Kingdom Securities Limited

Pre-Auction Fixed Income Note – April 2023

Total Issue KE 30.00Bn

FXD1/2022/003 – Coupon 11.766% - Tenure 2.1 years

FXD1/2019/015 – Coupon 12.857% - Tenure 10.9 years

April 17, 2023

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Primary Issue – Second Phase- FXD1/2022/03 AND FXD1/2019/15

The second phase of the April Primary issues seeks to raise KES 30.00Bn from the reopened FXD1/2022/03 and FXD1/2019/15. The market has continued to face tight liquidity leaving majority of players out of the market.

The last bond, FXD2/2018/010, managed a 17.9% subscription forcing treasury to issue a tap. During the same run, there was a tap for IFB1/2023/017 which received KES 5.12Bn of the KES 10.00Bn on offer.

The fiscal cycle has played to the traditional movement with third quarter of the fiscal year having a tight liquidity. This year, it is set to overshoot into the fourth quarter.

On overall, we forecast low subscription on tight liquidity space. Preference will remain on the FXD1/2022/003 due to the tenure despite only KES 518.80Mn traded in the secondary market since the beginning year. The bond has KES 58.84Bn issued with investors preferring to hold till maturity with the yields 108.2bps above par while the coupon of 11.7660% is 83.4bps higher than the 1-year paper.

The mid tenure FXD1/2019/015 was issued in January 2019 and reopened in July 2020. Total amount issued is KES 79.10Bn with KES 1.59Bn transacting year to date. Investors will shy away from the issue to due to the tenure and the huge holding that does not trade much. The y-t-m stands at 126.5bps above par. Below is our bidding guidance

Bond	FXD1/2022/003	FXD1/2019/015
Tenure	2.1 Years	10.9 Years
Offer	30.00 billion	
Coupon	11.766%	12.857%
Period of Sale	16-Mar-2023 to 18-Apr-2023	
Auction Date	19-Apr-23	
Value Date	24-Apr-23	
Conservative Bid	13.000% - 13.375%	14.400% - 14.650%
Aggressive Bid	13.500% - 13.875%	14.750% - 15.00%

Table 1: Bidding Guidance Source: KSL, CBK

IMF Global Economic Outlook

In the April 2023 Economic Outlook, IMF revised global growth forecast from 2.9% in January to 2.8%. This is driven by the invasion of Ukraine by Russia and three years of Covid. The report dubbed A Rocky Recovery, states that Global headline inflation is set to fall from 8.7% in 2022 to 7.0% in 2023 on the back of lower commodity prices but core inflation is likely to decline more slowly.

The regional reports forecast Sub Sahara Africa (SSA) to grow by 3.4% in 2023 with a growth of 4.8% when Excluding Nigeria and South Africa. The report states SSA will be affected by high global interest rates, elevated sovereign debt spreads, and exchange rate depreciations, among other factors, which have created a funding squeeze for many countries in the region. This challenge comes on top of policy struggles from the ramifications of the COVID-19 pandemic, the cost-of-living crisis and drying donor flows.

IMF retained Kenya's growth rate of 5.3%. The country faces favorable weather conditions but will grapple with growing domestic revenues which will impact deficit management.

Pre-Auction Fixed Income Note

Second Phase - April - 2023

Interbank Rate

The market continues to face liquidity challenges with the interbank shooting to 8.5315% on April 14th, 2023, 177.1bps higher compared to same date in March. The interbank rate has been edging upwards despite frequent market interventions while commercial banks reserves have remained on the KES 10.00Bn short term average.

The current liquidity environment will leave the interbank rate high while the market will continue to witness further interventions to contain the rate below the 10.0% levels.

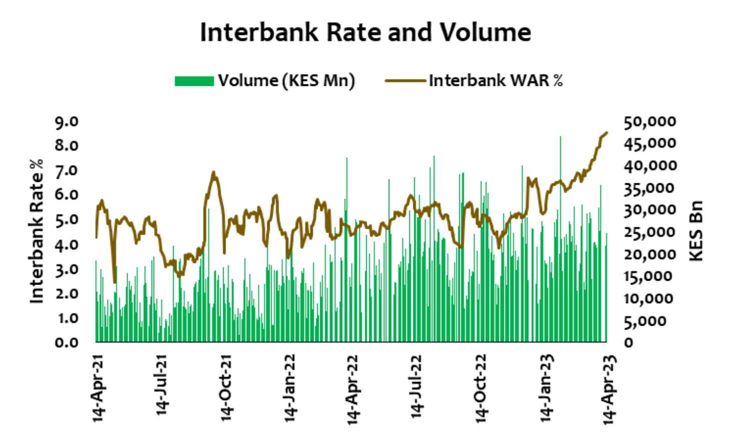

Figure 1: Interbank Rates and Volumes Source: KSL, CBK

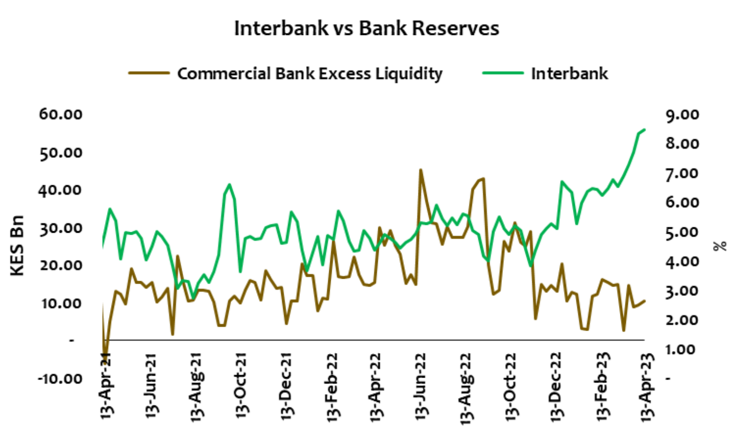

Figure 2: Interbank Rates and Commercial Bank Liquidity Source: KSL, CBK

Currencies

The intervention of the government in the interbank foreign exchange saw the benefits accrued in the initial stages diminish with the local currently shedding 3.8% m-m against the US dollar on April 14th, 2023. The shilling has lost 7.4%, 7.2%, 3.9% against the British pound, EURO, and Japanese yen respectively.

The shilling continues to get a beating from the international market with the green buck tightness remaining globally. The US Dollar shed 1.9% m-m as represented by the dollar index as the Fed Reserve governor giving hint for additional rate hike with majority of analyst predicting a 25basis hike on the current 5.0%. The Governor continues to view that inflation remains above target with March inflation at 4.98%, compared to 6.04% last month and 8.54% April 2022. This is higher than the long-term average of 3.28%.

KES	KES/USD	KES/GBP	KES/EUR	KES/JPY	Dollar Index
14-Apr-23	134.3529	168.2315	148.5150	101.3640	101.2450
W/W	0.8%	1.2%	1.8%	-0.5%	-0.3%
M-t-D	1.4%	2.5%	2.9%	2.2%	-0.5%
M/M	3.8%	7.4%	7.2%	3.9%	-1.9%
Y-t-D	8.9%	13.1%	12.8%	6.4%	-2.9%
Y/Y	16.4%	11.9%	18.7%	10.0%	0.9%

Table 2: Currency Movement Source: KSL, CBK

Demand on the local currency driven by the high import bill, especially on the energy bill, will continue to see the local currency shed value with debt and import bill depleting the country's foreign reserves which stand at USD 6,376Mn or 3.56 months of import cover.

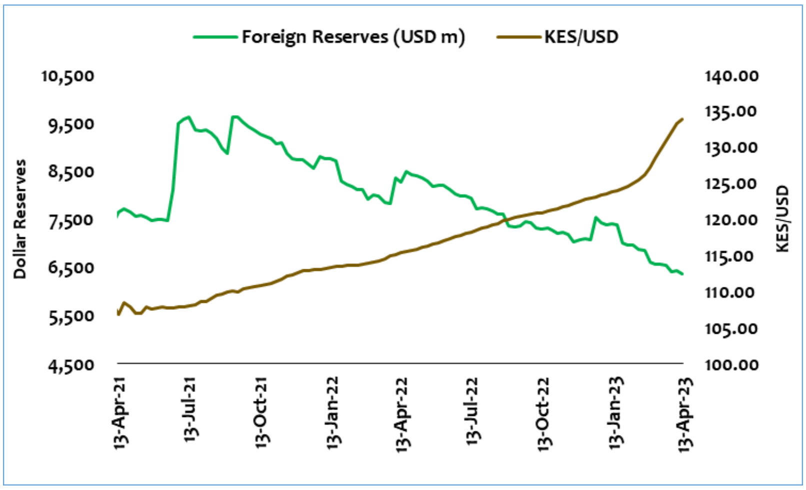

Figure 3: KES/USD and Forex Reserves Source: KSL, CBK

The shilling has depreciated at a faster rate than historical levels with three-month average of 2.8%. If the depreciation continues at this rate, the shilling is bound to close at KES 169.67/USD.

Relief is bound to come from the Government-to-Government agreement on the importation of petroleum product through international oil marketers which include Saudi Aramco, Abu Dhabi National Oil Company (ADNOC) and Emirates National Oil Company (ENOC). This method creates an advantage with Kenya getting 180 credit cycle days compared to the current 30-45 day credit cycle days and settlement in Kenya shilling from dollar as energy gobbles 30% of total import bill.

Treasury Bills

Treasury bills continues to witness an oversubscription with investors opting for short term investment as tight liquidity environment rules.

as per figure 5, the 91-day paper has posted better returns compared to the other two tenures with range narrowing with a range of 35.6bps and 86.0bps on the 182-day and 364-day respectively.

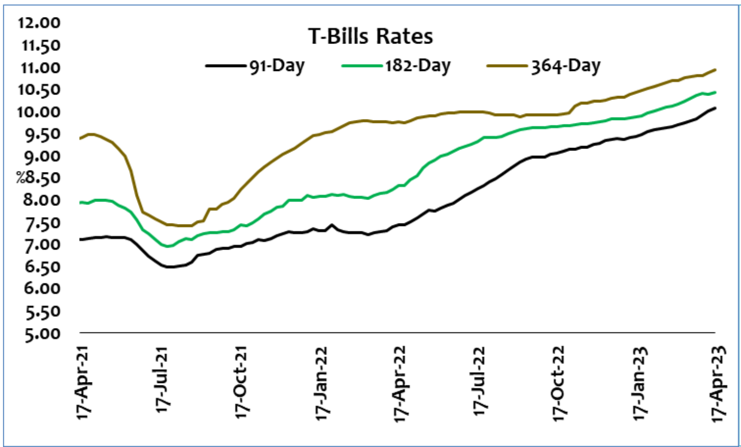

Figure 4: T-Bill Rates Source: KSL, CBK

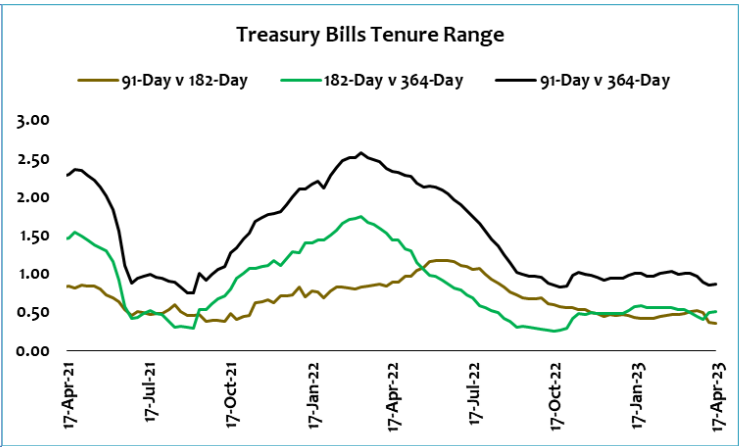

Figure 5: T-Bill Rates Range Source: KSL, CBK

The short-term paper will continue to benefit with investors opting to sit and wait the direction of the CBK and economy with regards to liquidity.

The yields will affect the yield on short-end bonds which should force the government to issue a new short-end bond for better prices and uptake compared to re-openings

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