Financial News

12th March 2018

Fiscal consolidation inevitable as revenue shortfall widens

The government reported a KES 84.00Bn shortfall in revenues in the six months to December 2017 with the faltering performance being primarily attributed to the current economic lethargy. While the economic outlook has improved, somewhat bolstered by a more certain political landscape and favourable weather, any recovery in the country's fiscal standing as a result may be limited.

The high fiscal deficit, currently at about 8.00% of GDP, has seen a steep increase in public debt to KES 4.60 Trillion, about 60.00% of GDP (2017). The trajectory in borrowing has triggered an intense public debate over the country's debt sustainability given the persistently high fiscal deficit. Nonetheless, calls for fiscal consolidation have gained traction especially from lenders and academics.

To this, Treasury will in a supplementary budget propose KES 18.00Bn and KES 60.00Bn spending cuts for the County and National governments, respectively. According to the IMF, such adjustments will help reduce the fiscal deficit to 7.20% of GDP in 2017/18 from 8.80% a year earlier. During the recently concluded Article IV consultation by the international lender, the government committed to such fiscal adjustments in support of its request for a six-months extension of the $1.5Bn standby facility.

While consolidation may seem like a fiscal imperative at the moment, potential for a backlash from parliament and county leadership threatens such an undertaking. Given the negative impact on growth, any adjustments need to be very tactical to avoid aggravating the slowdown. A combination of both revenue collection reforms and expenditure rationalisation may help bring down the deficit without making the process painful for the public.

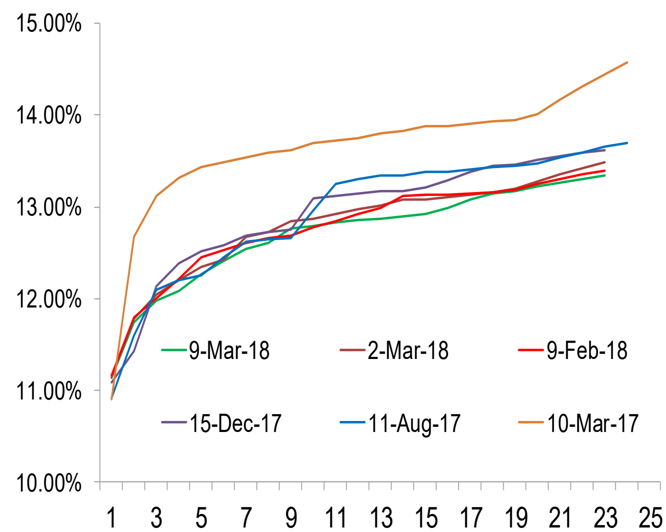
A review of interest rate controls could see stronger signals of lower interest rates by the MPC

A review of the current interest rate framework could be imminent after the government committed to modifying the interest rate controls as part of the IMF's 'requirements' for an extension of the precautionary facility set to expire on March 13th 2018. The extent of the review remains uncertain.

Indicative Rates	Previous	Current	Change bps
Avg Overnight	4.778%	4.568%	-20.93
91-Day T-bill	8.029%	8.026%	-0.30
182-Day T-bill	10.393%	10.385%	-0.80
364-Day T-bill	11.135%	11.128%	-0.70
Inflation	4.83%	4.46%	37.00
USD/KES	101.32	101.15	-0.17%

Source: Central Bank of Kenya

NSE yield curve



Source: Nairobi Securities Exchange

Government maturities and coupon payments

Month	KES (Bn)
12-Mar-18	41.89
19-Mar-18	27.29
26-Mar-18	18.60
April-2018	114.75
May-2018	118.86
June-2018	94.52
New Cumulative Borrowing	178.31

Source: Bloomberg

So far, there is a proposal by the Parliament Select Committee on Budget to abolish the floor (70.00% of CBR). Potentially better margins for commercial banks as a result could incentivize banks to increase lending to the private sector, although limitations to risk pricing by the ceiling could still lock out some segments of the population from the credit system.

The possibility of detaching lending rates from the CBR could see stronger signals of lower interest rates from the MPC when it meets next Monday. The impact on the yield curve will be insignificant although any strong indications of a total abolition of the caps could see the curve ease further on augmented expectations of lower interest rates rise, at least in the short term. A low interest rate bias by the policy setting committee will be supported by a benign inflation outlook and recent currency stability.

Sustained liquidity boosts subscription for Treasuries as positive sentiments drive shilling higher

Easy money market liquidity continues to improve the demand for Treasuries. Last week's Treasury bill auction registered a 154.97% subscription. The sale attracted KES 37.19Bn in bids against the offer of KES 24.00Bn. The fiscal agent accepted KES 32.66Bn at yields of 8.026% (Down 0.30bps), 10.385% (Down 0.80bps) and 11.128% (Down 0.70bps) for the 91, 182 and 364 day papers respectively. The bias remains on the longer end in line with the low interest rate expectations.

Meanwhile, the Kenya shilling continued to strength against its US counterpart. The gains have been driven by the lethargy in demand, improved investor sentiments, particularly now with reduced political risks and steady flows into the market.

Additionally, the government's request for a six-month extension of the US$1.50Bn stand-by credit facility with the IMF could herald some future stability for the local unit.

Weekly T-bill Auction Results

	91-Day	182-Day	364-Day
Yield	8.026%	10.385%	11.128%
Change (Bps)	-0.30	-0.80	-0.70
Amnt Offered (Bn)	4.00	10.00	10.00
Bids Received (Bn)	3.84	14.97	18.38
Performance (%)	96.12	149.68	183.79
Amount Accepted	3.17	11.56	17.93
Bid Cover	1.21	1.30	1.03
Redemption (Bn)	4.97	20.77	16.11
New borrowing (Bn)	-1.80	9.21	1.82

Source: Central Bank of Kenya

Regional Equities Market

	02.03.18	09.03.18	Wow
NSE- 20	3,755.95	3,720.21	-0.95%
NASI	181.26	180.60	-0.36%
NSE- 25	4,587.62	4,609.43	0.48%
USE ASI	2,078.81	2,094.76	0.77%
DSEI	2,405.45	2,362.08	-1.80%
TSI	3,893.73	3,893.73	0.00%
RSE ALSI	132.97	133.31	0.26%

Source: Regional Stock Exchanges

Equities market registers mixed performance

Performance in the equities market was mixed. The NSE-20 and NASI declined by 0.95% and 0.36% respectively while the NSE-25 advanced by 0.48%.

Reduced activity resulted in a 19.17% decline in turnover to KES 4.68Bn from KES 5.79Bn in the previous week. Local investors dominated the market for the second consecutive week accounting for 57.68% of the total traded value. Foreigners remained net sellers withdrawing US$ 2.51Mn compared to US$ 2.26Mn in the previous week.

Regional Market

	UGANDA		TANZANIA		RWANDA	
Period to (2018)	**Feb 15th**	**Mar 01st**	**Feb 23rd**	**Mar 09th**	**Mar 01st**	**Mar 09th**
91 Days T-Bill	8.685%	8.676%	3.40%	2.78%	5.870%	5.800%
182 Days T-Bill	8.900%	8.929%	3.69%	3.46%	7.152%	7.035%
364 Days T-Bill	9.327%	9.435%	6.25%	5.83%	7.958%	7.908%
Interbank O/N	6.40%	7.18%	1.64%	1.51%	5.50%	5.50%
CBR/CRR/ Key Repo Rate	9.00%	9.00%	8.00%	8.00%	5.50	5.50

Source: Bank of Uganda, Bank of Tanzania, National Bank of Rwanda

Uganda

The shilling weakened marginally during the week on account of a pick up in demand for the greenback from interbank players and importers. Even so, end week dollar flows from the agricultural sector coupled with the Central Bank's liquidity operations offered some support to the local currency which closed at 3645/3655 levels against the US dollar. The local currency is expected to trade within similar ranges though with a weakening bias given the expected increase in dollar demand.

Meanwhile, ample liquidity conditions continued to typify the interbank market with overnight rates oscillating in the 7.50% to 8.50% range in the week. There was no Treasury auction in the week.

This week, the fiscal agent will conduct a Treasury bill auction seeking to raise UGX 160Bn from the market. It is expected that yields could continue to exhibit an uptrend reflecting prospects of higher local borrowing by the government.

Tanzania

The shilling remained unchanged in the 2249/2259 range against the US dollar as activity on demand and supply counters balanced out. The Central Bank continues to actively participate in the foreign exchange market in an effort to offset any FX volatility. The local currency is expected to remain within familiar trading ranges in the week though risks from the policy fluidity could weigh on.

Meanwhile, liquidity conditions remain quite ample. Overnight cost of funds oscillated in the 1.46% to 1.51% range during the week. The Central Bank rid the market of TZS 150Bn in excess liquidity after receiving bids amounting to TZS 315Bn at 1.00%.

The week's Treasury bill auction was oversubscribed with the fiscal agent receiving TZS 265.28Bn against the TZS 168Bn on offer. The Central Bank accepted the TZS 168Bn it sought with yields declining to 2.78% (Down 62bps), 3.46% (Down 23bps) and 5.83% (Down 42bps) for the 91, 182 and 364 day papers respectively.

Kenya Government Debt Maturities (KES Bn)

Maturity	Issuer	Amount Outstanding	Principal	Interest
12-Mar-18	Treasury Bill	41.89	41.89	
19-Mar-18	Treasury Bill	27.29	27.29	
26-Mar-18	Treasury Bill	18.61	18.61	
	Treasury Bond-Coupon Payments			15.10
MARCH 2018		**111.64**	**111.64**	**15.10**
2-Apr-18	Treasury Bill	17.29	17.29	
9-Apr-18	Treasury Bill	17.70	17.70	
16-Apr-18	Treasury Bill	19.44	19.44	
23-Apr-18	Treasury Bill	25.51	25.51	
23-Apr-18	**FXD1/2013/5**	20.17	20.17	
30-Apr-18	Treasury Bill	13.33	13.33	
	Treasury Bond-Coupon Payments			17.26
APRIL 2018		**113.45**	**113.45**	**17.26**
7-May-18	Treasury Bill	18.81	18.81	
14-May-18	Treasury Bill	17.94	17.94	
21-May-18	Treasury Bill	23.91	23.91	
21-May-18	**FXD2/2016/2**	58.64	58.64	
28-May-18	Treasury Bill	21.64	21.64	
	Treasury Bond-Coupon Payments			17.01
MAY 2018		**140.94**	**140.94**	**17.01**
4-Jun-18	Treasury Bill	21.46	21.46	
11-Jun-18	Treasury Bill	13.84	13.84	
18-Jun-18	Treasury Bill	14.01	14.01	
25-Jun-18	Treasury Bill	17.28	17.28	
25-Jun-18	**FXD2/2013/5**	26.43	26.43	
	Treasury Bond-Coupon Payments			19.96
JUNE 2018		**93.02**	**93.02**	**19.96**
2-Jul-18	Treasury Bill	12.62	12.62	
9-Jul-18	Treasury Bill	15.63	15.63	
16-Jul-18	Treasury Bill	11.95	11.95	
16-Jul-18	**FXD2/2008/10**	13.50	13.50	
23-Jul-18	Treasury Bill	8.47	8.47	
30-Jul-17	Treasury Bill	20.79	20.79	
	Treasury Bond-Coupon Payments			9.48
JULY 2018		**82.96**	**82.96**	**9.48**