Innovative Thinking

Q3 2023
MARKET REPORT

Insurance | Financial | Investment | Risk | Pension | Health | I.T

ACTUARIAL SERVICES EAST AFRICA LIMITED

KENYAN MARKET PERFORMANCE

MACROECONOMIC REVIEW

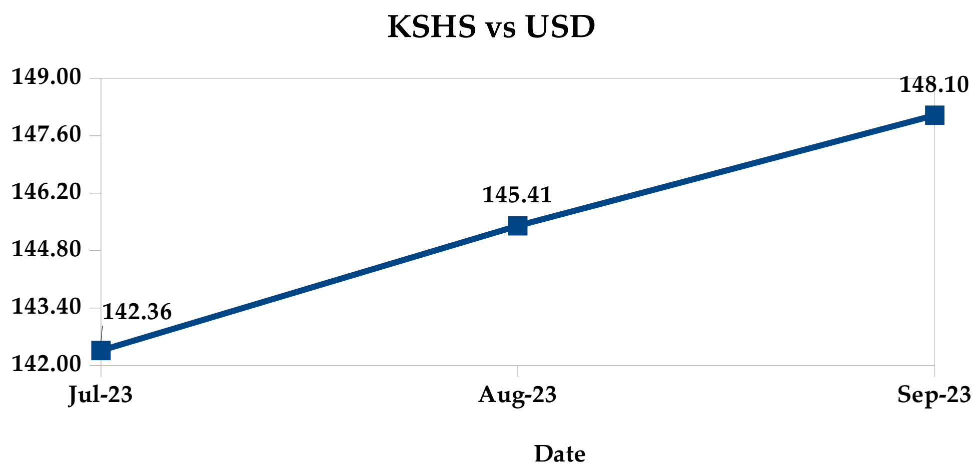
GDP

Kenya's economy grew by 5.4% in Q2 2023, up from 5.2% in Q1, according to the Kenya National Bureau of Statistics (KNBS). The rebound in the agricultural sector driven by favorable weather conditions, was the main driver of growth.

Kenya's GDP growth outlook for 2023 is positive, with IMF projecting 5.0%, a downward revision from 5.3%, and the Central Bank of Kenya (CBK) forecasting 5.5%, driven by the services and agriculture sectors. Manufacturing is expected to remain sluggish but the government's initiatives such as the value chains budgeting agenda and affordable housing program could potentially reverse this trend.

Currency

The Shilling faced a significant depreciation against the US dollar by 5.39% quarter-on-quarter and 19.99% year-to-date, exchanging at Kshs 148.10 at the end of Q3 2023. The observed depreciation is attributed to a persistent dollar shortage exacerbated by the greenback's strength and appeal amid rising interest rates, prompting capital flight from emerging markets like Kenya. Banks are capitalizing on the heightened demand for the Dollars and forex market volatility, resulting in increased profit margins from foreign currency transactions due to wider spreads.

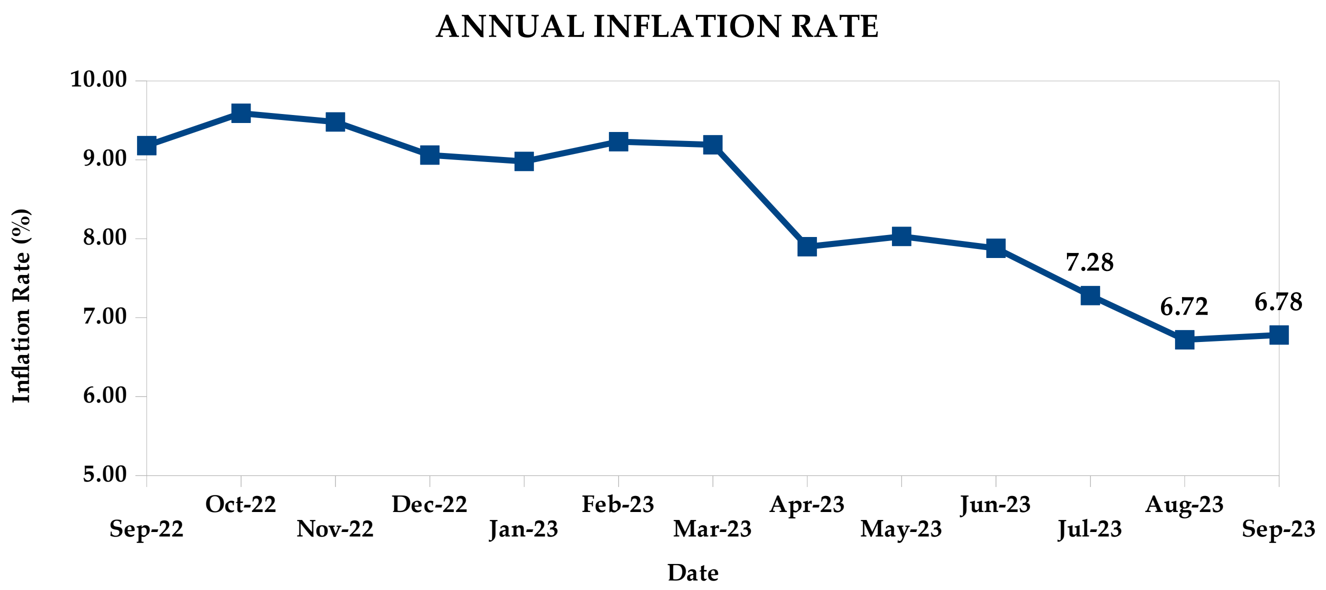


The usable foreign exchange reserves stood at USD 7,462 million at the beginning of the quarter, equivalent to 4.08 months of import cover, meeting CBK's statutory requirement but falling short of EAC's convergence criteria. However, the reserves consistently dipped below the 4- and 4.5-months of import cover threshold from mid-August through the end of the quarter. This continues to exert downward pressure on the Shilling, particularly as the country prepares for the fast-approaching dollar-denominated Eurobond repayment. The Shilling is expected to remain under pressure in the next quarter, due to rising interest rates in the US and high demand for the green.

The government remains committed to addressing the Shilling pressure and alleviating foreign currency strain through strategic actions including the renegotiation of state-backed fuel supply agreements with Saudi Aramco, Emirates and Abu Dhabi. These renegotiations extend the credit terms for an additional year, spanning through 2024. Furthermore, the government has successfully reworked freight and premium expenses, along with introducing credit terms that allow payments in the local currency.

Inflation

Inflation declined during the quarter, averaging 6.93%, well within the central bank's target range of 2.5% to 7.5%. The decline was driven by lower food, gas and electricity prices in the first two months of the quarter. However, inflation slightly inclined at the end of the quarter due to elevated fuel and sugar prices, which pushed the transport index and food inflation slightly higher.



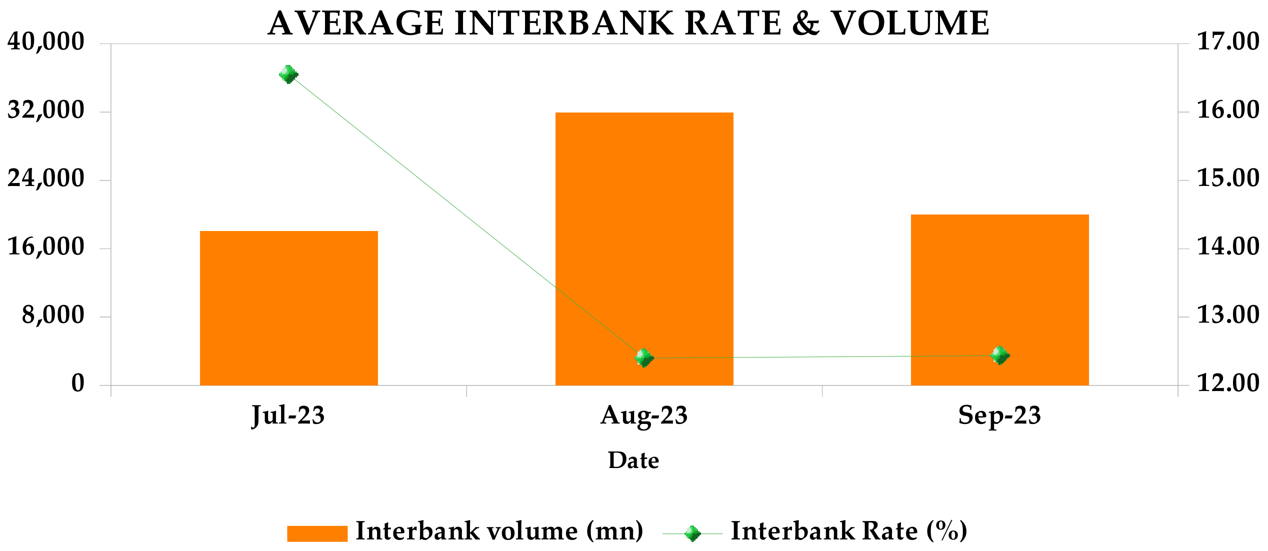
The Monetary Policy Committee (MPC) retained the Central Bank Rate (CBR) at 10.50% during the quarter, including at its most recent meeting on 3rd October 2023. The MPC noted that inflation was well within the target band and that the impact of the tightening of monetary policy in June 2023 to anchor inflationary expectations was still being transmitted in the economy.

Inflation is generally expected to remain well within the central bank's target range in the next quarter, supported by favorable weather conditions that are likely to bring down the food index. However, there is general concern about the trajectory of fuel prices, which could pose an upside risk to inflation.

Liquidity

Liquidity in the money markets increased during the quarter, as government payments more than offset tax remittances. The interbank rate declined from 16.55% at the beginning of the quarter to 12.44% at the end of the quarter, but reached a historical high of 17.4% at the start of August.

The average interbank rate rose to 11.85% in Q3 2023, up from 9.22% in Q2 2023. The volume of interbank transactions edged slightly higher from Kshs 18.08 billion at the start of the quarter to Kshs 20.0 billion at the end of the quarter. Commercial banks' excess reserves increased from Kshs 18.1 billion at the start of the quarter to Kshs 19.3 billion at the end of the quarter.



PMI

The average PMI in Q3 2023 was 48.0 slightly down from 48.1 in Q1 2023. The PMI fell to 45.5 in July, due to continued deterioration in the private sector and severe inflationary pressures. It rebounded to 50.6 in August signaling a renewed improvement after six months of contraction, with output, new orders and job creation recovering. However, the PMI dipped again to 47.8 in September, indicating intense cost pressures and a drop in customer demand. Despite the decline, firms remained somewhat optimistic, albeit still weak in a historical context.

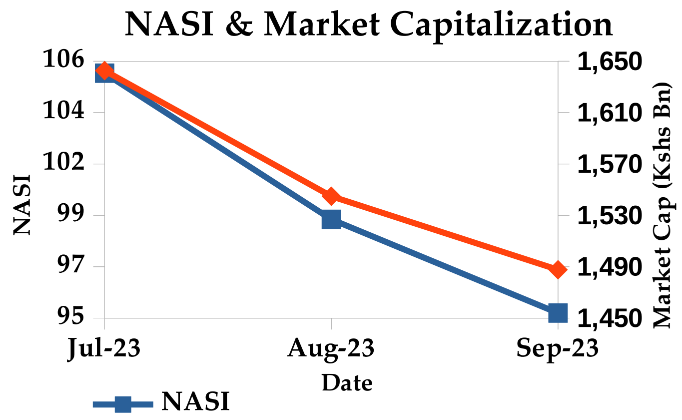
EQUITIES

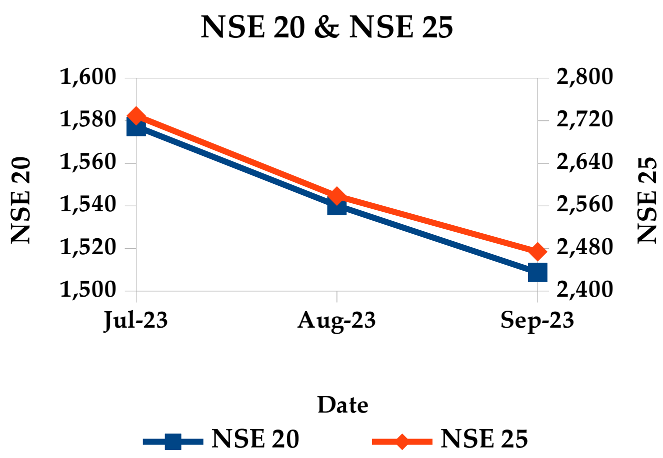
Despite the bourse reporting higher dividend returns, the NASI, NSE 20 and NSE 25 contracted by 11.01%, 4.20% and 9.35% respectively in Q3 2023, primarily due to foreign investors fleeing to safer havens in their local markets. Most large-cap stocks lost during the quarter, with KCB, Safaricom and EABL recording double-digit losses of 28.84%, 16.57% and 15.48% respectively. However, some large-cap stocks, such as Stanbic, Standard Chartered and ABSA outperformed the market with substantial gains.

Market capitalization continued its downward trend in Q3 2023, declining by 10.72% to close at Kshs 1.67 trillion. Total shares traded and equity turnover increased by 38.28% and 11.17% respectively to Kshs 1.06 trillion and Kshs 15.99 trillion, but the number of deals decreased from 73,777 in the previous quarter to 66,877.

Top 5 Gainers	QTD Change
Kenya Orchards	30.00%
Stanlib FAHARI I-REIT	22.52%
E.A Portland Cement	22.52%
E.A Cables	18.99%
Carbacid Investments	15.52%

Top 5 Losers	QTD Change
KCB	-28.84%
Trans-Century	-24.24%
Standard Group	-21.83%
Sasini	-19.67%
Crown Paints	-18.70%





Foreign investor flight persisted in Q3 2023, with net outflows totaling Kshs 2.94 billion, from Kshs 1.33 billion in the previous quarter. Safaricom recorded the highest foreign investor turnover, accounting for a massive 61.29% of the total, followed by Equity with 20.39% and ABSA with 7.20%. Given the rising interest rates, strengthening US dollar and the global economic slowdown, this flight is most likely the result of investors seeking more stable and attractive returns in their local markets.

Foreign Investor Activity		
Month	Inflows (Kshs. 'Mn')	Outflows (Kshs. 'Mn')
July	1,707.46	4,717.17
August	2,251.88	836.67
September	1,780.83	3,126.70

Top 5 Performers by Market Turnover		
Counter	Turnover (Kshs. 'Mn')	% of Total Market Turnover
Safaricom	8,408.81	48.90%
Equity	2,828.23	16.45%
ABSA	1,368.36	7.96%
KCB	1,011.53	5.88%
BAT	510.37	2.97%

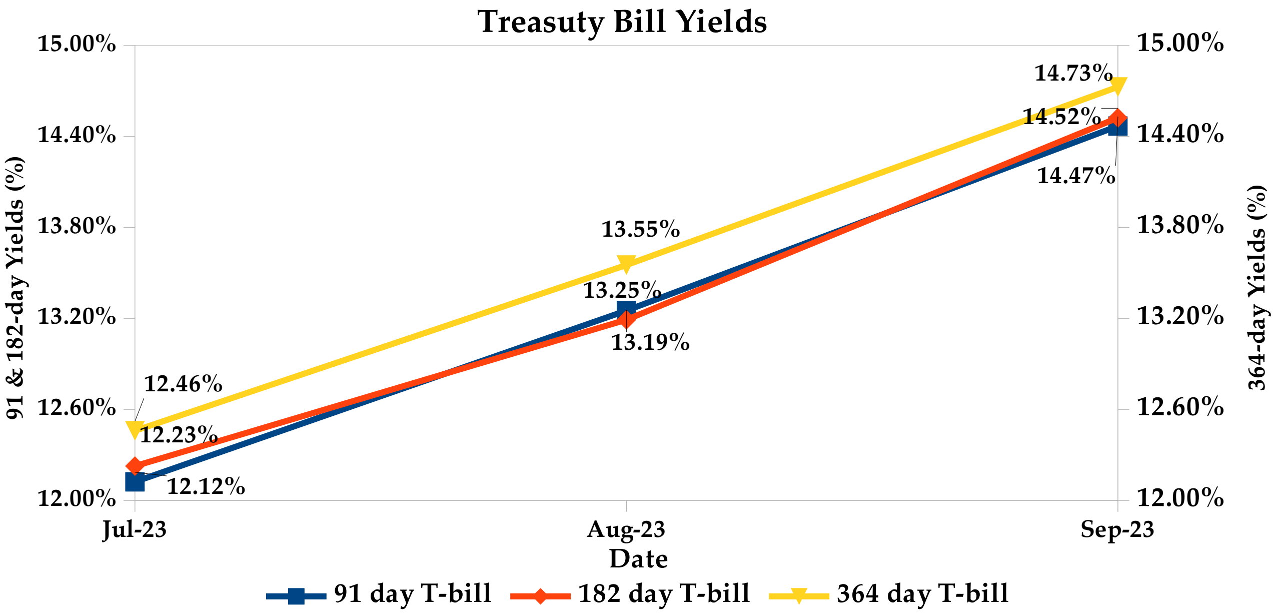
Major Highlights Within The Equities Market

- NSE launched two new market indices; the NSE 10 Share Index (N10) and the NSE Bond Index (NSE-BI).
- Safaricom increased the M-PESA account and daily transaction limit to Kshs 500,000, and the per-transaction limit to Kshs 250,000, following approval from CBK.
- CMA approved the conversion of ILAM Fahari I-REIT from an unrestricted to restricted I-REIT, and suspended trading of units from 6th to 25th October 2023 to facilitate reconciliation.
- CMA issued new guidelines requiring online foreign exchange brokers to improve their disclosure mechanisms, promote transparency and protect investors.
- NCBA Group announced plans to buy 66.67% of AIG Kenya Insurance Company Limited which would give it full ownership, as it already holds a 33.33% stake.

FIXED INCOME

Treasury Bills

The overall average subscription rate for the third quarter came in at 114.59%, an increase from 110.83% recorded in Q2 2023. Investors' preference for the shorter-term paper prevailed in Q3 at an average subscription rate of 576.43% compared to 521.12% in Q2 , in a bid to hedge against duration risk and on the appealing return compensation. Yields rose by 24.67%, 22.23% and 20.51% to settle at an average 13.39%, 13.43% and 13.70% for the 91-day, 182-day and 364-day papers respectively.

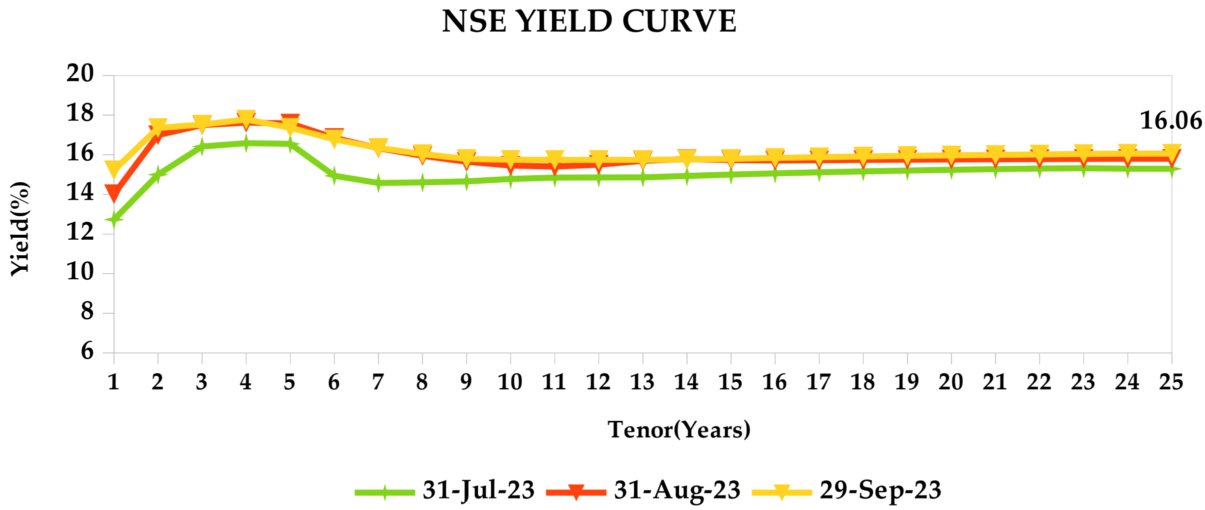


Treasury Bonds

In the primary market, CBK sought to raise Kshs 171 billion from FXD1/2023/2, FXD1/2023/5 and FXD1/2016/10 Treasury bond sales, up from Kshs 135 billion in Q2 2023. The average subscription rate was 119.43%, down from 148.04% in Q2 2023. This may be due to the absence of an infrastructure bond, which is popular with investors due to its tax-free status. CBK received Kshs 209.44 billion in bids, but only accepted Kshs 148.87 billion, marking an average acceptance rate of 74.49%, down from 99.08% in the preceding quarter.

The acceptance rate for the first tap sale in August was the lowest for the quarter, as investors were locked out due to their aggressive bidding for higher returns. However, CBK reopened the auction, giving investors another opportunity to participate and the acceptance rate was close to 100%. The average yield rose from 14.52% in Q2 2023 to 17.25% in Q3, as investors took advantage of the government's increasing borrowing appetite to demand higher returns to compensate for a weaker Shilling and hedge against inflation. This trend is expected to continue into the next quarter.

The secondary market saw increased demand for bond offers, with total turnover rising 36.73%, from Kshs 152.54 billion in the second quarter to Kshs 208.56 billion in the third quarter. Total bond deals soared 13.78% from 6,234 in Q2 to 7,093 in Q3. Yields on government securities in the secondary market increased during the quarter. We anticipate a surge in secondary market activity in the next quarter, driven by the upward trajectory of interest rates in primary auctions, which will create opportunities for strategic trade-offs.



Eurobonds

In the international market, yields on Kenya's Eurobonds rose by an average 274 basis points Q3 2023, as international investors expressed concerns about the country's external financing constraints. The rise in yields was attributed to the negative outlooks from major credit rating agencies including S&P, Moody's and Fitch which cited relatively high government debt, high funding requirements including the fast approaching $2 billion Eurobond maturity in 2024, weakening foreign exchange reserves, rising financing costs, tax hikes and the fiscal trajectory. The dollar shortage and depreciating Shilling exacerbated the rise in Eurobond yields.

Yields on Kenya's Eurobonds are expected to continue to rise until investors are more confident in the country's ability to manage its finances, particularly its ability to finance the upcoming Eurobond maturity.

Bond	QTD Change
2014 10-Year Issue	5.81%
2018 10-Year Issue	2.31%
2018 30-Year Issue	1.43%
2019 7-Year Issue	3.10%
2019 12-Year Issue	1.73%
2021 13-Year Issue	2.03%

Major Highlights In The Fixed Income Market:

- CMA approved Kenya's first-ever Sukuk bond issuance; Linzi Sukuk, issued by Linzi Finco Trust, in support of the affordable housing agenda.
- CBK launched the DhowCSD, a digital trading platform that streamlines local and foreign investor participation in government securities.
- Fitch Ratings revised Kenya's long-term foreign-currency Issuer Default Rating (IDR) outlook from Stable to Negative, while affirming the IDR at 'B'.
- IMF disbursed $415.4 million under the EFF/ECF agreement, including $110.3 million from access augmentation; an extension of the arrangement from 38 months to 48 months, and approved a $551.4 million 20-month arrangement under the RSF.
- CBK approved key measures to improve monetary policy implementation and transmission, including an interbank interest rate corridor around the CBR set at CBR ± 2.5% and changes to the terms and conditions of the CBK Discount (Overnight) Window facility.

GLOBAL MARKET PERFORMANCE

MACROECONOMIC REVIEW

The IMF's World Economic Outlook (WEO) July 2023 update projects global growth to fall from 3.5% in 2022 to 3.0% in both 2023 and 2024. This forecast is modestly higher than the IMF's April update, but it remains weak by historical standards. Despite the global recovery to pre-pandemic levels and the slowdown in Russia's invasion of Ukraine, inflation remains high and continues to erode household purchasing power. Central banks are raising interest rates to combat inflation, but this is also raising borrowing costs and constraining economic activity.

However, the recent resolution of the US debt ceiling tensions and the swift and strong action by authorities in March 2023 to contain turbulence in US and Swiss banks have eased global financial conditions and reduced the risk of a sharp economic downturn. Nonetheless, central banks' tight monetary policies continue to restrict the availability of credit.

Advanced economies are leading the slowdown in global growth from 2022 to 2023, with weaker manufacturing and other country-specific factors offsetting stronger services activity. In emerging markets and developing economies (EMDEs), the growth outlook is broadly stable for 2023 and 2024, but with significant variation across regions. Rising borrowing costs in advanced economies could lead to financial crises in more vulnerable EMDEs. In low-income countries, fiscal positions are increasingly precarious.

Global inflation is expected to fall from 8.7% in 2022 to 6.8% in 2023 and 5.2% in 2024. This is a downward revision of 7.0% for 2023, largely due to subdued inflation in China. However, the forecast for inflation in 2024 has been revised upwards reflecting higher-than-expected inflation. Core inflation, which excludes food and energy prices, is generally declining more slowly than overall inflation.

COMMODITIES

Crude Oil

ICE Brent and Crude Oil WTI futures prices rose significantly in the Q3 2023, inching closer to $100 a barrel. Brent crude futures rose from $74.90 to $95.31, a 27.25% quarter-on-quarter gain and a 17.77% year-to-date gain. WTI crude futures rose from $70.64 to $90.79, a 28.52% quarter-on-quarter gain and a 16.09% year-to-date gain. After a persistent decreasing trend in the first half of the year, this trend reversal was prompted by OPEC's production curbs, which compressed global crude supply. In addition, Russia's invasion of Ukraine disrupted global commodity flows, causing significant supply constraints and price increases. However, production cuts slowed in the third quarter compared to the previews quarter as oil prices recovered. Overall, the significant increase in oil futures prices in the Q3 2023 reflects the global oil market's supply-demand balance.

According to the International Energy Agency's (IEA) August 2023 Oil Market Report, global oil demand is at an all-time high, owing to strong summer air travel, increased oil consumption in power generation and surging Chinese petrochemical activity. Global oil demand is expected to rise by 2.2 million barrels per day (mb/d) to 102.2 mb/d in 2023, with China accounting for more than 70% of the increase. However, growth is expected to drop to 1 mb/d in 2024 as the post-pandemic rebound fades, economic conditions deteriorate, efficiency conditions tighten and new electric vehicles weigh on demand. Global oil supply is expected to grow, the US driving the non-OPEC gains. Non-OPEC production is also expected to dominate global supply growth in 2024. However, the supply cuts by Saudi Arabia and Russia are expected to dominate oil prices for the remainder of this year.

Gold

Gold prices fell for the second quarter in a row in Q3 2023, down 3% for the quarter, following declines of 2% in August and 5% in September, which offset July's 4% gain. This was gold's lowest quarterly performance since the first quarter of 2022. The decline in gold prices was linked to the US dollar strengthening significantly against other major currencies, making gold more expensive for buyers holding foreign currencies.

Bond yields have also risen considerably, making gold, a non-yielding asset, less appealing. Furthermore, the Fed kept raising interest rates during the quarter in an effort to combat inflation. This fueled concerns about a looming recession, which weighed on gold demand.

Despite price declines, gold remained a popular safe-haven asset in the third quarter, as investors sought refuge from global economic and geopolitical uncertainties. If the greenback continues to strengthen and bond yields continue to rise, gold prices could dip. However, if global economic and geopolitical uncertainties escalate, demand for gold as a safe-haven investment option may rise.

US MARKET PERFORMANCE

MACROECONOMIC REVIEW

GDP

According to IMF's WEO July update, GDP growth in the US is expected to decelerate. Growth is anticipated to slow from 2.1% in 2022 to 1.8% in 2023, with a further slowdown to 1.0% in 2024. The 2023 forecast has been modestly revised upward by 0.2%, mainly attributable to robust consumption growth experienced in the first quarter. This growth underscores the job market's resilience, which has bolstered real income and spurred a rebound in vehicle purchases. This surge in consumption, however, is projected to be fleeting, as consumers have depleted their excess savings accumulated during the pandemic. Additionally, the Fed's expected interest rate hikes are poised to impact economic dynamics in the coming quarters.

The US Dollar Index, which measures the value of the Dollar against a basket of foreign currencies, rose 3.13% in the Q3 2023, the highest in nine years. This was due to the Federal Reserve's hawkish stance on interest rates, which caused Treasury yields to rise and the currency to appreciate. The Dollar also benefited from expectations that the US economy will withstand rising interest rates and oil prices better than other economies. The Dollar is forecast to strengthen further in the coming months as the Fed continues its tightening policy stance.

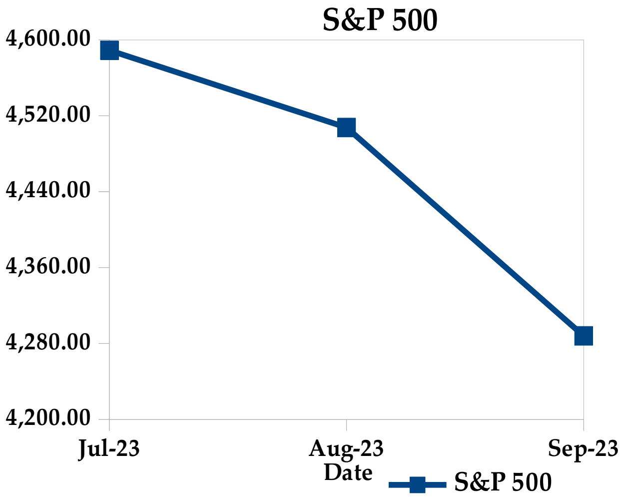
Inflation

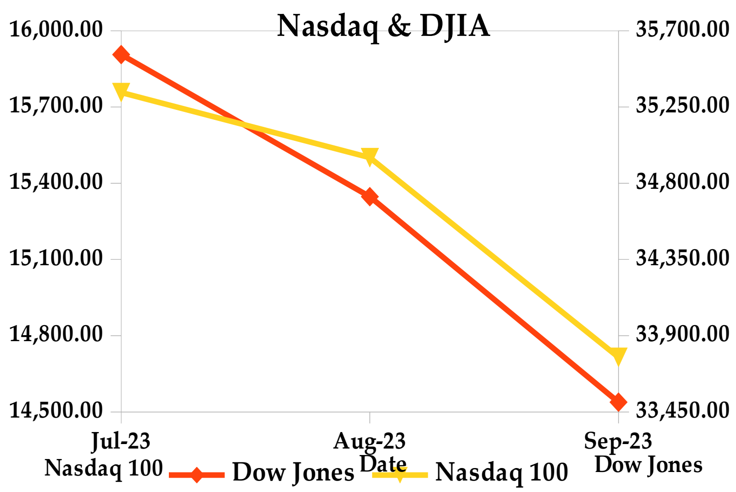
US inflation accelerated at the start of the quarter, reaching 3.2% in July, marking a halt to a 12-month streak of declines. This was due to base effects and an increase in the cost of apparel and transportation services. Inflation accelerated further in August to 3.7%, due to a further increase in the cost of transportation services. However, inflation remained steady at 3.7% at the end of the quarter, as a softer decline in energy prices offset slowing inflationary pressures in food, new vehicles, apparel, medical care commodities, shelter and transportation services.

The Fed raised interest rates by 25 bps at its July meeting, following a similar rate hike in May, resuming its tightening campaign after a pause in June, bringing borrowing costs to the highest level since January 2001. However, the Fed kept interest rates unchanged at its September meeting in order to better assess the impact of high borrowing costs on inflation as well as the evolving outlook and risks. The Fed emphasized that it is prepared to raise interest rates further if necessary to effectively manage inflation.

EQUITIES

US stock market fell in the third quarter of 2023, as investors worried about the Federal Reserve's hawkish interest rate outlook and the potential for a government shutdown. The S&P 500, Dow Jones Industrial Average and Nasdaq Composite ended the quarter down 3.65%, 2.61% and 3.06% respectively. However, the core personal consumption expenditures (PCE) price index, the Fed's preferred inflation measure, slowed to 0.1% from 0.2%, raising hopes among investors that inflationary pressures might be showing signs of early easing.



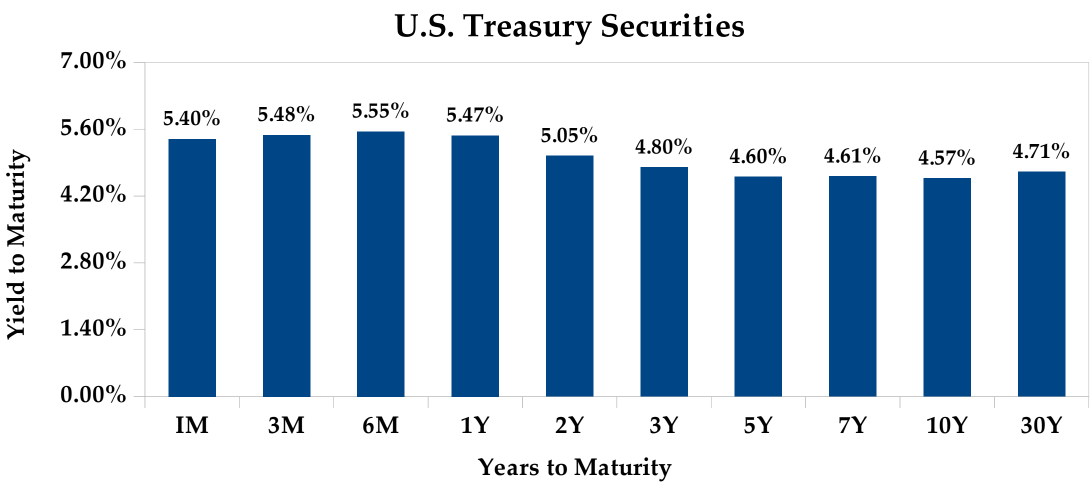


Technology stocks ended the third quarter nearly 6% lower, led by Alphabet and Meta Platforms. Energy and financial sector stocks slumped as investors rebalanced their portfolios. Energy remained by far the biggest-gaining sector for the third quarter, due to a drop in the PCE price index in August. Nike shares soared 6% after the company reported record first-quarter earnings.

FIXED INCOME

Compared to equities, the bond market performed better due to rising yields. During the third quarter of 2023, bond investors grappled with the Fed's continued aggressive interest rate hikes and concerns about a potential government shutdown after the US House of Representatives failed to pass a short-term spending measure. These factors led to a further increase in short-term bond yields, which rose more sharply than long-term yields, leading to an inverted yield curve. Specifically, the 2-year Treasury yield rose to 5.05%, up from 4.91% at the beginning of the quarter. The 10-year Treasury yield also rose, but at a slower pace to 4.57%, up from 3.86%.

Given the expected slowdown in economic growth in 2023, the Fed's continued hawkish stance and the potential surge in oil prices which will keep inflation high, yields are likely to continue rising in the last quarter of the year.



EUROPEAN MARKET PERFORMANCE

MACROECONOMIC REVIEW

GDP

Euro area growth is expected to decline sharply in 2023 to 0.9% from 3.5% in 2022, due to the ongoing war in Ukraine, high energy prices and supply chain disruptions. However, growth is projected to recover in 2024 to 1.5%. The economic outlook varies across Eurozone countries. Due to stronger service and tourist sectors, Italy and Spain are predicted to grow faster than Germany in 2023. Germany in Q1 showed signs of a mild recession, due to sluggish manufacturing output and overall economic contraction.

UK growth is projected to slow sharply in 2023 to 0.4% from 4.1% in 2022. However, growth is expected to recover in 2024 to 1.0%. The upward revision of GDP growth for 2023 is a positive sign and suggests that the UK economy is more resilient than previously thought. The stronger-than-expected consumption and investment are likely due to falling energy prices, lower post-Brexit (UK's withdrawal from the European Union) uncertainty and a resilient financial sector.

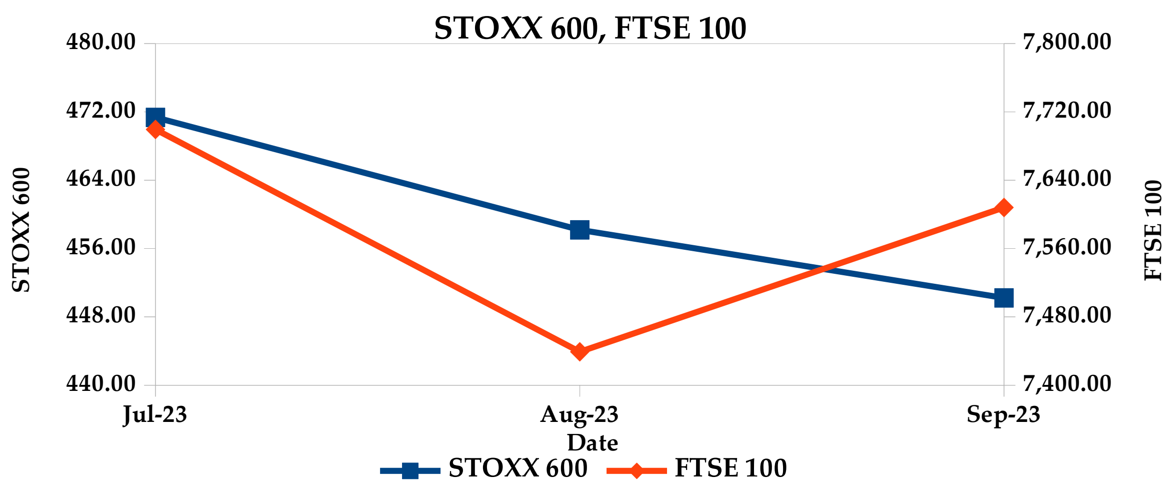
Inflation

In the euro area, inflation fell steadily from 5.5% in June to 4.3% in September, the lowest level since October 2021, due to a significant decline in energy prices. Prices for services, non-energy industrial goods and food, alcohol and tobacco also increased at a slower pace at the end of the quarter. Inflation declined in Germany, France and Netherlands but accelerated in Italy and Spain. UK's inflation rate also eased from June through to August, attributed to a slowdown in food inflation and a decline in the cost of accommodation services.

Despite the moderate decline in inflation over the quarter, with the inflation rate still significantly above the central bank's 2% target, the European Central Bank (ECB) raised interest rates twice in July and September by 50 bps to 4.5%. However, the Bank of England raised interest rates by 25 bps to 5.25% in August and maintained this rate in September, marking the first pause in policy tightening in nearly two years. Policymakers in both central banks remain committed to further tightening if deemed necessary.

EQUITIES

In Q3 2023, European indices displayed a mixed performance. The broader STOXX 600 lost 2.54%, while the FTSE 100 gained 1.02%, attributed to mounting concerns over rising Treasury yields, a notable upswing in oil prices and the depreciation of both the Euro and Sterling Pound, which marked a deviation from their three-quarter streak of appreciation. Nonetheless, the continued decline in inflation reinforced investor expectations of a potential pause in interest rate hikes by the ECB.



Oil and gas shares faced significant headwinds, with macroeconomic uncertainties casting a shadow on market sentiment. Likewise, technology stocks had a challenging quarter, grappling with rising bond yields and concerns over the duration of interest rate hikes. However, individual stocks like Commerzbank and Adidas, alongside luxury brands such as LVMH and Richemont managed to achieve quarterly gains.

ASIAN MARKET PERFORMANCE

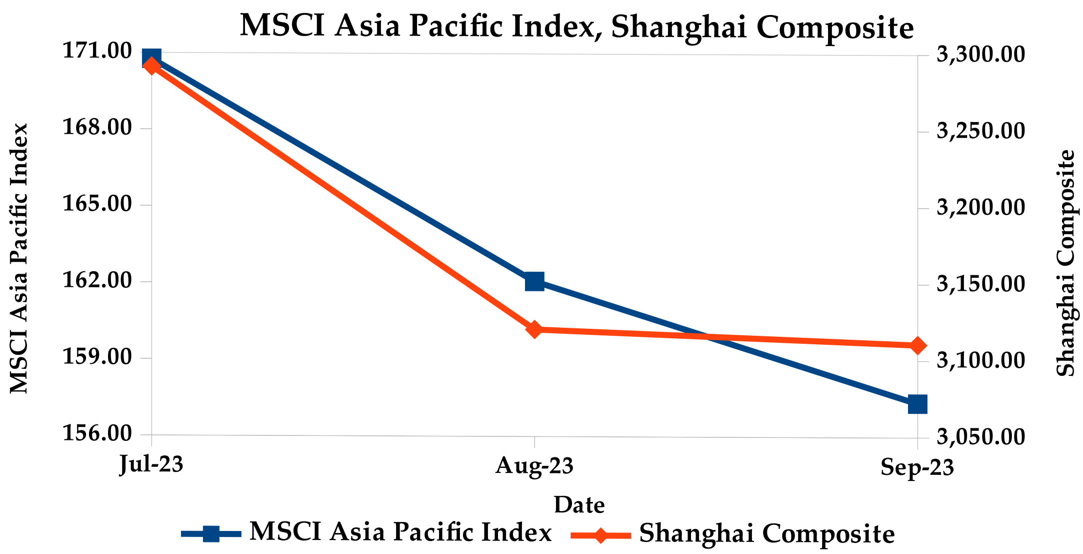
MACROECONOMIC REVIEW

Growth in emerging and developing Asia is expected to reach 5.3% in 2023 and 5.0% in 2024, with China growing at 5.2% in 2023 and 4.5% in 2024. India is expected to grow at 6.1% in 2023, a 0.2 percentage point upward revision from the April projection. The main drivers of growth in emerging and developing Asia are consumption and investment. However, due to the protracted real estate slowdown, Chinese investment underperformed. Net exports countered some of the investment slowdown, but their contribution is diminishing as the global economy slows. The upward revision of India's growth forecast reflects momentum from stronger-than-expected growth in the fourth quarter of 2022 due to increased domestic investment.

Overall, the growth outlook for emerging and developing Asia is positive, but the ongoing real estate downturn in China and a slowing global economy may dampen this sentiment.

EQUITIES

Asian indices fell in the third quarter, with the MSCI's most comprehensive index of Asia Pacific equities excluding Japan and the Shanghai Composite index falling by 3.63% and 2.86% respectively, prompted by investor expectations of a potential transition away from the Bank of Japan's prolonged easing monetary policy stance towards interest rate hikes. This shift comes after 17 months of Japan's inflation rate surpassing its targets, with inflation currently at a 40-year high.



In addition there were growing concerns about China's slowing economic development and a potential housing market collapse which heightened when China Evergrande Group, a struggling developer, halted all planned loan issuances in response to a government inquiry. These numerous worries played a crucial influence in pushing the indices' downward trend.

DISCLAIMER

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