Madison Investment Managers
August 2022 Economic Highlights
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Economic Update

Disputed elections amidst worsening economic outlook

As the country awaits the verdict of the Supreme Court on the challenged presidential election results, the outlook of local macro-economic conditions continues to decline. As of 30th June 2022, the total national government outstanding bills amounted to KES 504.7bn, with 65.5% of the pending bills belonging to contractors and suppliers. This position adds on more stress to an already burdened debt situation in the country.

Early in the month, the IMF added fresh conditions to the ongoing 38-month USD 2.34bn loan programme that began in April 2021, including: scrapping fuel subsidies, a push for Kenya Power to fully bridge its fiscal deficit by 2023, and the implementation of national tax policy currently being drafted. The proposed removal of fuel subsidies spells difficult times ahead for Kenyans who have been sheltered from the impact of rising global oil prices in the last year. Oil marketers, during the month, had warned of imminent fuel shortages in the country if the government failed to clear KES 65.0bn pending bills.

Food insecurity in the country is projected to increase due to the poor performance of the 2022 long rains. The National Drought Management Authority projects that the number of people in need of assistance could increase to 4.35mn by October 2022 if short rains season performs below average.

Inflation

Inflation hit a 5-year high of 8.5% on surging food and fuel prices

Driven by rising food prices and higher fuel prices, inflation has spiked to levels last seen in 2017, and has exceeded CBK's target range by 1.0%.

The annual Food and Non-Alcoholic Beverages Index spiked by 15.3% year-on-year. On a month-to-month basis, the index jumped by 0.5% as prices of basic food such as maize flour, sugar and mangoes increased by 4.7%, 4.6% and 4.1%, respectively, outweighing price decreases in other food items. The Alcoholic Beverages, Tobacco and Narcotics index also increased by 0.7% month-on-month due to an increase in the prices of beer and wines.

Also contributing to the uptick in inflation was the surging prices of laundry soap and detergents which rose by 36.0% and 21.1%, respectively, compared to last year's prices. Monthly, the two categories' prices rose by 1.5% and 0.7%, respectively. In addition, the elevated prices of fuel continue to put pressure on inflation.

The Currency

The Shilling has weakened by 6.1% against the USD so far in 2022

In the month of August, pressure continued to pile on the KES which weakened by 1.0% against the USD to close at KES 120.01, from KES 118.80 at the start of the month. The depreciation was largely attributable to the strengthening of the US Dollar owing to a heightened global demand. Locally, currency demand from importers has exerted downward pressure on the Shilling.

As at 25th August 2022, the Central Bank of Kenya (CBK) held an adequate forex reserves position of USD 7.6bn equivalent to 4.4 months of import cover. We noted the Shilling exhibited weakness against the USD but strengthened against some major global and local currencies during the month.

Going forward, we view key risks to the KES to be:

i. High import bill, outweighing export revenue
ii. Interest rate hikes in developed markets resulting in capital outflows from emerging and frontier markets
iii. Upcoming foreign debt interest payment
iv. New Covid-19 variants
v. Effects of the Russian-Ukraine crisis on global trade

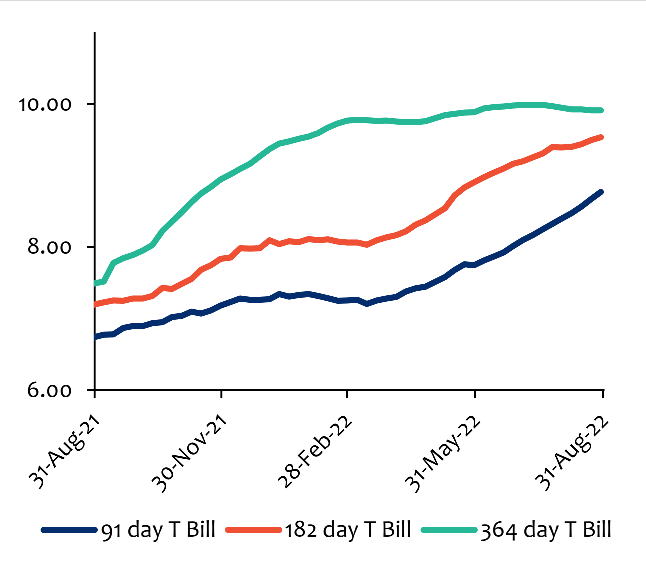
Kenya Shilling Performance	Aug-22	Jul-22	YTD
USD	(1.02%)	(0.82%)	(6.07%)
Sterling Pound	2.22%	0.47%	7.60%
Chinese Yuan	1.37%	(0.12%)	2.08%
Japanese Yen	3.18%	(2.55%)	11.97%
Uganda Shilling	2.61%	(2.23%)	(1.54%)

**CBK, Madison Investment Managers Limited (MIML) Research)*

Fixed Income Performance

T-bill yields had mixed movements in the month

In the month under review, average yields on the 91-day and 182-day papers rose by 37bps and 16bps to 8.57% and 9.45%, respectively. Average yields on the 364-day paper, on the other hand, dropped by 6bps to 9.92%. Overall subscription also reduced to 73.2% on average from 97.4% observed in July 2022.



(Central Bank of Kenya, Madison Investment Managers Limited (MIML) Research)

In August, the Central Bank re-opened FXD1/2022/3, FXD2/2019/10 and FXD1/2021/20, seeking to raise a total of KES 50.0bn for budgetary support. The auction was under-subscribed at 98.3%. The CBK received bids worth KES 49.1bn and accepted KES 38.5bn - an acceptance rate of 78.4%.

The weighted average rate of accepted bids for the bonds came in at 12.45%, 13.88% and 13.96%, respectively, while the coupon rates were 11.77%, 12.30% and 13.44%, respectively. FXD1/2022/3 is subject to a withholding tax rate of 15.00% while 10.00% applies for FXD2/2019/10 and FXD1/2021/20.

Secondary bond turnover rose by 12.3% in August to KES 68.4bn from KES 60.9bn in July 2022.

Equities Market Performance

NSE benchmark indices recorded mixed performance in August

In the month of August, the equities indices recorded mixed performances largely brought on by uncertainty over the outcome of the General Elections. The NASI and NSE 25 declined by 2.6% and 0.6%, respectively, while the NSE 20 advanced by 2.9%. NCBA and Absa bank shares rose by 16.6% and 7.2%, respectively, while Safaricom and EABL shed 6.7% and 2.7%, respectively.

Foreign investors maintained a net selling position in the month, with net outflows of KES 1.7bn relative to outflows of KES 3.0bn recorded in July. Equities turnover in the month fell by 33.3% to KES 5.3bn from KES 8.0bn in recorded last month.

The Nairobi Securities Exchange announced that it expects its first main-market segment listing before the end of December this year. This will be the first major deal since 2018.

Global Markets

US Fed warns of more pain on households and businesses after policy deliberations

The US Federal Reserve bank held its annual economic symposium at Jackson Hole on 26th August 2022 to discuss monetary policy and price stability. The Fed Chair, Jerome Powell, noted that reducing inflation would require maintaining a restrictive policy stance for some time. While the plan to continue raising interest rates is expected to bring some pain to households and businesses, the Fed Chair reiterated that the Fed will take forceful and rapid steps to lower inflation to 2.0%, its target level, from the current reading of 8.5% (July 2022).

This stance comes against a backdrop of spiralling food and energy prices in the Eurozone where August inflation hit a new record high of 9.1%. To combat inflation, central banks across the globe will need to hike interest rates. This, in effect, will slow down economic growth, raise the risk of recession in economies already weighed down by the effects of inflation and add more stress to households and businesses.

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