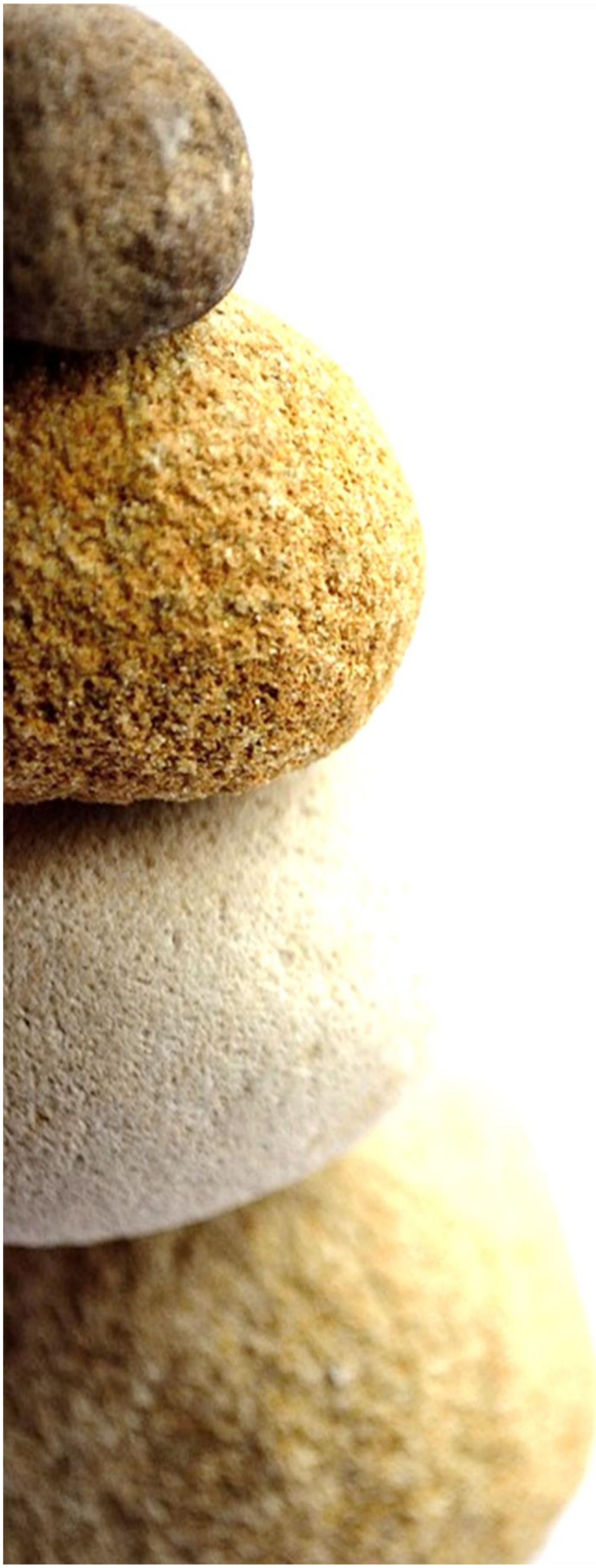


MADISON
Investment Managers

February 2023

Monthly Economic Highlights

Table of contents

Economic Performance

The Stanbic Purchasing Manager's Index (PMI) declined to 46.6 in February from 52.0 a month earlier. This was the first contraction in the private sector since August 2022.

The rollback was mainly due to the steep weakening of the shilling in the month of February, coupled with higher inflationary pressure which led to reduced activity in the private sector.

Performance

Real GDP expanded by 4.7% in Q3 2022 from a 9.3% growth recorded in the same quarter of 2021

Agriculture

The sector contracted by 0.6% in Q3 compared to a 0.6% growth posted in Q3 2021

Manufacturing

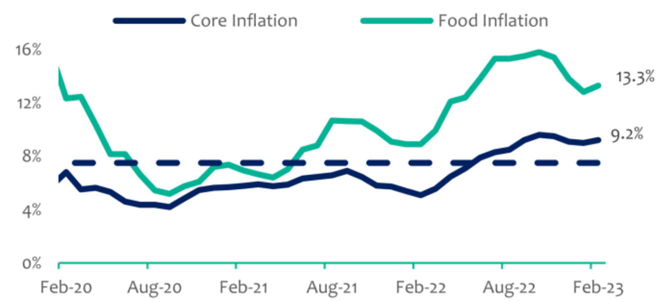
Sector grew by 2.4% in Q3 2022 compared to a 10.2% growth reported in Q3 2021

Outlook

In 2023, World Bank projects Kenya's economy will decelerate to 5.0% from an estimated 5.5% in 2022.

Inflation

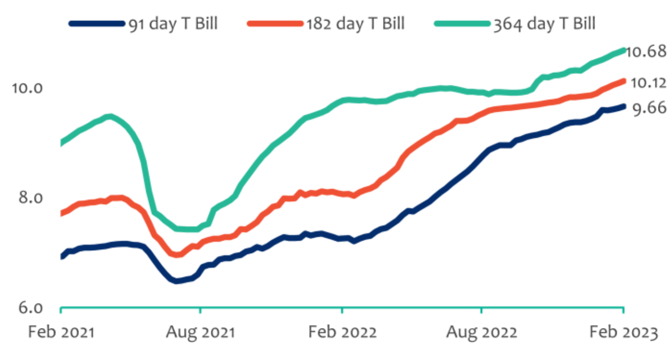
Annual inflation rose to 9.2% in February from 9.0% recorded in January, marking the first increase after 3months. The uptick was mainly attributed to the increase in food prices (cabbage, kales and tomatoes increased by 11.3%, 11.0% and 7.8%, respectively).



Source: Central Bank of Kenya

Interest Rates

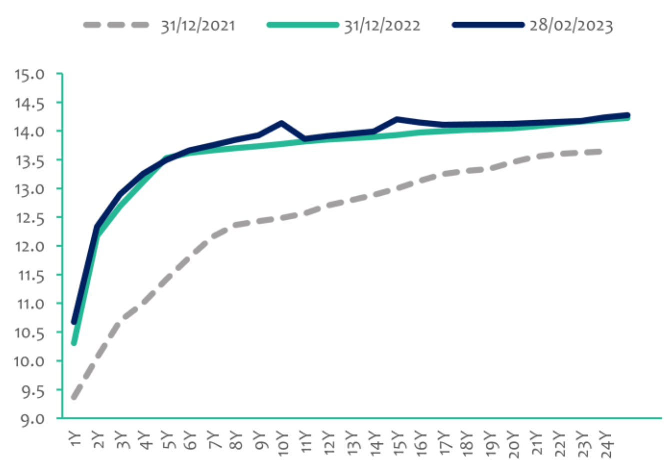
During the month, short-term interest rates were on the rise: the 91-day, 182-day and 364-day treasury bills rose by 17bps, 18bps and 20bps, and closed the month at 9.66%, 10.12% and 10.68%, respectively.



Source: Central Bank of Kenya

Bond Market

In the primary market, the government issued FXD1/2023/10 and reopened FXD1/2017/10, seeking to raise KES 50Bn for budgetary support. They received bids worth KES 19.5Bn and accepted KES 16.7Bn in total. Due to the underperformance, a tap-sale on the same bonds was issued. From this, the apex bank accepted bids worth KES 12.1Bn. As a result, the CBK ended up raising KES 28.8 Bn.



Source: NSE Website

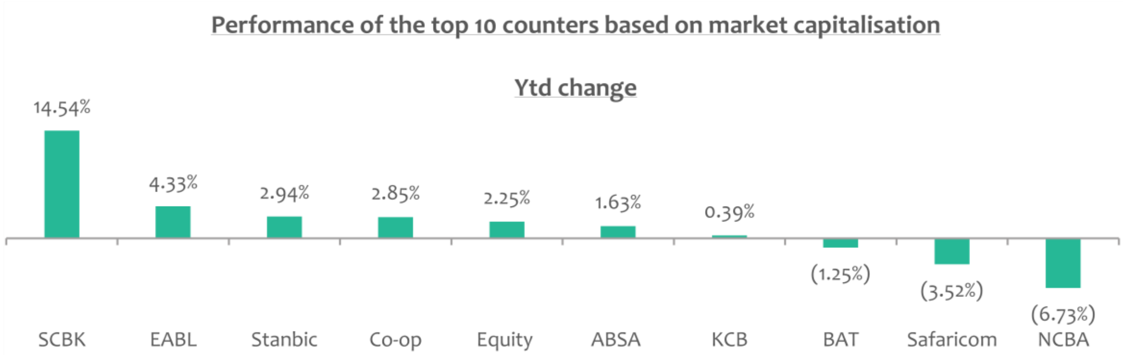
In the secondary market, bond market turnover rebounded by 5.87% to KES 46.6Bn from KES 48.0Bn recorded in January 2023.

Equities Market

During the month, the equities benchmark indices reported mixed performances. The NASI and NSE 25 went up by 0.1% and 0.7%, respectively. Meanwhile, the NSE 20 retreated by 0.6%.

Equities turnover in the month declined by 41.0% to KES 4.6bn from KES 7.8bn recorded in the prior month. Foreign investors maintained a net selling position in the month, with net outflows of KES 0.3bn, compared to net outflows of KES 2.9bn recorded in January.

Kenya shilling depreciation, global interest rates rising and weakening global macros continue to weigh down on the equities market performance.



Source: NSE Website

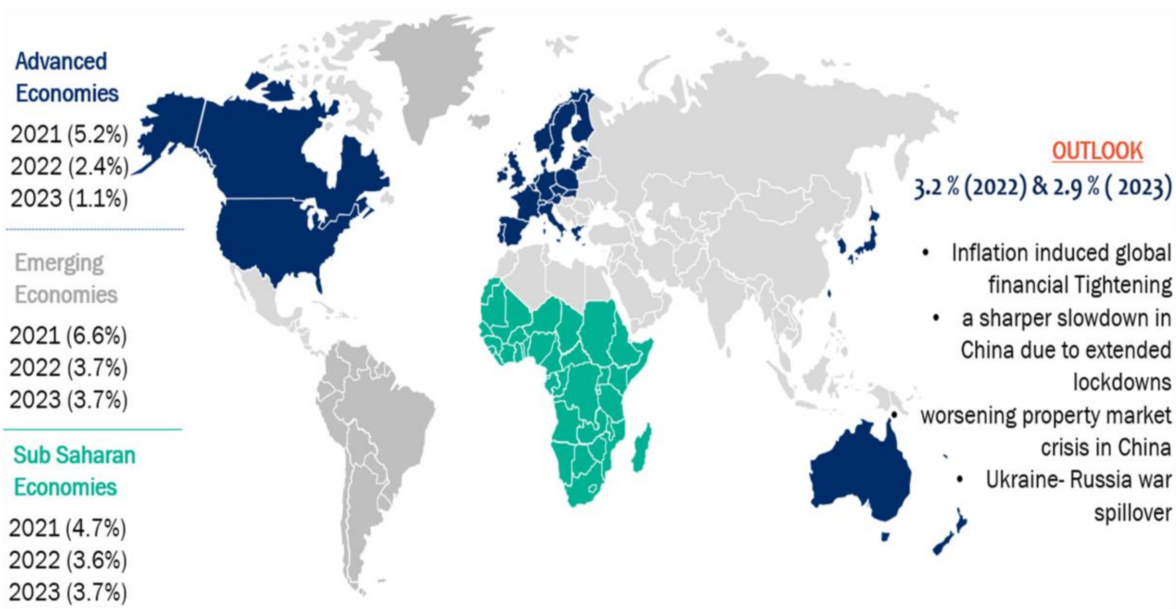
Source: NSE Website

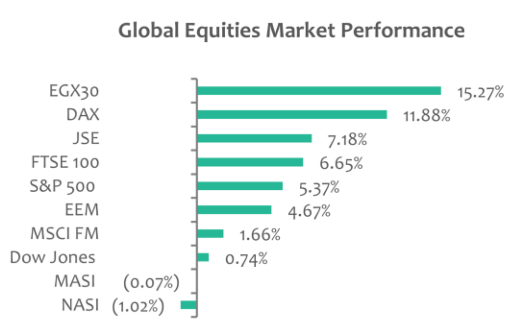
Global Markets

According to the IMF, the global economic growth is expected to decelerate to 2.9 % in 2023 compared to 3.2% in 2022. This expectation reflected negative shocks from simultaneous policy tightening aimed at containing high inflation, worsening financial conditions and continued disruptions from Russia's invasion of Ukraine.

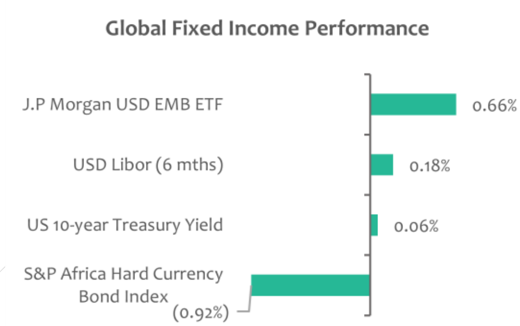
The Federal Reserve raised the target range for the fed funds rate by 25bps to 4.5%-4.75% in its February 2023 meeting, dialing back the size of the increase for a second straight meeting but still pushing borrowing costs to the highest since 2007.

At the start of the year investors were bullish that macroeconomic weaknesses would be moderate hence a strong performance on the equities market. However, persistent inflation and more aggressive tightening of monetary policies seem to be the main risks.





Source: Madison Investment Managers Research Data Room



Source: Madison Investment Managers Research Data Room

Investment Strategy

1. Fixed income

Heightened inflation, depreciating KES, global increase in interest rates, tightening liquidity (as demonstrated by the high interbank rates), blooming private sector growth - all point to a rising interest rate environment.

Investing in short term tenor assets of not more than 3 months for deposits might prove to be beneficial to investors. This will shield portfolios from interest rate risk and duration risk. Bank deposits of rates of 12% and above remain attractive.
Treasury bills remain unattractive at the moment as banks offer a better return.

On a long-term basis, Infrastructure Bonds (IFBs) are likely to provide value for investors in the bonds space more than Fixed Coupon Bonds (FXDs) due to their tax-free nature. We have seen yields on IFBs drop while same tenor FXDs rise presenting investment opportunities.

2. Equities

Currently, the equities market is weighed down by currency depreciation and dollar scarcity which has made the asset class very volatile. Additionally, the increasing foreign outflows have continued to pull the return lower.
Although the market is cheap on a price to earnings perspective and attractive on a dividend perspective, we are still concerned that macroeconomic factors both locally and globally pose the greatest headwinds to this asset class in the medium term.
Banking stocks are likely to perform well as FY 2022 results are released this month. However, we expect to see the stocks prices drop again on book closure of dividends.

3. Regional Markets

The Ugandan bond market has considerable higher yields on a FX adjusted perspective than Kenya. The Bank of Uganda recently cut taxes on interest income from 20% to 10% on bonds with tenors over 10 years. Though the market is smaller than Kenya, there exists pockets of value for investors hunting higher yields on long-term dated papers where interest rates are north of 16% - 18% on selected bonds.

Disclaimer

The Capital Markets Authority does not take responsibility for the financial soundness of the scheme or for the correctness of any statements made or opinions expressed in this regard. Past performance is not an indicator of future performance as price of units may rise or fall. In certain specified circumstances, the right to redeem units may be suspended.

MADISON
Investment Managers