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Trustee and Investment Services LTD



**National
Bank**

A Subsidiary of KCB Group PLC

MONTHLY MARKET REPORT AUGUST 2022



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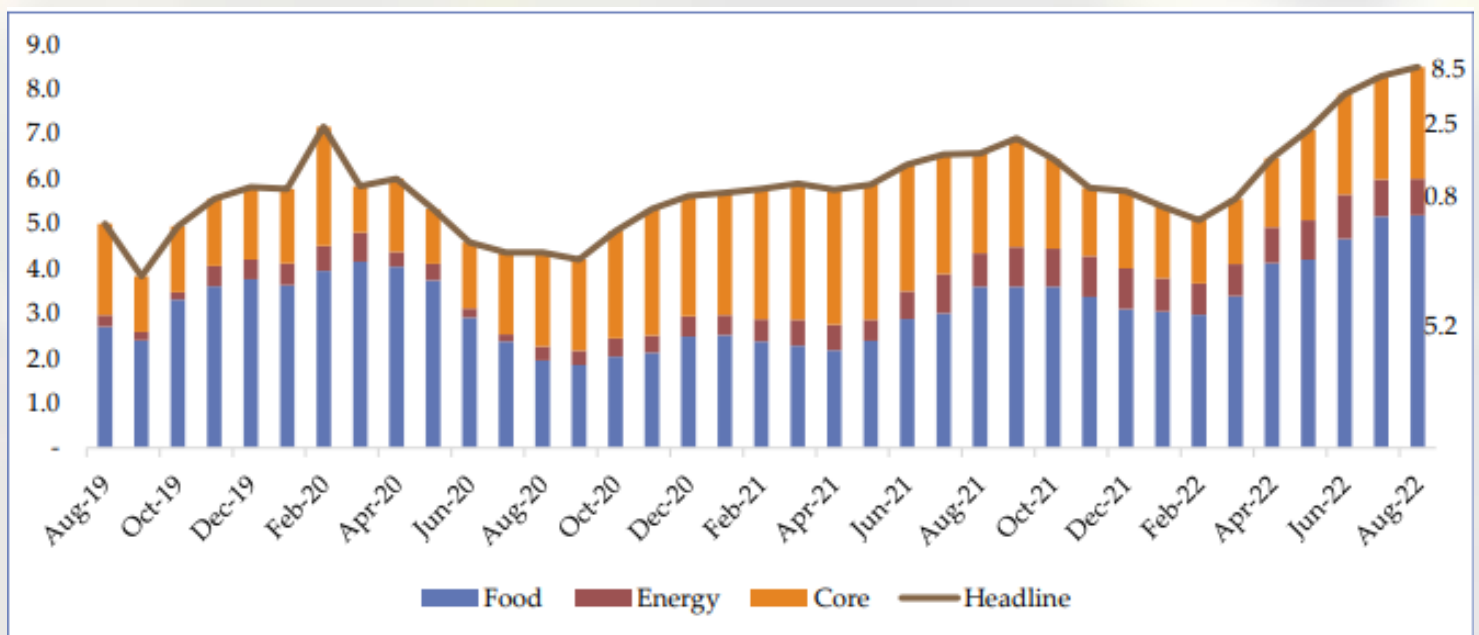
MACROECONOMIC HIGHLIGHTS

INFLATION:

The overall year on year inflation rate as measured by the Consumer Price Index (CPI) was 8.5% in August 2022, exceeding the National Treasury's target of 2.5%-7.5%. The rise in inflation was mainly due to an increase in prices of commodities under food and non-alcoholic beverages (15.3%); transport (7.6%) and housing, water, electricity, gas and other fuels (5.6%) between August 2021 and August 2022. These three divisions account for over 57% of the weights of the 13 broad categories. The prices of commodities under furnishings, household equipment and routine household maintenance recorded a 10.3% increase during the review period.

Month on month, the CPI increased by 0.4% from an index of 125.05 in July 2022 to 125.58 in August 2022. The month-on-month Food and Non-Alcoholic Beverages Index increased by 0.5% between July 2022 and August 2022.

The charts below provide details on Inflation Evolution (%):



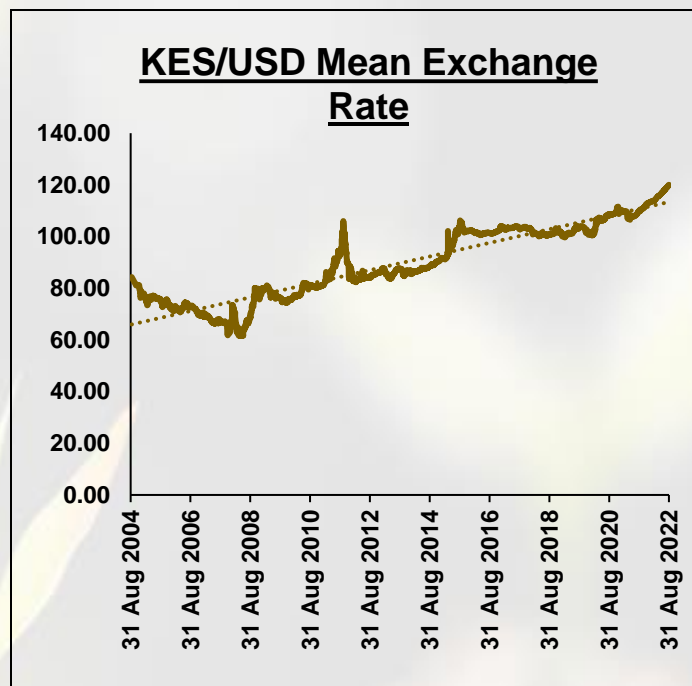
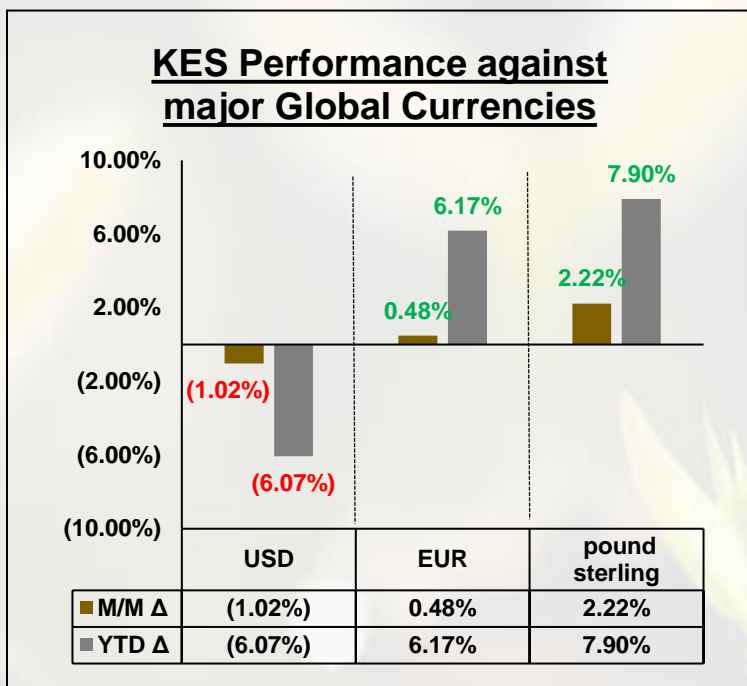
Inflation Outlook: Risks to the outlook remain tilted to the upside in the short term driven by rise in food prices which remains the biggest contributor to inflation. The rise is partly due to the rise in global food prices as well as poor rains and higher input costs.

CURRENCY PERFORMANCE:

The Kenya Shilling depreciated by 1.02% against the US Dollar, to close the month at KES 120.01, from KES 118.80 recorded at the end of July 2022. The performance was on the back of a stronger greenback, coupled with increased local demand. The US dollar has been one of the few beneficiaries this year of a market battered by geopolitical fears which saw investors ditch riskier investments and seek shelter in assets that they perceive as more secure. The strengthening of the dollar has also been partly attributable to the FED ramping up to battle inflation by raising interest rates.

On a YTD basis, the shilling has depreciated by 6.07% against the US dollar but has gained by 6.17% and 7.90% against the Euro and Pound Sterling, respectively.

The charts below provide details on currency performance during the month:



Currency Outlook: Pressure on the shilling is expected to sustain largely attributable to the strengthening of the US dollar, coupled with a high oil imports bill following the continued rise in global crude oil prices. Strong remittances inflows continue to support the current account and the stability of the exchange rate. The US remains the largest source of remittances into Kenya, accounting for 58% in July 2022. The usable foreign exchange reserves remained adequate at USD 7,608 million (4.39 months of import cover) as of August 25th and is above CBK’s statutory requirement to endeavor to maintain at least 4 months of import cover. This is expected to continue providing a buffer against any short-term shocks in the foreign exchange market.

FIXED INCOME HIGHLIGHTS

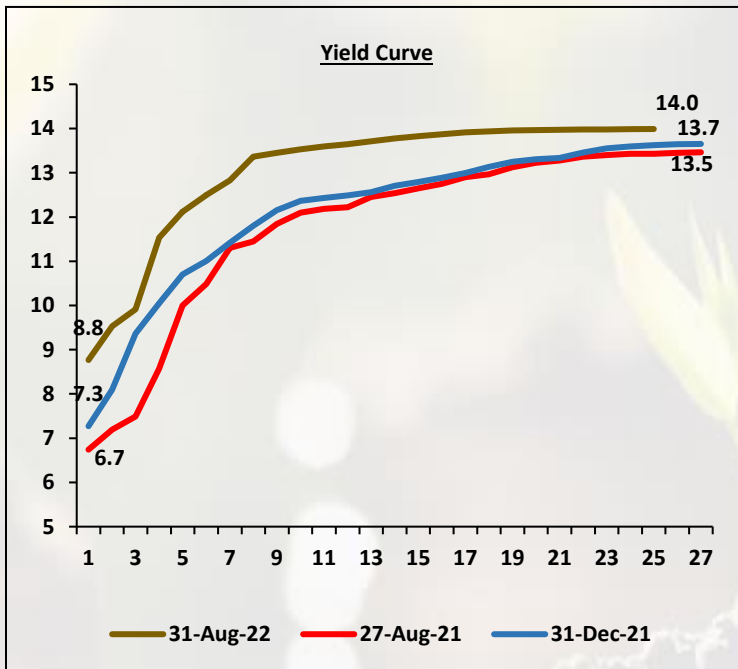
The yields on the 91-day, 182-day and 364-day treasury bills averaged 8.57%, 9.45% and 9.92% respectively in August 2022 compared to 8.28%, 9.34% and 9.97% respectively in July 2022. The yields for 91- day and 182-day tenors continued to increase with notable under subscriptions for 182-day and 364-day bills.

In the Primary Bond Market, The Central Bank of Kenya (CBK) reopened FXD1/2022/03, FXD2/2019/10 and FXD1/2021/20 treasury bonds with an aim of raising KES 50.0 BN. The issues recorded a total undersubscription of 98.25%. The government accepted KES 38.53 bn of the KES 49.13 bn worth of bids received, translating to an acceptance rate of 78.42% on aggregate.

The table below provides more details on the bond issued during the month:

Bond Auctioned	Value Date	Due Date	Effective Tenor to Maturity (Years)	Coupon	Amount offered (KES bn)	Total bids (KES bn)	Actual Amount Raised (KES bn)	Average Accepted Yield	Subscription Rate	Acceptance Rate
FXD1/2022/03	22/08/2022	07/04/2025	2.6	11.77%				12.45%		
FXD2/2019/10	22/08/2022	02/04/2029	6.6	12.30%	50.00	49.13	38.53	13.88%	98.25%	78.42%
FXD1/2021/20	22/08/2022	22/07/2041	19.0	13.44%				13.96%		
Total					50.00	49.13	38.53		98.25%	78.42%

Yields remained elevated in line with market expectations driven by the persistence of high inflation, tightening monetary policy action and subsequent risk aversion precipitated by the electioneering period. Secondary bonds turnover rose by 12.25% to KES 68.39 bn, from KES 60.93 bn recorded in July 2022.



Tenor	Jan-22	Jul-22	Aug-22	Δ YTD	Δ M-O-M
91-day	7.3%	8.4%	8.8%	1.5%	0.4%
1yr	9.4%	9.9%	9.9%	0.5%	(0.0%)
2Yr	10.1%	11.5%	11.5%	1.5%	0.1%
5Yr	11.4%	12.7%	12.8%	1.4%	0.1%
10Yr	12.5%	13.7%	13.6%	1.2%	(0.0%)
15Yr	13.0%	13.9%	13.9%	0.9%	(0.0%)
20Yr	13.5%	14.0%	14.0%	0.5%	(0.1%)
23Yr	13.6%	14.1%	14.0%	0.4%	(0.1%)

Fixed Income Outlook: Despite the continued improvement in revenue collections, rising expenditure, coupled with debt service requirements could sustain wide deficits and as such we expect Interest rates to continue picking up as debt pressure builds following increased fiscal needs in the medium-term, coupled with recent raising of the Central Bank Rate (CBR) from 7.00% to 7.50%.

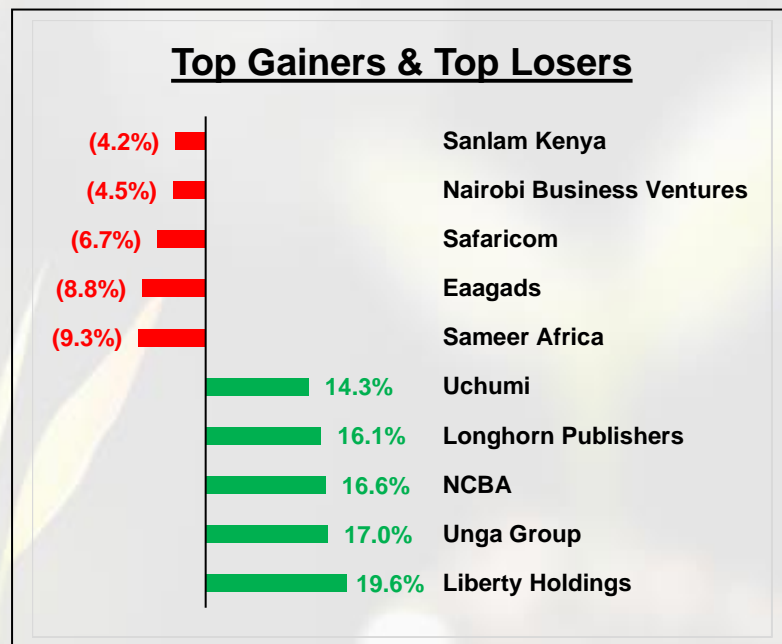
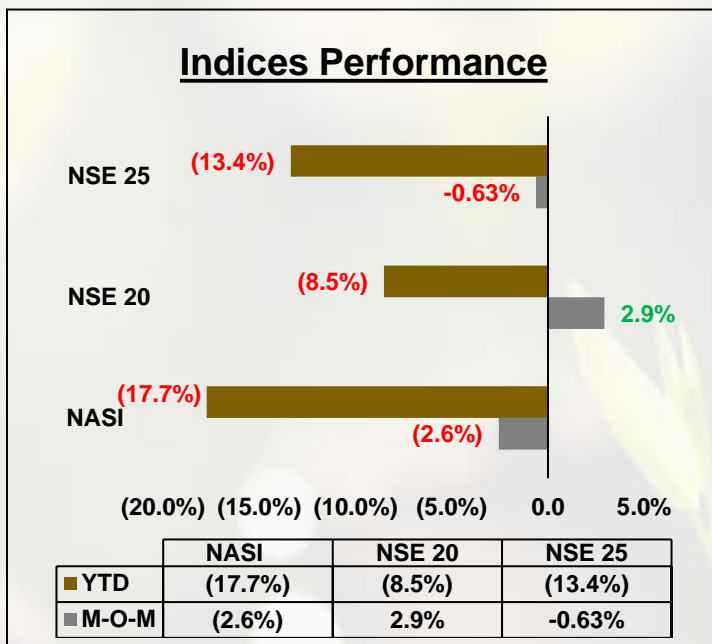
Prospects of raising funds in the external credit markets have dimmed due to elevated yields in emerging markets following tightened monetary policy in a number of advanced economies to counter inflation (The Eurobond maturing in 2024 for instance closed the month at a yield of 16.9%, up from 4.4% in January). This has further anchored appetite for local deficit financing. Even then, the ability for local borrowing to plug revenue deficits amid the current levels of inflation suggests that any borrowing will attract a hefty premium. **Based on the backdrop of the current fixed income market outlook we maintain our preference for medium term papers to mitigate the “duration risk” whilst maintaining adequate real return given the rising inflation.**

EQUITIES MARKET PERFORMANCE

The equities market recorded mixed performance in August, as depicted by the key indices, which saw NASI, and NSE 25 shed 2.55% and 0.63%, respectively. NSE 20 on the other hand gained 2.93%. The performance was driven by losses recorded in large cap counters such as Safaricom (-6.68%), KCB Group (-0.73%) and E.A Breweries (-2.74%). The losses were mitigated by gains in other counters such as NCBA (16.63%), Cooperative Bank (4.20%) and ABSA (7.24%).

Equities turnover declined by 33.30% in August 2022 to KES 5.33 bn from KES 8.00 bn in July. overall foreign activity closed with a net outflow of KES 1.66 bn a decline from KES 2.97 bn in July. The bourse saw Safaricom record a turnover of KES 2.81 bn, representing 54.61% of the month’s total turnover, a rise from 43.02% in July. Liberty Holdings was the month’s top gainer having appreciated by 19.64% to close at KES 6.70 while Sameer Africa was the month’s top loser, shedding 9.32% to end the month at KES 3.60.

The charts below show the equities market performance during the period of review:



Equities Outlook: We expect to see a rebound in the short term as the market corrects from the negative investment sentiment that was precipitated by the elections. We however remain cognizant of the risks in the medium term, on account of US interest rates hikes that have seen capital outflows in emerging markets.

Pockets of value exist as the market is currently trading at a Price to Earnings (P/E) multiple of 7.3x which presents a discount in comparison to the historical average of 12.7x, and a dividend yield of 5.7%, above the historical average of 4.1%. This presents a suitable opportunity to buy the dip for future capital appreciation. We believe investors should take up positions in value stocks trading at discounts to their intrinsic value with a bias towards the telecommunication and banking sectors which we believe will be well-positioned to rebound in a higher interest rate environment.

POST-ELECTION OUTLOOK

Coming out of peaceful electioneering period and with the formation of a new Government, the market is expected to be on a recovery path from the negative market perception which had seen capital flight as well as a wait and see approach by most investors.

We believe the below flashpoints will be on investors' radar with regards to the outlook.

- i. Inflationary pressure: Elevated inflation has been a general theme during the electioneering period driven by rise in food prices and partly due to elevated global crude oil prices. This has been despite a raft of measures being put in place inclusive of subsidies to tackle the runaway inflation. In order to maintain an adequate positive real rate of return (adjusted return for the effects of inflation), we expect investors to be keen on how the new Government will handle inflation which is currently above the National Treasury's target range of 2.5%-7.5%.
- ii. Interest Rate Risk and Debt Pressure: Kenya's fiscal position has been a longstanding source of vulnerability. In the short to medium term Kenya faces rising borrowing costs as the U.S. Federal Reserve and other major central banks hike interest rates to tame inflation. This has made investments in the U.S. more attractive on a risk-return basis as rates rise, consequently enhancing capital flight from emerging markets due to the narrowing spreads of hard-currency debt over safe-haven U.S. Treasuries. As such fiscal consolidation is expected to be on the forefront in order to reduce debt pressure in the current high cost of credit environment.



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