KINGDOM SECURITIES

Fixed Income Pre-Auction Note

January 2025

FXD1/2018/15
FXD1/2022/25
KES 30Billion

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Primary Auction - FXD1/2018/15 AND FXD1/2022/25

The National Treasury re-opened two papers, FXD1/2018/15 (8.3 -years) and FXD1/2022/25 (22.8-years) targeting KES 30.00Bnfrom its first auction of 2025.

In an aim to manage short-term government liquidity requirement, the Central Bank of Kenya issues the two long-term papers pointing to the government's appropriate cost of financing long-term papers. This is even as we expect more interest rate cuts in an aim at pushing for economic growth by way of improving credit to the private sector.

We recommend the following bidding rates for your consideration based on the prevailing economic conditions discussed hereafter:

Bond	FXD1/2018/15	FXD1/2022/25
Amount	KES 30 billion	
Tenure	8.3-Yrs	22.8-Yrs
Coupon	**12.65%**	**14.188%**
Period of Sale	13th December 2024 to 15th January 2025	
Value Date	20th January 2025	
Conservative	**14.20% - 14.40%**	**15.75% - 15.95%**
Aggressive	14.41% - 14.70%	15.96% - 16.15%

The FXD1/1018/15 (8.3-yr) paper last traded at an implied yield of 13.98% in the secondary market while the FXD1/2022/25 (22.8-Yr) traded at an implied yield of 15.60%. The papers on either side of FD1/2018/15 trade at implied yields of 13.98% and 13.96% for papers of 8.1-years and 8.8-years respectively.

Owing to the low liquidity demand by the government, we foresee conservative bidding on both two papers. This will be supported by a slightly liquid market occasioned by the general easing of interest rates in the market.

We forecast heavy concentration on the long-term paper (FXD1/2022/25) especially as the paper seems lucrative for long-term investor such as pension funds and insurance firms which could love to lock some long-term investments. This is because of its high coupon of 14.188% and 10% with-holding tax rate, steady relatively high income and protection against market interest volatility.

As rates come down, the two papers provide room for some good investment portfolios as explained hereafter.

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Central Bank and Monetary Policy

Overall inflation for 2024 averaged at 4.5% from 7.7% with the last three months closing at 2.7%, 2.8% and 3.0% for October, November and December respectively.

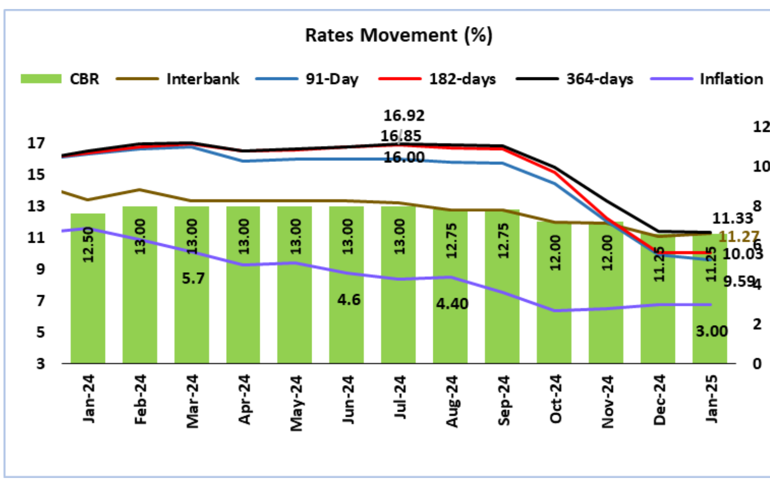
This saw the Central Bank Monetary Policy Committee (MPC) implement a further 0.75% or 75.0bps rate cut on the official base lending rate from 12.0% to the current level of 11.25%.

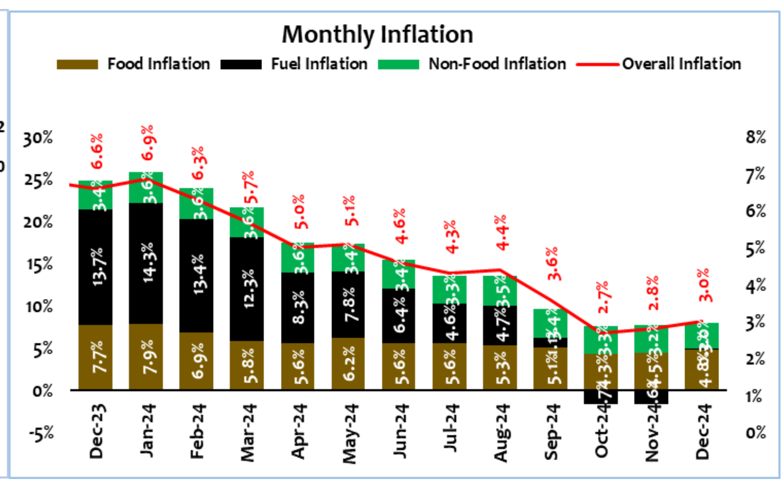
We view this as a measure to support overall macro-economic growth by way of growing private sector credit and making it accessible to businesses. Private sector credit growth recorded the worst growths of 1.3%, 0.4% and 0.0% in the months of August 2024, September 2024 and October 2024 respectively. The situation mainly emanated from increased credit risk, escalating non-performing banks loans which resulted to tightening of credit scores to the private sector. This is in addition to loans becoming expensive as the base lending rate touched over a decade high of 13.0%.

Further, gross domestic product (GDP) growth rates for Q2-2024 and Q3-2024 recorded low growth rates of 4.6% and 4.0% respectively compared growths of 5.6% and 6.0% recorded in similar periods in 2023 respectively. The declines followed economic growth declines in most sectors.

Considering all this, we anticipate additional interest rate cuts to promote private sector access to credit which will in turn spur economic growth.

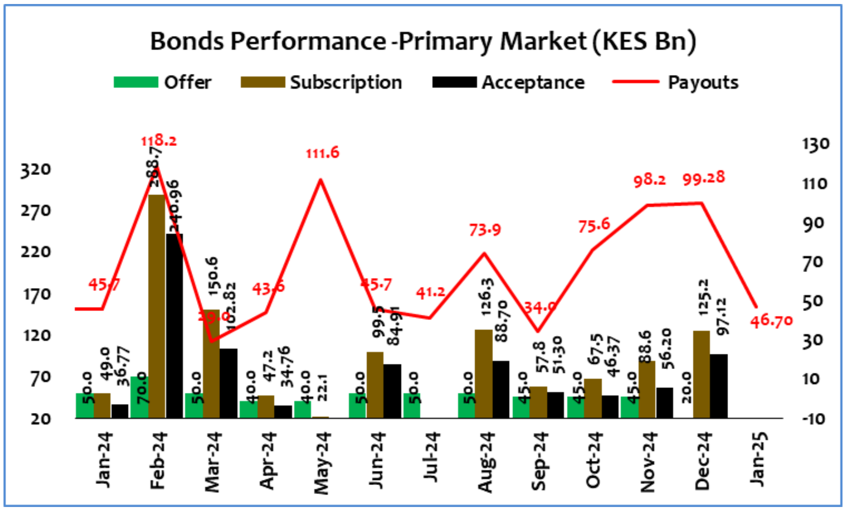
The interbank rate however remained well anchored around the CBR rate as per the Central Bank policy that directs the rate to operate within margins of CBR±250bp to the current rate of 11.27% as of 13th January 2024.





Primary Market Bonds Performance

The primary auctions have remained heavily supported by re-investments from both coupon and bond maturity payouts. New investments continue also to support subscriptions especially from pensions funds, insurance firms and fund managers.



Coupon Payouts

January 2024 – KES 46.70Bn

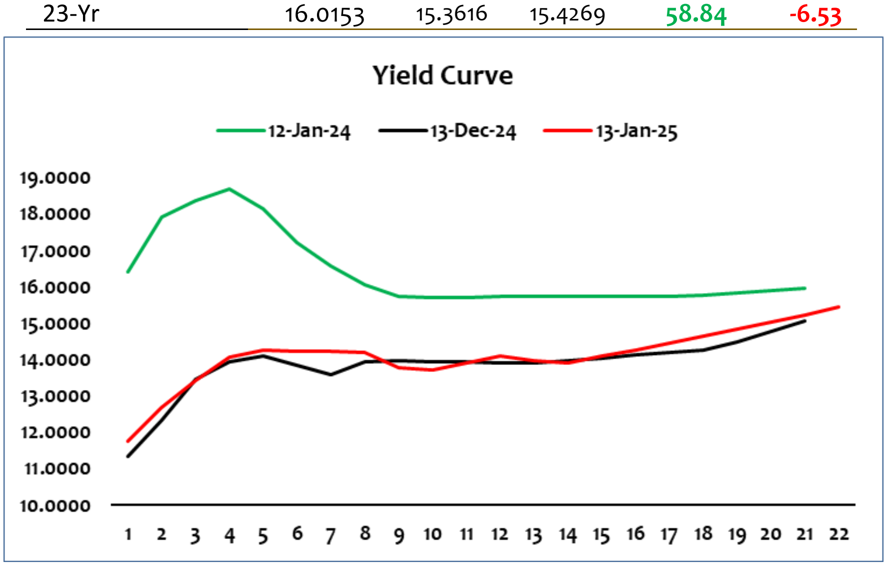
February 2025 - KES 81.17Bn

Yield Curve

The yield curve continues shifting downwards, pulled down by the ongoing interest rate cuts implemented by the Central Bank. In the last one month, the long end of the yield curve shifted upwards on upon government issuance of long-term papers, the FXD1/2018/20 - (13.3 years) issued in December 2024 and the current paper in this primary auction.

The short end of below 9-years also shifted upward on the same reason after the government re-opened the FXD1/2023/10 - (8.2 years) paper and the current re-openings.

Yield Key Rates %	12-Jan-24	13-Dec-24	13-Jan-25	y-t-d bps	w-w bps
2-Yr	17.9287	12.3422	12.6699	525.88	-32.77
5-Yr	18.1540	14.1088	14.2437	391.03	-13.49
10-Yr	15.7046	13.9398	13.7123	199.23	22.75
15-Yr	15.7253	14.0379	14.0790	164.63	-4.11
20-Yr	15.8996	14.7587	15.0291	87.05	-27.04
23-Yr	16.0153	15.3616	15.4269	58.84	-6.53



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