Kingdom Securities Limited

Pre-Auction Fixed Income Note – August 2022

Total Issue KES 70.00Bn

New – IFB1/2022/18Yr – Coupon – MDA – Term 18 Years

August 15, 2022

Research Analyst:
Willis Nalwenge, CFA
wnalwenge@co-opbank.co.ke
Office: +254 711 049 183

Research Analyst:
Shadrack Manyinsa
smanyinsa@co-opbank.co.ke
Office: +254 711 049 956

Bond Dealer
Ashley Odundo
aodundo@co-opbank.co.ke
+254 711 049 195

Bond Dealer
Asena Moffat
amoffat@co-opbank.co.ke
+254 711 049 663

Primary Bond Issue – KES 50.00Bn

The CBK is in the market seeking KES 50.00Bn with three reopened bonds, short, mid, and long-term bonds. The regulator continues with yield management strategy while seeking quick financing on the short-term issues.

In July, the market responded on a wait to see on the general elections, midst a tight liquidity environment. Interbank was +5.0% the whole month with high demand. T-Bills were undersubscribed with investors tactical strategy focusing on 91-day paper, Central Bank has changed tact from use of TADs to reverse repos to manage the liquidity.

CBK need for funds will see aggressive bids cut off while need for liquidity will see high subscriptions and acceptance on the short-term bond. Key rates favor government cut on yields accepted with interbank stable despite the tight liquidity environment. Yield curve has remained stable month on month an indication that the market does not expect high payout gains on the primary issue.

Bond	FXD1/2022/03Yr	FXD2/2019/10Yr	FXD1/2021/20Yr
Tenure	2.7 Years	6.7 Years	19.1 Years
Coupon	11.766%	12.300%	13.444%
Period of Sale		29-July 2022 to 16th Aug 2022	
Value Date		22nd August 2022	
Conservative	11.850% - 11.950%	13.400% - 13.550%	13.550% - 13.850%
Aggressive	12.000% - 12.15%	13.600% - 13.750%	13.900% - 14.125%

Table 1: Bidding Guidance   Source: KSL, CBK

On overall, we forecast 90% - 100% subscriptions supported by upcoming KES 70.94Bn in August payout.

The FXD1/2022/03Yr was issued in April 2022 with 85.1% performance levels. Despite being a short-term bond, it has traded only 11.1% of volume issued. The bond is trading at marginal discounted levels. We forecast heavy interest on the paper tenure and government need for liquidity therefore sacrifice on the yields.

The FXD2/2019/10Yr was issued in April 2019 and this is the first reopening. The bond has traded only 0.2% y-t-d and is about 122bps discounted. The issuer is banking on the attractive tenure, low holdings compared to its peers with nearly same tenure and while giving investors short-mid tenure paper to reinvest the maturities of the FXD1/2017/05Yr maturing on 22nd August 2022. On the contrary, current yields, does not give government much space on uptake. We advise investors to go slow on the paper.

The long paper of FXD1/2021/20Yr will be attractive for investing upcoming coupons by insurance companies. The bond was issued in August 2021 and reopened in January 2022 with good reception. The paper will attract investors who focus on income as it offers better coupon compared to its tenure peers. We do not anticipate heavy investments due to the tenure.

Inflation

Inflation stood at 8.3% in July pushed up by a rise in food and non-alcoholic beverages.

Season weather forecast for June, July, and August indicate adequate rain for the short rainy season. August is projected to have slightly enhanced rainfall pounding the key agricultural areas. This will benefit food prices in the month of September and October.

Energy and Petroleum Regulatory Authority (EPRA) retained the petroleum pump prices flat which will play a large factor in containing inflation levels.

We forecast August inflation to range 8.46% - 8.62% with pressure from food index and transport index influenced by demand from need to travel during the election period.

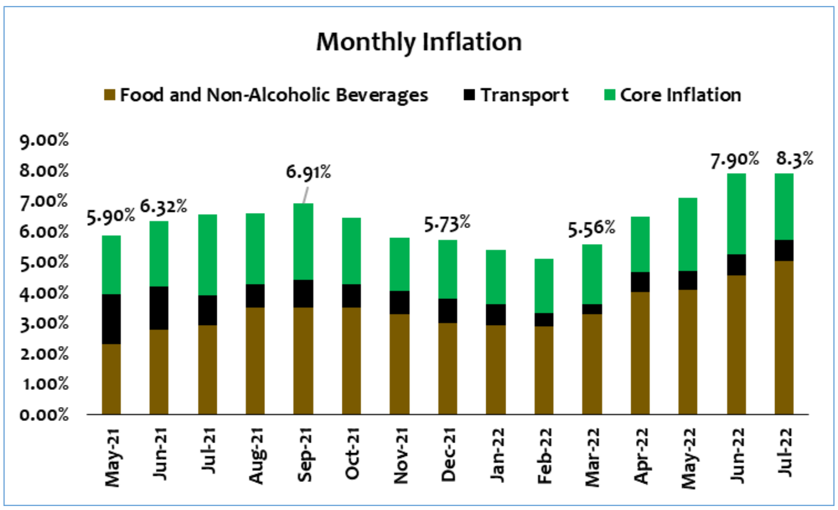


Figure 1: Bidding Guidance Source: KSL, KNBS

Interbank Rate

Interbank rate has remained above 5.0% since mid-June, standing at 5.6969% on August 12th. To manage liquidity, CBK changed liquidity management tactic from TADs to use of reverse repos.

Commercial bank reserves were at a 4-week average of KES 27.55Bn, with the funds remaining short-term that cannot be deployed for long term investments.

We forecast the rate to remain above 5.0% in the month of August as liquidity remains tight especially tier 2 and tier 3 banks.

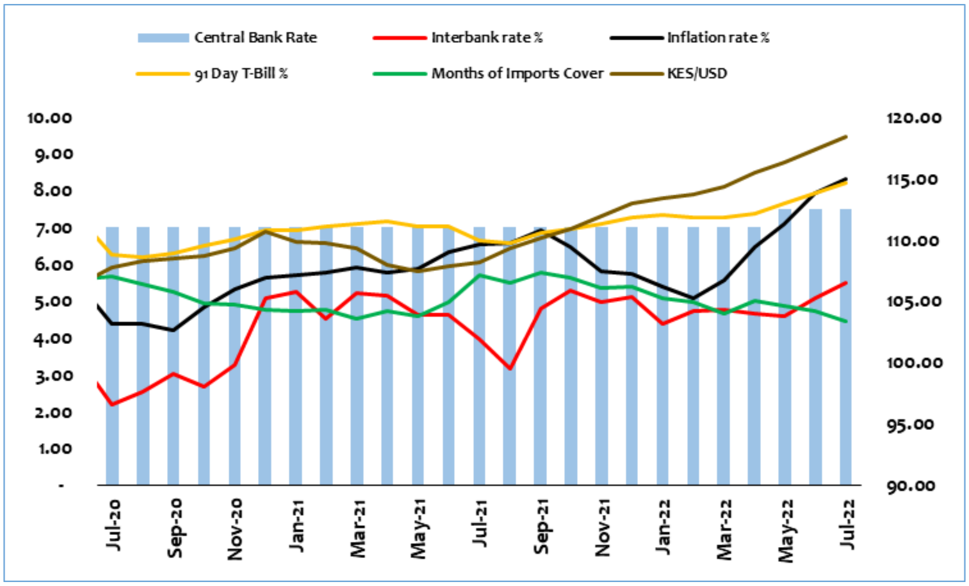


Figure 2: Key CBK Rates Source: KSL, CBK

Currency

The shilling lost 1.0% m-m against the US dollar. During the period, the local currency plunged 2.7%, 2.5% and 4.2% against the British Pound, Euro, and Japanese Yen respectively. Commercial banks retained a c.9.0% premium on the CBK rate.

The duel between government debt payment and traders demands has put pressure on the country's forex reserves which dipped to USD 7,682Mn or 4.43 months of import cover. The rate is higher than CBK target of 4.0 months of import cover but was lower to the East Africa Community (EAC) required target of 4.5 months of import cover.

The low levels have left the shilling more exposed on external shock with the levels due to dip further with USD 77.50Mn due on the 2028 and 2048 Eurobonds on last week of August.

KES	KES/USD	KES/GBP	KES/EUR	KES/JPY	Dollar Index
12-Aug-22	119.3118	145.4203	122.8929	89.6373	105.5500
W/W	0.2%	0.6%	1.3%	0.4%	-0.9%
M-t-D	0.4%	0.7%	1.4%	1.1%	0.2%
M/M	1.0%	2.7%	2.5%	4.2%	-2.2%
Y-t-D	5.5%	-4.5%	-4.1%	-8.7%	9.7%
Y/Y	9.3%	-3.8%	-4.0%	-9.3%	13.4%

Table 2: Bidding Guidance Source: KSL, CBK

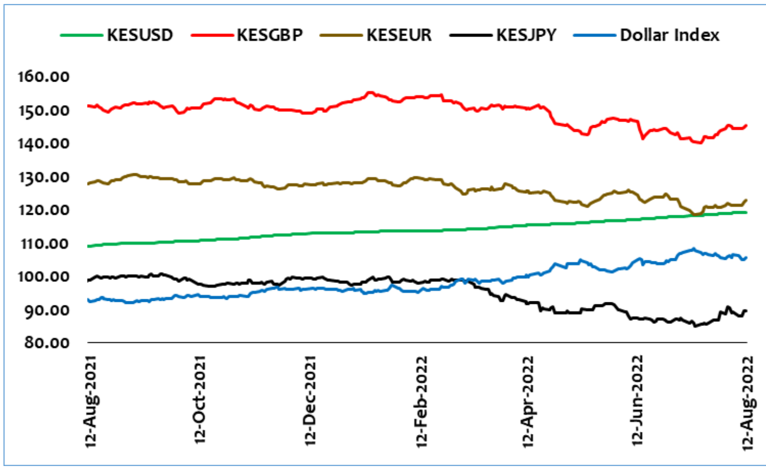


Figure 3: Currency Movement Source: KSL, CBK

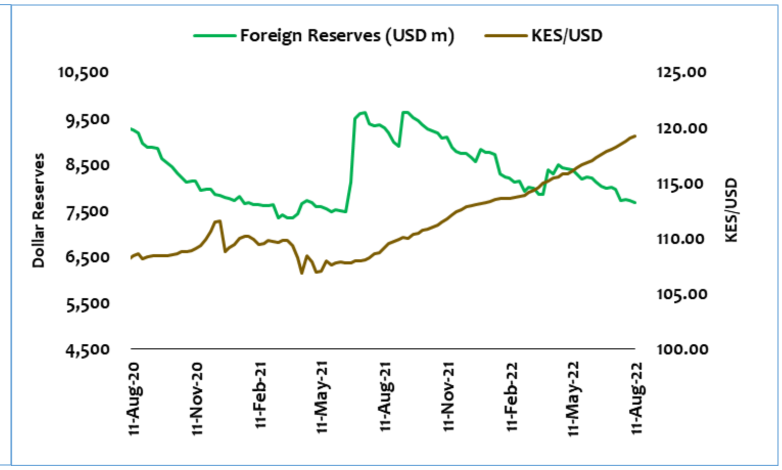


Figure 4: Currency Movement Source: KSL, CBK

Global News

The US July inflation was at 8.5% y-y and remained flat m-m compared to a projection of 8.7%. Inflation rate is seen to slowdown and has stemmed the likelihood of aggressive rate hike by Fed Reserve in September which is further supported by declining international oil prices which has aided stem inflation.

Trader's view on the stance, the Fed Reserve might take lead to US yields shifting downwards. Analyst view that with inflation cooling off, strong consumer confidence and strong employment levels could lift economic numbers.

International petroleum prices declined by 1.0% m-m as of 12th August 2022. The prices continue to favor consumers due to uncertainty on demand and supply. Global fear of raising inflation and rate hikes that are likely to hit economic growth affecting demand has pushed prices down.

International Energy Agency (IEA) raised monthly demand forecast by 380,000 barrels per day (bpd) while also banking on 500,000bpd injection from Russia. OPEC cut forecast by 250,000 as six oil and gas fields shut down after a leak which will cut about 500,000bpd from the Gulf of Mexico.

International Petroleum Price		
Period	Brent	WTI
12-Aug-22	98.15	92.09
W-W	3.4%	3.5%
M-T-D	-8.3%	-12.1%
M-M	-1.0%	-1.0%
Y-T-D	24.3%	19.6%
Y-Y	37.6%	33.3%

Table 3: Bidding Guidance Source: KSL, investing.com

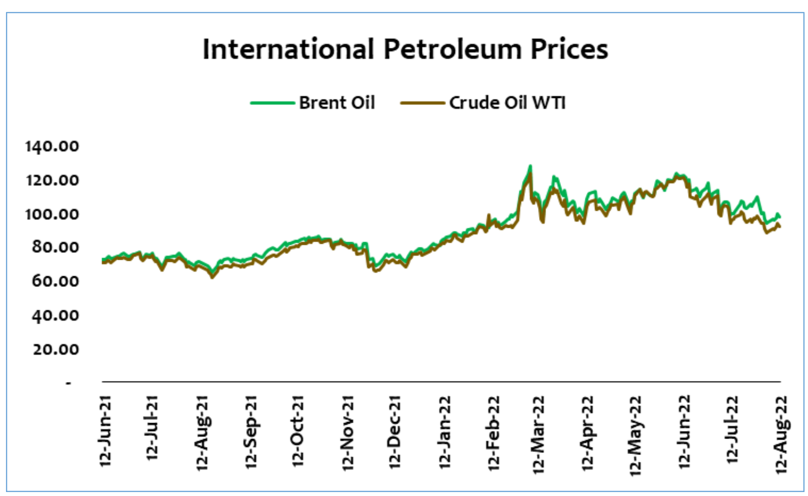


Figure 5: Currency Movement Source: KSL, investing.com

Treasury Bills

T-Bills has seen a 6-month under-subscriptions based on the tight liquidity levels. Of recent months, demand has skewed to the 91-day paper with most investors adjusting for tactical purpose the tenure yield rising 39.8bps m-m basis to 8.565%. The 182-day paper rose by 18.0bps to 9.433% while the 364-day paper lost 5.8bpst to close to 9.922%.

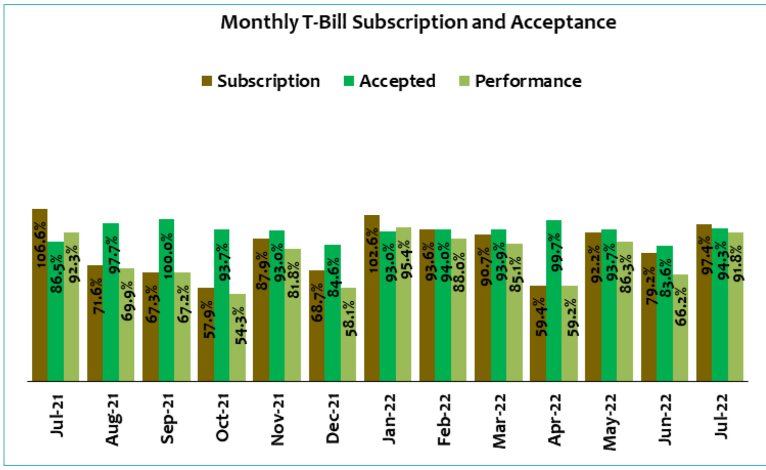


Figure 6: T-Bill Performance Source: KSL, CBK

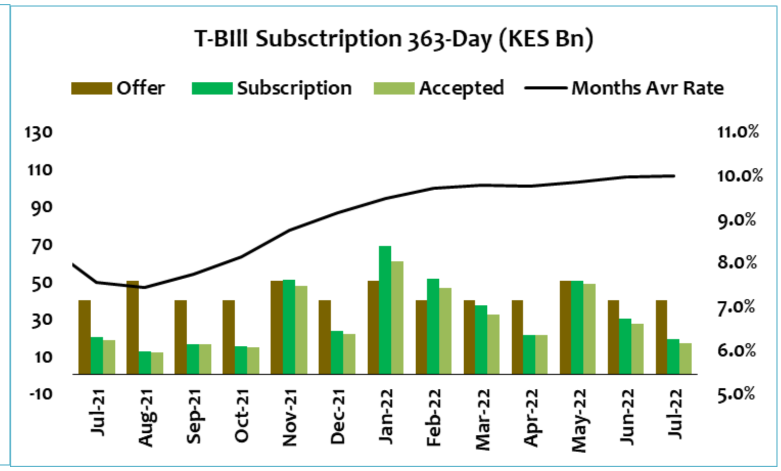


Figure 7: T-Bill Performance 364-Day Source: KSL, CBK

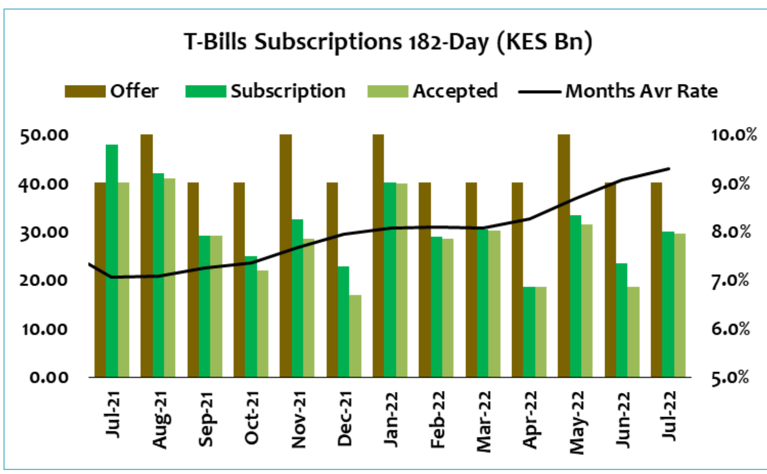


Figure 8: T-Bill Performance 182-Day Source: KSL, CBK

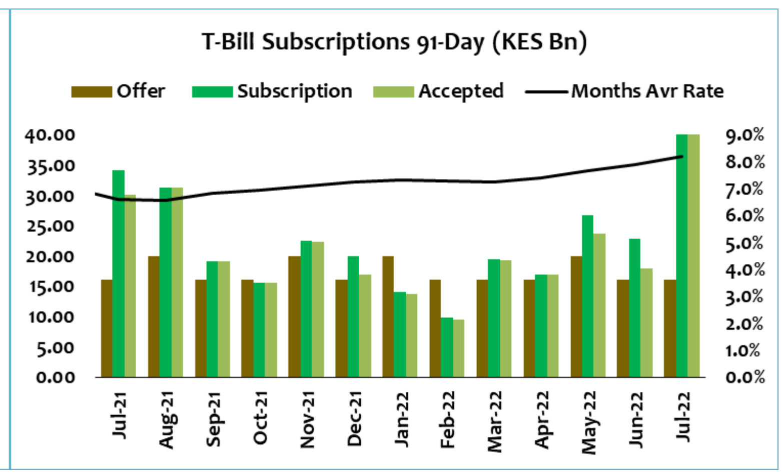
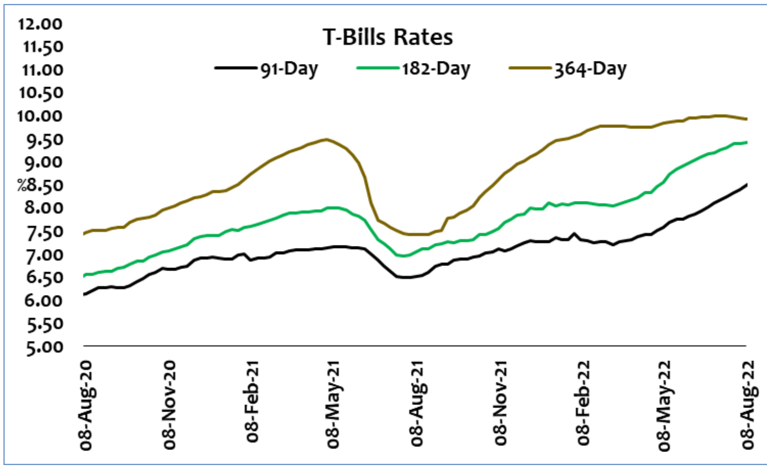


Figure 9: T-Bill Performance 91-Day Source: KSL, CBK

Liquidity management has remained key for investor. We forecast undersubscription to remain into the month of September with as T-Bill payouts stand at KES 72.03Bn and 67.23Bn against a demand for KES 96Bn and KES 120bn in August and September respectively.

During the period, demand will continue to focus on the 91-day and 182-day papers while the rise on rate of return will slow down as the range between the paper and the 364-day paper tempers down.



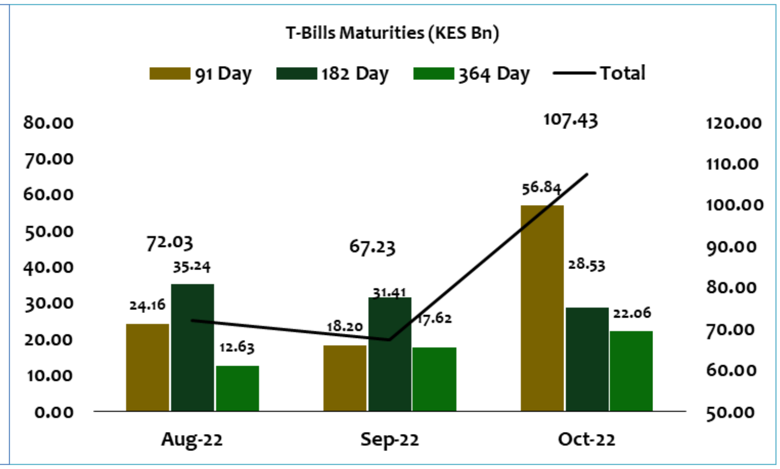


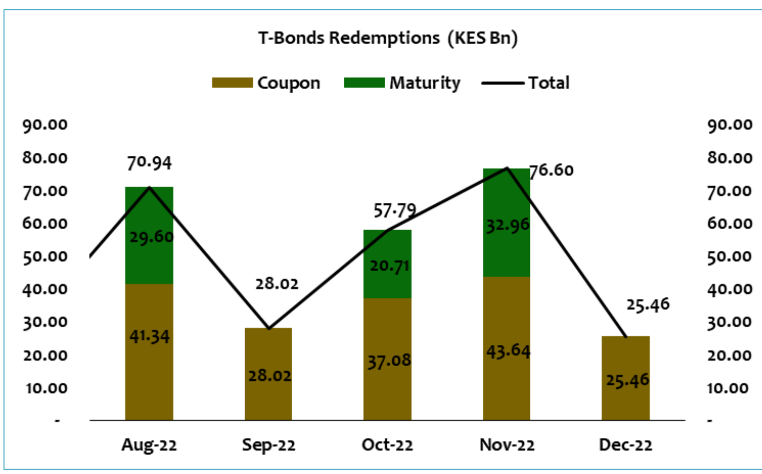
Figure 10: T-Bill Performance 91-Day Source: KSL, CBK

Figure 11: T-Bill Performance 91-Day Source: KSL, CBK

Bonds Market

CBK has offered KES 50.00Bn in August primary issue against an expected payout of KES 70.94Bn in KES 41.34Bn in coupons and KES 29.60Bn in maturities scheduled for August 22nd. The issue is expected to see a near 100.0% subscription based on the payout. We expect a positive performance due to the demand.

Yield Curve has not seen much movement m-m while there has been an upward shift y-y. The stability of the m-m yield curve has shown investors have limited space on pricing the primary as a rise in yield curve to compensate on the pricing of the reopened bonds will not offer much gains on the secondary market.



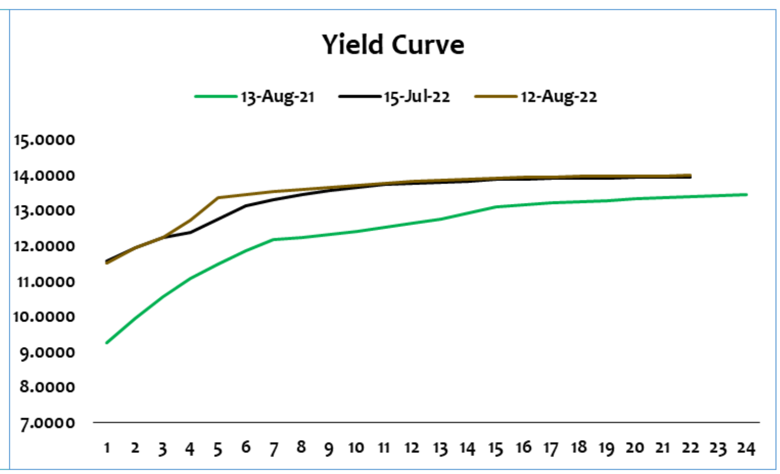


Figure 12: T-Bill Maturities Source: KSL, NSE

Figure 13: T-Bill Maturities Source: KSL, NSE

Yield Key Rates %	13-Aug-21	07-Jan-22	15-Jul-22	12-Aug-22	y-y bps Δ	y-t-d bps Δ	y-t-d bps Δ
2-Yr	9.2620	9.9932	11.5632	11.5162	225.4	152.3	-4.7
5-Yr	11.0771	11.4177	12.3816	12.7200	164.3	130.2	33.8
10-Yr	12.5197	12.7156	13.5661	13.6499	113.0	93.4	8.4
15-Yr	13.1500	13.2475	13.8115	13.8896	74.0	64.2	7.8
20-Yr	13.2812	13.4326	13.9198	13.9657	68.5	53.3	4.6
24-Yr	13.3848	13.5848	13.9485	13.9841	59.9	39.9	3.6

Table 4: Key Yield Rate Source: KSL, NSE

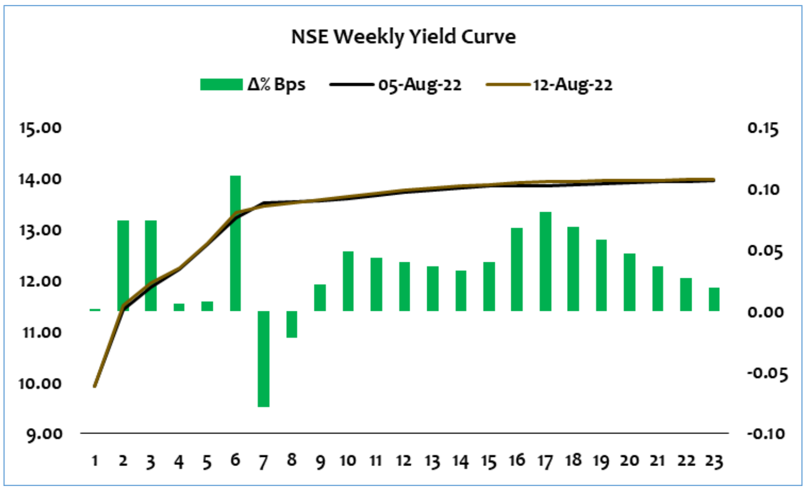


Figure 14: Monthly on Month Yield Curve Source: KSL, CBK

Eurobond

The peaceful electioneering process left a smile on Kenyan Eurobond holders with the 2024 yields declining by 722.8bps to 11.779% m-m Eurobond yields declined. The 2027 bond yields were down 420.7bps as international investors adjust to the notion of new administration.

We expect further downward shift on yields as the election fever dies down and new administration takes reign.

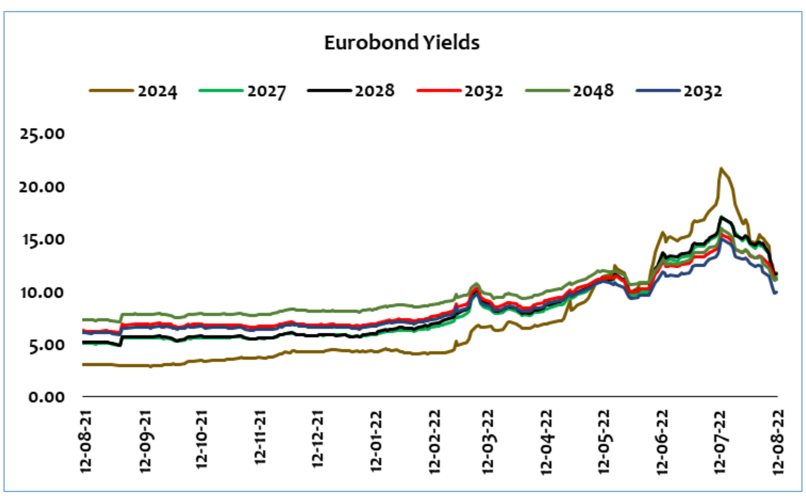


Figure 14: Monthly on Month Yield Curve Source: KSL, CBK

Eurobond BPSΔ						
Bond Tenure	2024	2027	2028	2032	2034	2048
12-Aug-22	11.779%	11.370%	11.697%	11.209%	9.964%	11.121%
W-W	-335.7	-293.9	-287.5	-196.6	-188.6	-152.7
M-T-D	-284.4	-277.4	-270.4	-199.0	-243.1	-204.0
M-M	-722.8	-420.7	-399.2	-294.2	-363.9	-350.9
Y-T-D	739.0	561.2	592.8	442.4	345.8	302.9
Y-Y	873.2	631.3	646.5	494.8	388.1	383.3

Table 5: Eurobond Yield BPS Change

Source: KSL, Bloomberg

Research Analyst Certification:

The research analyst(s) primarily responsible for the preparation and content of all or any identified portion of this research report hereby certifies that all the views expressed herein accurately reflect their personal views. Each research analyst(s) also certify that no part of their compensation was, is, or will be, directly or indirectly, related to the view(s) expressed by that research analyst in this research report.

Terms of Use – Disclaimer:

Kingdom Securities Ltd – A subsidiary of Co-operative Bank Limited.

Co-operative Bank House- 5th Floor, P.O Box 48231 - 00100 Nairobi, Kenya

Office: 0711049540/0711049956

Email: kingdomresearch@co-opbank.co.ke

Research Department

Willis Nalwenge, CFA wnalwenge@co-opbank.co.ke

Shadrack Manyinsa smanyinsa@co-obank.co.ke

Equities Trading

Justus Ogalo, ACSI jogalo@co-opbank.co.ke

Fixed Income Trading

Ashley Odundo aodundo@co-opbank.co.ke

Asena Moffat amoffat@co-opbank.co.ke

Client Service and Operations

Hycinth Monchari hmonchari@co-opbank.co.ke

Timothy Kagunya tkagunya@co-opbank.co.ke