which has continued to spread globally thus affecting petroleum demand.
- Opec+ opted to leave output unchanged in their December meeting with the aim price recovery. America, China and India announced to release oil from their strategic reserves to contain prices downward.

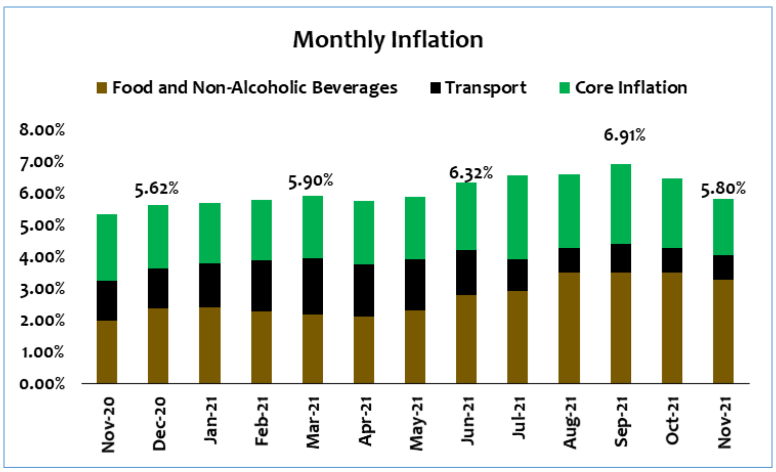

Figure 1: Kenya Inflation Source: KNBS, KSL

Interbank Rate

Tight liquidity continues to put pressure on the intrabank rate with bank reserves remaining stable with November interbank rate easing by 29bps to 4.97% from 5.26% in October 2021.

We expect the tightness to remain for the rest of the year as with the rate averaging 5.0% for December on low maturities due to;

1. high demand especially for small banks while
2. CBK will is expected to be in the market to mope up any excess liquidity with the aim of stabilizing the shilling.

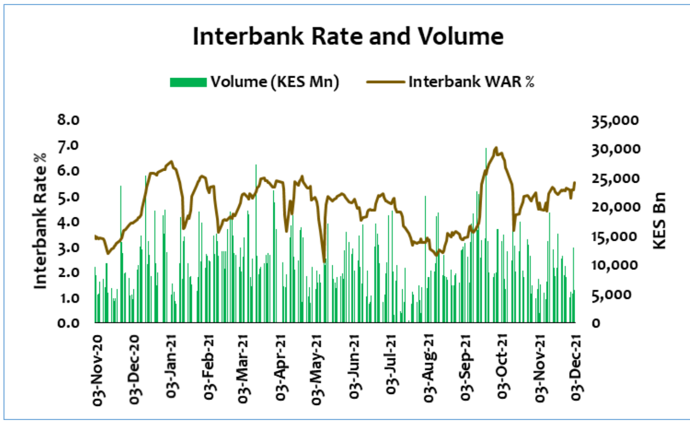

Figure 2: Interbank rate and Volumes Source: CBK, KSL

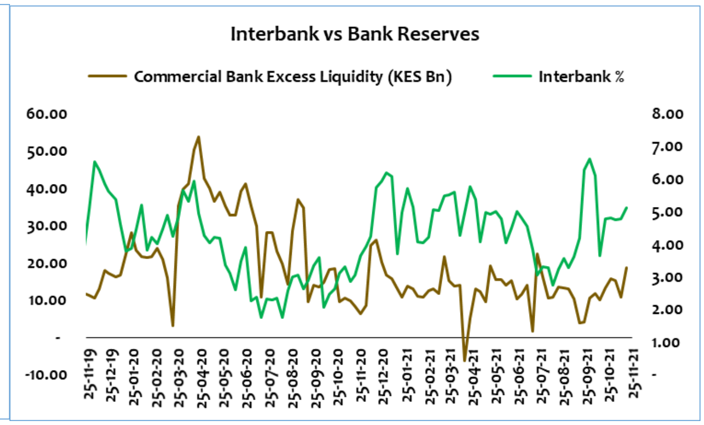

Figure 2: Interbank rate and Bank Reserves Source: CBK, KSL

Currency

- Kenya shilling has shed 3.1% y-t-d and 1.8% y-y on the dollar as of December 3rd, 2021. The local currency has weakened by 0.6% y-t-d and 1.4% on y-y against the British pound but strengthened by 4.9% and 5.6% y-t-d and 4.3% and 5.5% against the Euro and Japanese yen respectively.

3-Dec-21	KES/USD	KES/GBP	KES/EUR	KES/JPY	Dollar Index
W/W	0.2%	0.0%	0.7%	1.2%	0.1%
M-t-D	0.1%	0.1%	0.0%	0.3%	0.2%
M/M	1.1%	1.4%	1.2%	1.9%	2.5%
Y-t-D	3.1%	0.6%	4.9%	5.6%	7.1%
Y/Y	1.8%	1.4%	4.3%	5.5%	6.1%

Table 2: Currency Source: CBK, KSL

- Forex reserves have declined by 4.4% at the end of November to USD 8,773Mn from USD 9,175Mn on;
  - i. Payment of c.USD 80.0Mn interest on Eurobond 2027 and 2032 that was duet on the third week of November.
  - ii. Regulator continues participate in the enter the market to mop liquidity with the aim of containing the weakening shilling.
- International level the dollar continued to strengthen against other major currencies shrugging off weak unemployment data as unemployment eased to 4.2% while the US economy seem to have recovered by up to 80% and the anticipation of a fed reserve rate hike. Dollar index gained by 7.1% y-t-d and 6.1% y-y.
- A weakening economy and a pushed back interest rate hike expectation left the British pound weak while the news of the new Covid-19 variant is not encouraging to the overall Europe economy.

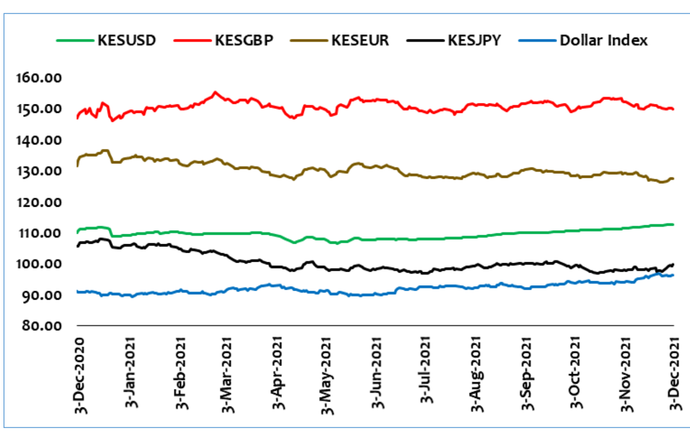

Figure 4: Currency Movement Source: CBK, KSL

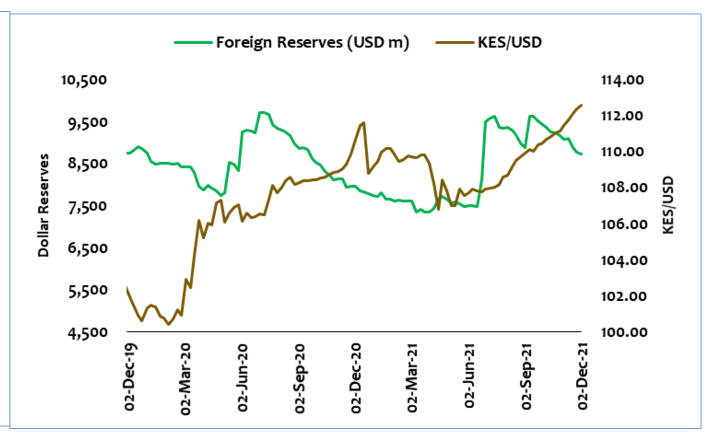

Figure 5: Dollar Reserves Source: CBK, KSL

- We expect the shilling to continue to remain under pressure on dwindling foreign reserves and expected interest payment of USD 100.25Mn on th e2024 and 2034 Eurobonds

Treasury Bills

- T-Bill performance improved but remained undersubscribed in November at 87.9% with acceptance at 93.1% compared to 57.9% in subscription and 93.7% acceptance seen in October 2021.

November-2021						
Tenure	**Offer (KES Bn)**	**Subscription**	**Acceptance**	**WAR % 25/10/21**	**WAR % 29/10/21**	**Δbps M-M**
364-Day	**50,000**	101.4%	93.1%	8.355%	8.944%	58.9
182-Day	**50,000**	64.8%	88.1%	7.417%	7.835%	41.8
91-Day	**20,000**	112.0%	100.0%	7.020%	7.181%	16.1
Total	**120,000**	87.9%	93.0%			

Table 3: November 2021 T-Bills Performance Source: CBK, KSL

- Reinvestments remains key liquidity provider in the T-bill market as subscriptions demand shifting to the 364-day paper due to better returns as the paper saw a 58.9bps upward jump on return while the 182-day and 91-day papers advancing by 41.8bops and 16.1 bps respectively.

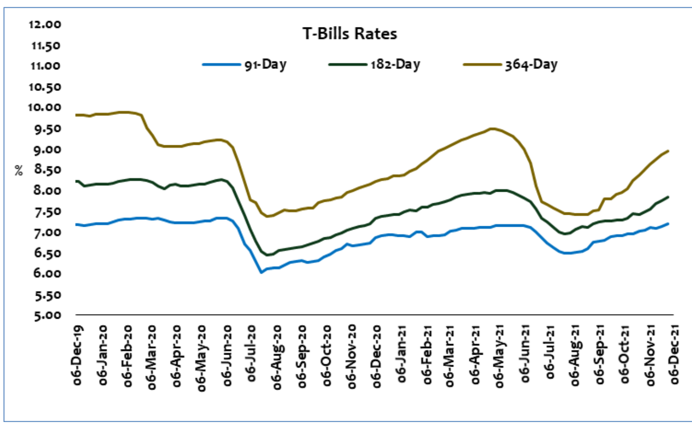

Figure 6: T-Bills Returns Source: CBK, KSL

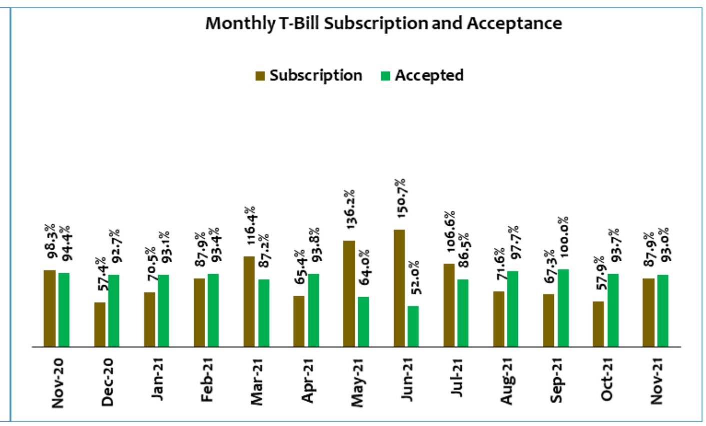

Figure 7: T-Bills Subscriptions Source: CBK, KSL

- We expect an undersubscription for the month with KES 66.59Bn expected in redemptions compared to a target of KES 120.00Bn for the month.
- Focus will remain on the 364-day with acceptance on the paper remaining high.

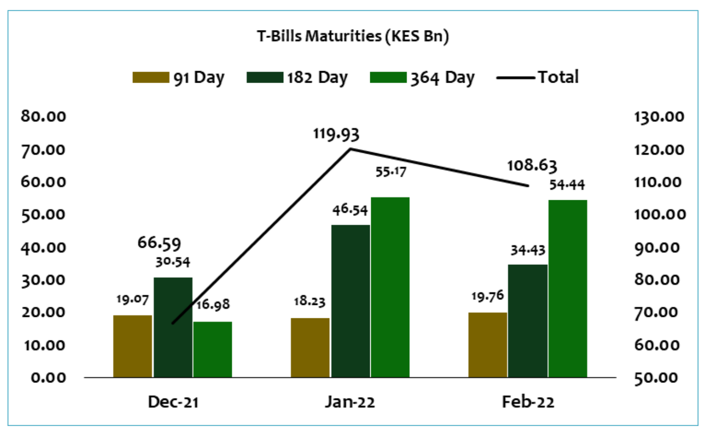

Figure 8: T-Bills Maturities Source: CBK, KSL

Treasury Bonds

- November saw a subscription of 168.3% buoyed by a 133.2% subscription on the FXD1/2021/5Yr bond, an indication of how thirsty the market was for a new short-term paper.
- Government demand for funds continues to be reflected on the high acceptance to offer rate of 139.0% in the month of November 2021.
- Secondary market retained a quagmire stance with the short end the monthly yield curve shifting upwards due to tight liquidity while long end shifted downward as supply overshot demand as indicated by figure 10.

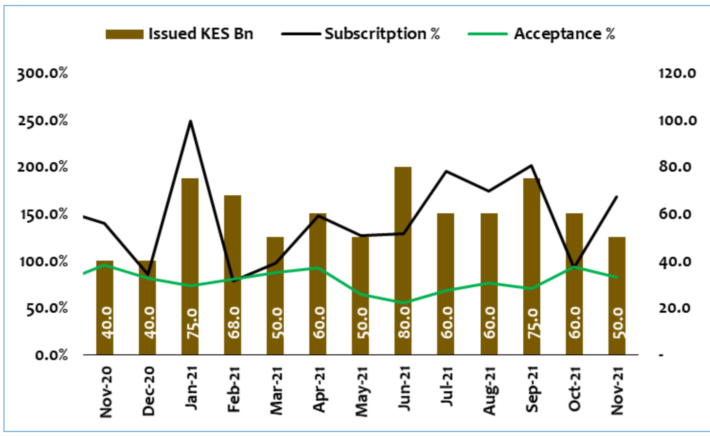

Figure 9: T-Bills Bonds Primary Issue Source: CBK, KSL

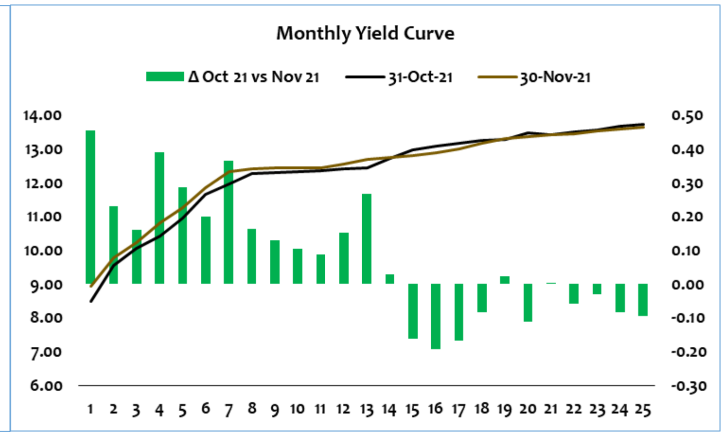

Figure 10: Yield Curve Source: KSL, NSE

- In December we expect KES 24.38Bn in coupons payment in the month with over 50% payment coming in on the third week of the month.
- We expect low subscription on the December issue due to
  i. low market interest on the two papers FXD4/2019/10 has traded KES 13.99Bn or 1.8% of total trades y-t-d while FXD1/2018/20 has moved KES 7.06Bn or 0.8% on total turnover over the same period.
  ii. tight liquidity in the market.

Eurobond

- Kenyan Eurobond Yields saw an upward shift on
  i. November due interest payment date on the Euro bond 2027 and 2032
  ii. the news of the Omicron Covid-19 variant and
  iii. the yields edged further upwards on as growing countries placed flight bans on several southern African nations due to concerns over the new variant.
- The yields have been on the downward shift as additional information with regards to the stain come to the market.
- We expect the rate to shift downwards further towards the end of the year.

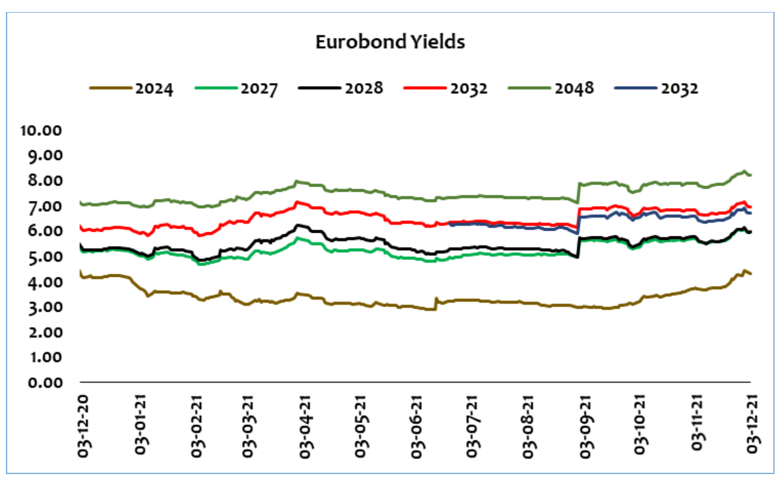

Figure 11: Eurobond Yields Source: KSL, Bloomberg

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