



Primary Bond Auction Note February 2024



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Tapping the Goldilocks Zone

7th February 2024

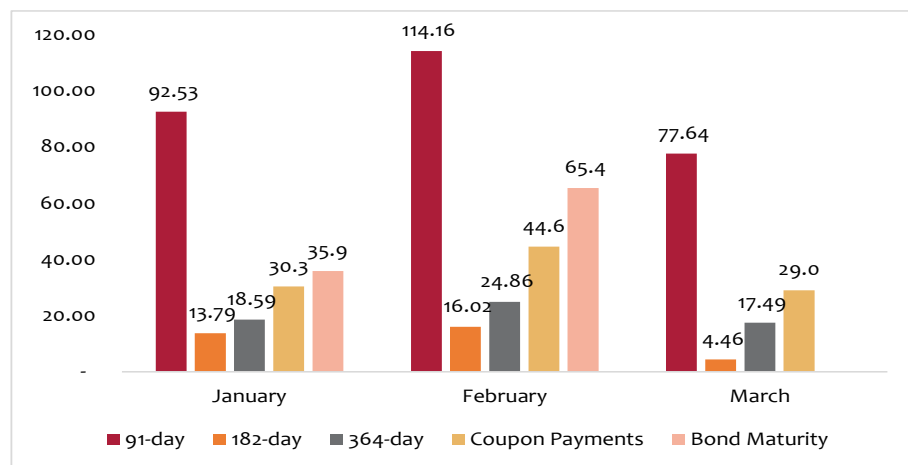


In the [February 2024](#) Primary Bond Auction, the National Treasury is seeking to raise KES 70.0Bn through the opening of the IFB1/2024/8.5 Infrastructure Treasury Bond earmarked for funding of infrastructure projects in the FY2023/24.

We note that the 2yr–10yr inversion spread widened from 220.6bps as of 22nd December 2023 to 225.2bps as of 26th January 2024. From our vantage point, we expect a steepening of the yield curve in response to the repricing of risk premia at the short end of the curve. **We continue to believe the goldilocks zone for the Exchequer currently remains at the short end of the yield curve to preserving the long end of the term structure.** As such, overplays in pricing of risk premiums will be contained for the near short term.

Currently, the weighted average tenor to maturity of the Infrastructure Bond (IFB) series stands at c. 6.8 years. The government has approximately KES 265.04Bn worth of T-Bills and coupon and principal bullet repayments due in February 2024. **We estimate that part of the auction proceeds will go towards refinancing upcoming maturities.**

Chart 1: 4Q2023 Maturities of Domestic Government Securities (KES Bn)



Source: Nairobi Securities Exchange, Genghis Capital

January 2024 Primary Bond Auction Review

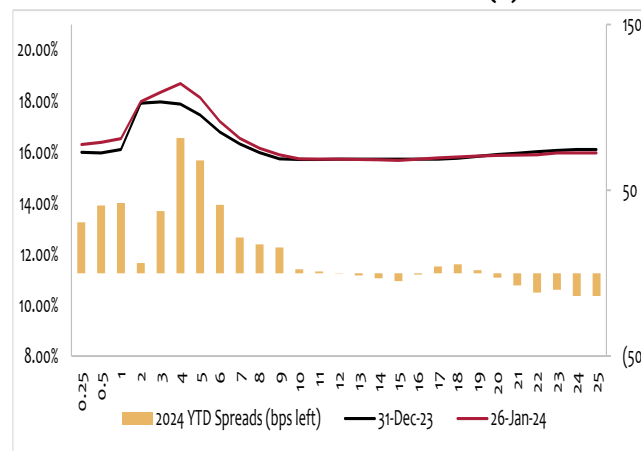
The [January 2024](#) Primary bond auction featured the re-opening of the FXD1/2023/005 (4.6 years) and the opening of the FXD1/2024/003 (3.9 years) seeking to raise KES 35.0Bn. Of the KES 35.0Bn sought, the Exchequer **received** bids totaling KES 37.15Bn – representing a performance rate of 106.15%. The Exchequer accepted bids totaling KES 25.02Bn. This acceptance rate of 67.33% signified a less assertive Exchequer, as yield continue with their positive momentum. The two papers printed a market-weighted average rate of **19.0675%** and **18.6314%** for the FXD1/2023/005 and FXD1/2024/003, respectively.

The weighted average rate of accepted bids printed at **18.7697%** and **18.3854%** for the FXD1/2023/005 and FXD1/2024/003 issues respectively. The average yield spreads stood 133bps and 43bps above the prevailing yield curve at issuance.

IFB1/2024/8.5	
Issuer:	Republic of Kenya
Total Amount:	KES 70 Billion
Purpose:	Funding of Infrastructure Projects in the FY 2023/24 Budget
Tenor:	Eight and a half Years (8.5)
Coupon:	Market Determined
Price Quote:	Discounted/Premium/Par
Period of sale:	24/01/2024 to 14/02/2024
Minimum Amount:	KES 50,000.00
Taxation:	Tax-Exempt
Redemption Dates:	15/02/2027 - 20% of outstanding principal 11/02/2030 - 30% of outstanding principal 09/08/2032 - 100% final redemption
Classification:	Non-benchmark bond
Non-competitive bids per CSD Account:	Max. KES 50 Million per CSD Account
Competitive bids per CSD Account:	Minimum KES 2 Million per CSD Account

Source: February 2024 Primary Bond Prospectus

Chart 2: Yield Curve movement (%)



Source: Nairobi Securities Exchange (NSE)

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Monetary policy environment

Recently the Monetary Policy Committee convened to reassess the benchmark lending rate. On February 6th, 2024, the MPC opted to raise the benchmark lending rate from 12.50% to 13.00% -a 50 basis points increase aimed at fortifying the economy against a resurgence in secondary inflationary pressure as well its pursuit infuther stabilising depreciation of the Kenyan shilling.

In January, the general inflation rate remained stubbornly near the upper limit of the Central Bank's target range. Surveys within the agricultural sector suggest that inflation is anticipated to increase over the next three months, driven by ongoing currency depreciation and elevated import expenses. Regarding exchange rate dynamics, although the shilling appears to have stabilized against the dollar, there remains a lingering risk of further depreciation. This risk is attributed to the expected rise in the 2024 current account deficit, projected to increase to 4% from 3.9% in 2023, reflecting a rebound in imports due to reduced global inflationary pressures.

Anticipating an upward trajectory in inflationary pressure fueled by the surge in non-food and fuel inflation coupled with possibility for further exchange rate depreciation, the MPC chose to elevate the benchmark lending rate. This decision is part of a strategy to curtail money supply in the economy, promoting stability in both prices and the exchange rate. The expectation is that the MPC may adopt further measures to tighten monetary policy in the future should inflationary pressures and currency depreciation persist, aligning with the government's objectives for growth and price stability.

Secondary bond market trends

Secondary bond market activity increased by 12.6% m/m, with turnovers clocking KES 62.58Bn in January 2024 up from KES 55.6Bn in December 2023. The highest-grossing trades were skewed toward long-dated IFB issues. However, the most traded paper over the month of January 2024 remained the IFB1/2023/6.5 paper.

Discount securities recorded a slight increase in January 2024 with the average performance rate at c. 156.25% vis-à-vis c. 141.69% in December 2023. We attribute the broad overperformance in part to lucrative effective yields in the spot market. This, in our view, reflects the rising investors' preference for short-tenor papers as a hedge against duration risk.

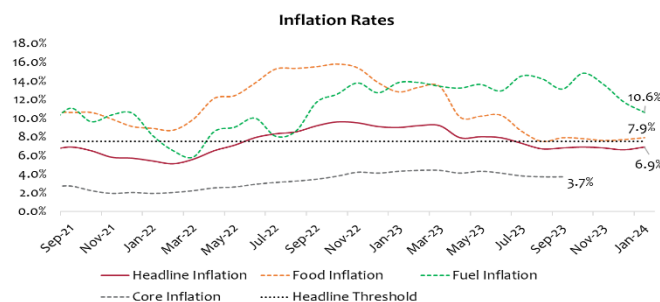
We anticipate additional pressure on the spot rates as the short end of the term structure keeps up with the inversion pace. Notably, the 91-day, 182-day, and 364-day T-Bills yields have all soared by an average of 38bps since the year began. This reflects exuberant risk pricing by investors in response to the increasingly uncertain environment with the significant upcoming debt rapayments.

Price levels

The year-on-year (y/y) headline inflation (**Chart 3**) for the month of Janaury 2024 increased marginally by 30bps to 6.9% up from 6.6% in Janaury 2023. The increase was largely attributable to the 160bps increase in prices of housing ,water , electricity and Other fuels' to 9.7% in January 2024. In contrast, transport index declined marginally to 10.6% y/y on account of a decline inpetrol and diesel prices. The rise in food inflation was bening during the month with the price of oranges , potatoes , carrots and cabbages witnessing the largest increase in prices.

With inflation stabilizing below the CBK benchmark, the upside risk however remains pegged on further volatility in fuel prices given the weakening slide of the Kenya shilling and geopolitical tensions in the middle east. As such we anticipate headline inflation to oscillate below the National Treasury's upper bound threshold of 7.5% over the medium term.

Chart 3: Inflation trends



Source: Kenya National Bureau of Statistics (KNBS)

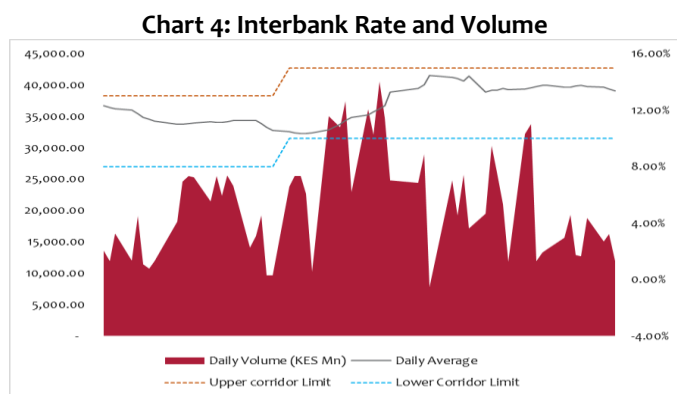
Market liquidity conditions

Rates in the interbank market (**Chart 4**) increased marginally in January 2024, with the average interbank rate coming in at 13.69% (203bps m/m). We note that interbank volumes also remained at marginally elevated levels to those recorded prior to the introduction of the interest rate corridor. Discount window borrowing witnessed a decrease

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in the month of January. We think this signifies that demand for liquidity has decreased with the increase in the interest rate affecting recovery of pent-up liquidity demand.

Over to the Open Market Operations, the CBK injected upto amount of KES 478.25Bn in December 2023 (vis-à-vis KES 323.94Bn injected in November 2023) via Rev. Repo Agreements. We anticipate liquidity conditions in the interbank market to improve following recent changes to improve liquidity in the market.



Yield curve inversion steepens.

The yield curve (Chart 2) continued to steepen its inversion trend in January 2024, with the 2yr-10yr inversion spread widening to 225bps as of 26th January 2024. Short-term yields have paced by an average of 38bps YTD. Medium-term yields at the belly of the curve on the other hand have surged by an average of c. 20bps YTD while long-term yields have climbed by 5bps YTD. Broadly, yields have risen by an average of 18bps since the year began.

We believe the the short end of the yield curve offers the Exchequer long-term benefits given the current risk environment. Exuberant pricing of risk premia and aggressive bidding in the primary markets is thus contained in the short term. **From our vantage point, we expect further steepening of the yield curve in response to the repricing of risk premia at the short end of the curve.**

Projection

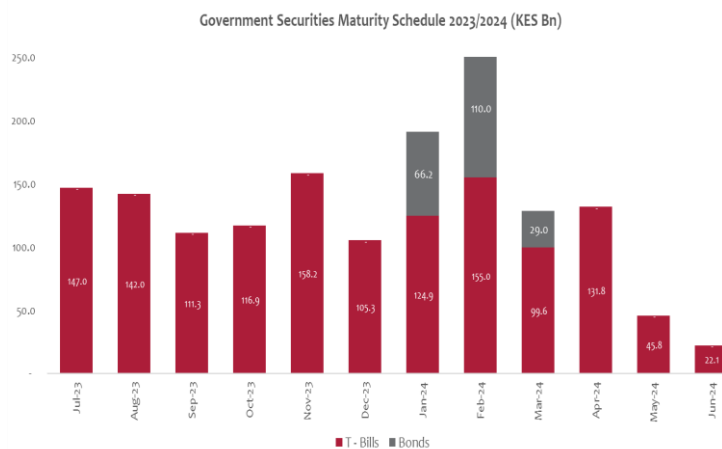
We expect aggressive bidding and high participation rates in the February 2024 auction. From our analysis of the prevailing macroeconomic environment, market liquidity levels, upcoming coupon payments and investor bids at past auctions, **we recommend bid levels of 18.90-19.50 for IFB1/2024/8.5**

Table 2: CBK Open Market Operations

	Term Auction Deposits (KES Mn)	Rev Repo Agreements (KES Mn)
2022		
JAN	35,600	93,618
FEB	-	100,632
MAR	-	107,928
APR	-	85,568
MAY	5,000	56,214
JUN	113,200	56,200
JUL	93,500	55,500
AUG	-	94,300
SEP	-	89,300
OCT	-	63,050
NOV	-	48,338
DEC	-	74,320
2023		
JAN	-	206,428
FEB	-	117,948
MAR	-	95,440
APR	-	88,549
MAY	-	179,157
JUN	-	292,000
JUL	95,050	-
AUG	154,578	22,500
SEP	242,980	6,500
OCT	-	306,486
NOV	-	323,939
DEC	-	478,250

Source: Bloomberg, Genghis Research

Chart 5: Government Securities Maturity Schedule FY2023/2024 (KES Bn)



Source: Genghis Research, NSE

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Table 3: 2023-2024 Primary Market Bond Auctions Granular

	Offered Amount (KES, Mn)	Paper(s)	Duration at Issuance (yrs)	Total Bids Received (KES Mn)	Total Bids Accepted (KES Mn)	Performance Rate	Market Average Rate	Average Rate of Accepted Bids	Premium above the Yield Curve	Coupon Rate (%)
Jan-23	50,000	FXD1/2020/005 - Reopening	2.4	27,620	24,353		12.917%	12.879%	0.159%	11.667%
		FXD1/2022/015 - Reopening	14.3	14,012	7,160		14.337%	14.186%	0.291%	13.942%
				41,632	31,513	83.3%				
	10,000	FXD1/2020/005 - Tapsale	2.4	13,903	13,571			12.879%		11.667%
Feb-23		FXD1/2022/015 - Tapsale	14.3	4,119	4,056			14.186%		13.942%
				18,022	17,627	180.2%				
	50,000	FXD1/2017/010 - Reopening	4.5	8,030	7,470		13.897%	13.875%	0.345%	12.966%
		FXD1/2023/010 - New Issuance	10.0	11,515	9,279		14.217%	14.151%	0.358%	14.151%
Mar-23				19,545	16,749	39.1%				
	10,000	FXD1/2017/010 - Tapsale	4.5	8,856	8,594			13.875%		12.966%
		FXD1/2023/010 - Tapsale	10.0	3,608	3,607			14.151%		14.151%
				12,463	12,201	124.6%				
1Q2023	50,000	IFB1/2023/017 - New Issuance	17.0	59,772	50,877		14.469%	14.399%	0.212%	14.399%
				59,772	50,877	119.5%	14.469%	14.399%		14.399%
	20,000	IFB1/2023/017 - Tapsale	17.0	12,712	12,711			14.399%		14.399%
				12,712	12,711	63.6%				
Apr-23	190,000			164,147	141,678	101.7%				
	20,000	FXD2/2018/010 - Reopening	5.8	3,571	3,360		14.393%	14.366%	0.641%	12.502%
				3,571	3,360	17.9%				
	10,000	IFB1/2023/017 - Tapsale	17.0	5,119	5,117	51.2%		14.399%		14.399%
May-23	30,000	FXD1/2022/003 - Reopening	2.1	7,329	1,757	24.0%	13.839%	13.471%	0.662%	11.766%
		FXD1/2019/015 - Reopening	10.9	CANCELED			-	-	-	12.857%
				7,329	1,757	31.0%	13.839%	13.471%		
	20,000	FXD1/2023/003 - New Issuance	3.0	20,744	20,294		14.259%	14.228%	0.892%	14.228%
Jun-23				20,744	20,294	103.7%				
	10,000	FXD1/2023/003 - Tapsale	3.0	10,603	10,602	106.0%				14.228%
	20,000	FXD1/2023/003 - Tapsale	3.0	27,206	27,202	136.0%				14.228%
	60,000	IFB1/2023/007 - New Issuance	7.0	220,519	213,399	367.5%	15.857%	15.837%	1.476%	15.857%
2Q2023				220,519	213,399	123.7%				
	15,000	FXD1/2023/003 - Tapsale	3.0	18,560	18,552					14.228%
					231,951					
	175,000			313,651	300,284	144.7%				
1H2023	365,000		7.3	477,798	441,962	123.2%				
Jul-23	40,000	FXD1/2016/010 - Re-opening	3.2	22,664	15,740		16.5820%	16.3280%	2.083%	16.328%
		FXD1/2023/005	5	29,100	22,833		17.0260%	16.8440%	2.482%	16.844%
				51,764	38,573	129.4%				
	20,000	FXD1/2016/010 - Tapsale	3.2	32,217	31,230					16.328%
Total		FXD1/2023/005 - Tapsale	5	12,212	12,211					16.844%
				44,429	43,441	222.1%				
				96,193	82,014					
Aug-23	40,000	FXD1/2023/002	2	38,302	11,660		17.5545%	16.9723%	0.640%	16.972%
		FXD1/2023/005 (Re-opening)	4.9	14,704	7,456		18.1646%	17.9538%	1.732%	16.844%
				53,006	19,116	132.5%				
	20,000	FXD1/2023/002 - Tapsale	1.9	17,376	17,374					16.972%
Sep-23		FXD1/2023/005 - Tapsale	4.9	6,225	6,123					16.844%
				23,601	23,497	118.0%				
	35,000	FXD1/2023/002	1.9	18,015	15,013		17.5834%	17.4537%	0.453%	16.972%
		FXD1/2016/010 (re-opening)	2.9	15,994	6,616		18.4865%	17.9266%	0.554%	15.0390%
Oct-23				34,009	21,629	97.2%				
	15,000	FXD1/2023/002	1.9	2,631	2,610					16.972%
		FXD1/2016/010 (re-opening)	2.9	815	763					15.039%
				3,446	3,373	23.0%				
Nov-23				37,455	25,002					
	35,000	FXD1/2023/002	1.9	6,506	4,825		17.9637%	17.7358%	0.318%	16.972%
		FXD1/2023/005	4.8	5,792	1,482	35.1%	18.4647%	17.9919%	0.700%	16.844%
				12,298	6,307					
Dec-23	50,000	IFB1/2023/6.5 (New issuance)	6.5	88,900	67,056	177.8%	18.1037%	17.9327%	0.543%	17.933%
				88,900	67,056					
	25,000	IFB1/2023/6.5 (Tap sale)	6.5	47,239	47,867	189.0%	17.9327%	17.9327%		17.9327%
				47,239	47,867					
Jan-24	35,000	FXD1/2024/003	3	29,089	22,069		18.6314%	18.3854%	0.3942%	18.3854%
		FXD1/2023/005 (re-opening)	4.6	8,063	2,947		19.0675%	18.7697%	1.2801%	16.8440%
				37,152	25,016					
	15,000	FXD1/2024/003 (Tap sale)	3	9,340	9,308	79.3%	18.3854%	18.3854%		18.3854%
YEAR TO DATE		FXD1/2023/005 (Tap sale)	4.6	2,552	2,416		18.7697%	18.7697%		16.8440%
				11,892	11,724					
	645,000			885,534	749,561					

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