Macro-Economic Outlook

Kenya's Macro-Economic Outlook – Q4 2023

Global economic growth remains sluggish, hit by high borrowing rates occasioned by inflation pressures that continue raising the cost of living across the globe. As a result, world economic growth is expected to drop from 3.5% in 2022 to 3.0% in 2023 and 2.9% in 2024 according to the World Economic Outlook of October 2023.

US economy was up 2.4% in Q2-2023 from a 2.0% in Q1-2023 and 2.1% in Q2-2022, being supported by growths in consumer spending which went up faster than expected. The UK reignited its economic growth to 1.8% in Q2-2023 from 0.2% in Q2-2022 and 0.9% in Q1-2023. The growth comes as investors in America and Europe continue shifting focus to projects in advanced economies even as China and Russia appear to focus on African investments.

Global geopolitical tensions resulting from wars in some parts of the middle East also continue impacting investments with many investors recalling their investments especially from emerging economies.

Sub-Saharan African economic growth is expected to slow down to 2.5% in 2023 from 3.6% in 2022 with more than half of its countries being downgraded in the 2023 estimates on account of worsening debts debt levels occasioned by elevated interest rates. This is as many Central Banks try to cool the high inflations that skyrocketed on supply chain constraints upon the Russia-Ukraine war. Slow economic growth coupled with high foreign dominated public debt, continues weighing down many Sub-Saharan currencies.

Kenya FY GDP Growths

2018 - 5.6%

2019 - 5.1%

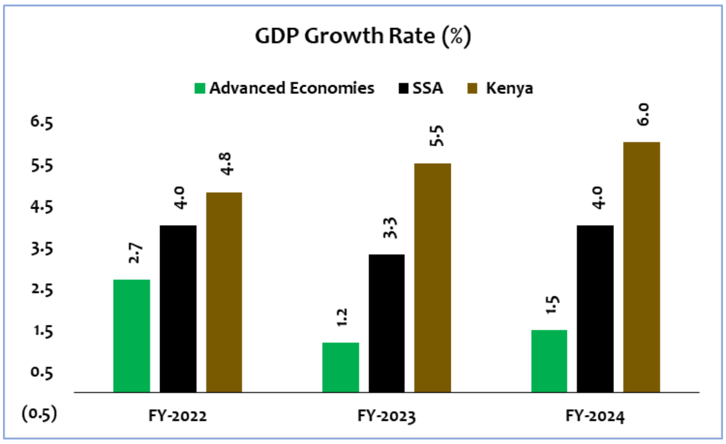
2020 - (0.3%)

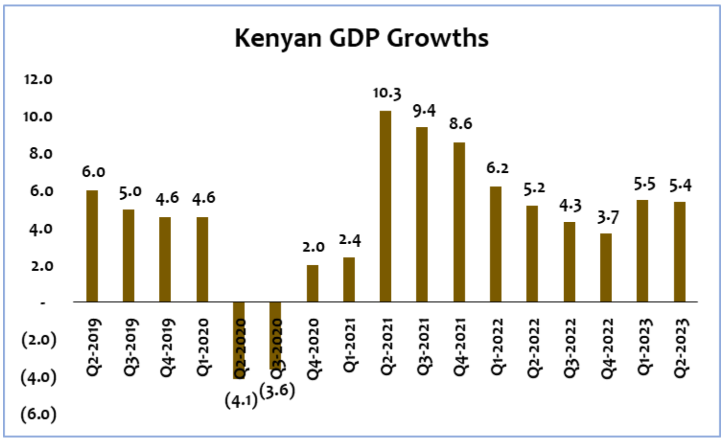
2021 - 7.6%

2022 - 4.8%

H1 203 – 4.5%

2024 - 5.5% Est.





Locally, Kenyan economy is expected to grow by 5.5% in FY-2023 from 4.8% in 2022, having grown by 5.45% in the first half of 2023, supported by strong growths in agriculture, financial and insurance sector and the hospitality sectors which went up 7.7%, 13.5% and 12.2% during the quarter. This is in relation to a contraction of 2.4% in agriculture and growth of 16.1% in the financial & insurance and hotel and accommodation sectors respectively, as per the National Statistics.

Agriculture contributes about 22% of the overall GDP with the sector employing over 40% of the total population and more than 70% of the rural population.

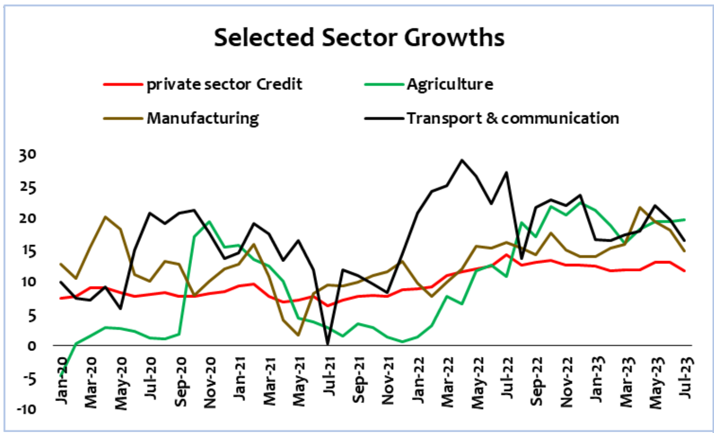
The rise in agricultural growth benefitted from favorable weather conditions on the rains witnessed the period, resulting to increased food supply and overall declines in food prices.

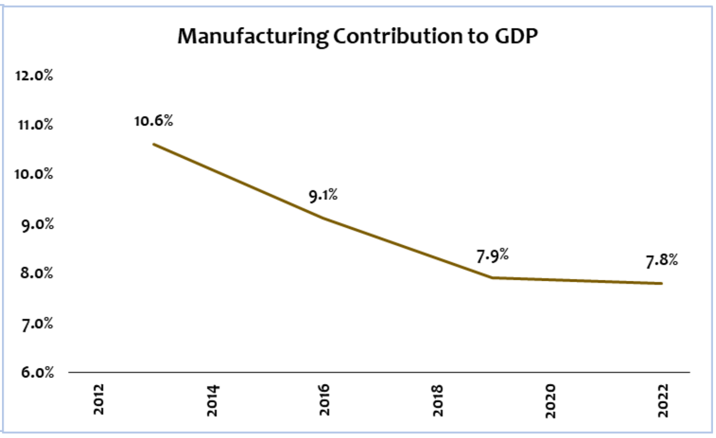
Improved tea exports eased pressure on the local currency on better prices witnessed in the global market.

Manufacturing sector remains low, slowing down to a growth of 1.5% in Q2 2023 from 3.6% same time last year, prompting the government to initiate industrial parks to sour industrialization grow local exports. This is aimed to grow the manufacturing contribution to total GDP from 7.8% in FY-2022 to 20% of GDP by 2030 especially through value addition.

So far, the government has launched about thirteen Agri-industrial parks across thirteen counties.

Stanbic Bank's Purchasing Managers' Index fell to below the 50-point mark to 47.8 points on low consumer spending as the disposable income remained affected by higher prices passed by manufactures to consumers.





CBK

At its last monetary policy meeting, the committee retained the Central Bank Rate (CBR) at 10.5% for the second time since June following the moderation of the overall inflation and the slow transmission of the policy rate in the overall market.

We forecast the CBR to remain flat at (CBR) at 10.5% in Q4-2023 as inflation remains within the CBK target of 5% ± 2.5% and the tight liquidity in the market.

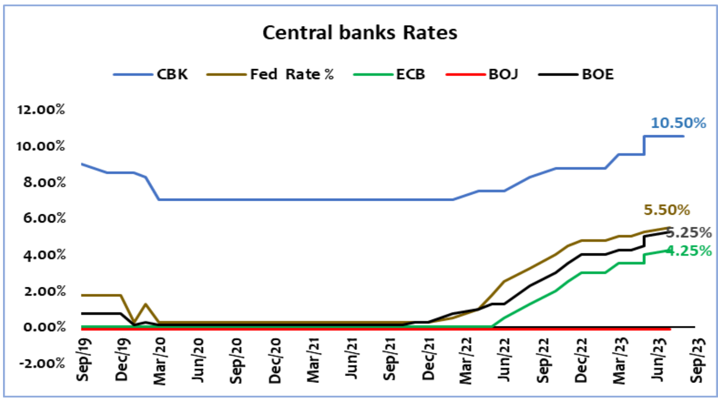
The tight liquidity in the market has seen CBK support liquidity through repurchase of securities from the market.

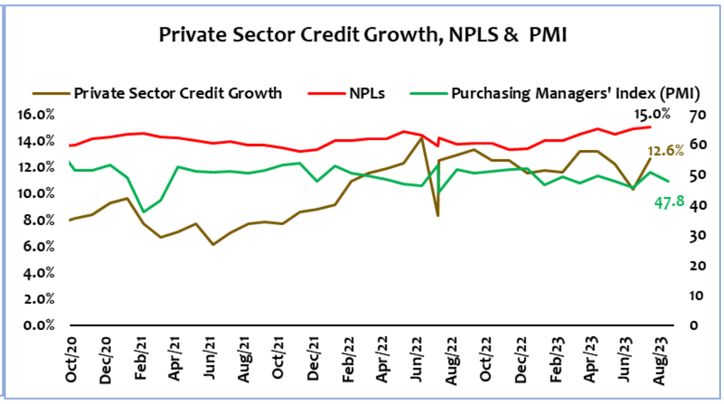
Kenya's current account deficit is estimated to improve to a deficit of 4.1% of GDP in 2023 from 5.1% in FY-2022, on what we attribute to the to higher taxes implemented on July 1st, implying more revenue to the government. We view the establishment of the above industrial parks to positively impact the balance of payments and thereby reduce the current account deficit.

The economy is expected to remain steady, having grown by 5.45% in the first half of 2023. We project the first half of 2023 (H1-2023) to have grown even faster on improved agricultural products and the onset of the harvesting in the food basket Western region of Kenya. We expect Q4-2023 to be slightly slow, especially in the holiday month of December.

The Banking sector remains stable and resilient with nearly all the listed banks recording spikes in their profits. However, non-performing loans (NPLs) continue posing a risk on rising defaults resulting to heavy provisions thereby affecting overall profits. As of August, overall NPLs ratio was at 15.0%compared to 14.2% of August 2022 with higher NPLs emanating from manufacturing, mining & quarrying and in the real estate sectors on what we attribute to low sales.

The private sector credit continues strengthening signaled by a 12.6% growth in August with strong growths in the transport and communications and manufacturing benefitting from hiked costs passed to consumers.





We anticipate the PMI to improve to above 50-point mark elevated by expected increase in spending in the festive season. Private sector credit is set to remain on an upward trend elevated by the tea bonuses.

Bank NPLs will improve slightly to about 14.5% even as credit in the manufacturing sector is set to improve on increased purchase orders.

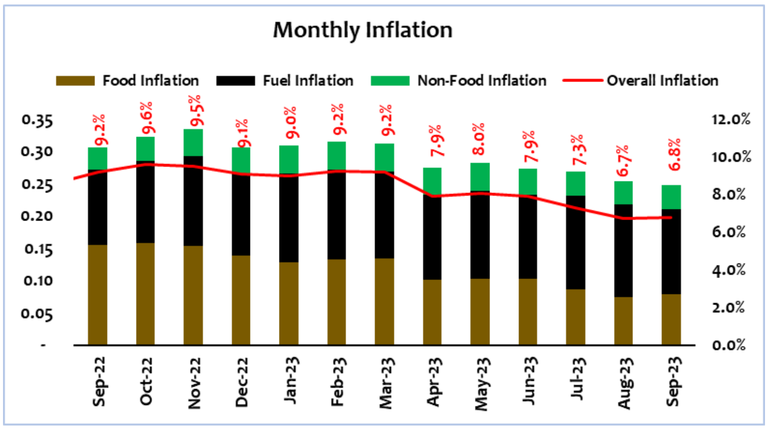
We expect the high appetite for funds by the government to push government treasury rates higher in Q4-2024 even as the tight liquidity environment continues leaving the interbank on the upper side of the CBR±2.5%, averaging at 12.36% in the last one month.

Inflation

Overall inflation has receded down to the government target range with September recording a slight increase from 6.7% to 6.8%. The inflation was contained by declines in food prices as supply increased, benefiting from the long rains received in H1-2023.

We expect the inflation rate to remain under pressure, especially from pump prices as the sector experiences supply cuts Organization of the Petroleum Exporting Countries (OPEC) in a move to push prices up. Russia has been cutting its oil supply to the market since last year even as Saudi Arabia joined in the supply cut in April and is expected to continue till end of 2023.

Value added tax of 16.0% worsens the situation making the commodity further expensive with a ripple effect across economies. We forecast the inflation rate to remain within a range of 6.8% and 7.5% in the last quarter of 2023.



Public Debt

According to CBK's provisional statistics public debt grew to KES 10,189.53Bn as of June 2023, with KES 5,452.94Bn or 53.5% and KES 4,736.60Bn or 46.5% being external and domestic respectively.

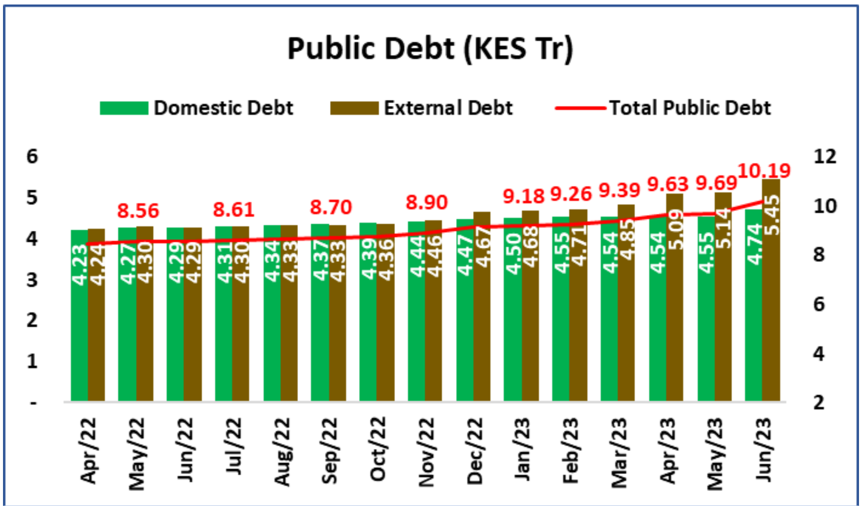
The parliament in June 2023, approved the conversion of Kenya's debt ceiling from KES 10trillion to a debt anchor based on the country's gross domestic product (GDP).

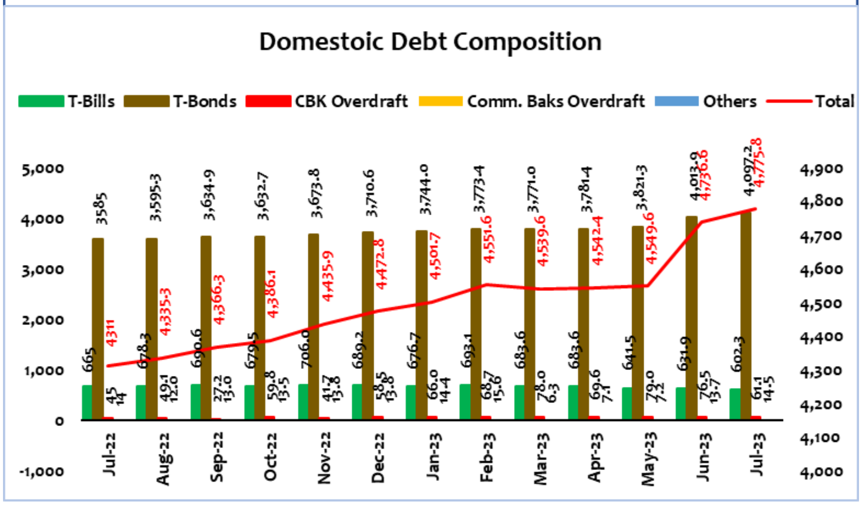
The external public debt remains elevated by the strengthening of the US dollar, growing the actual value by 20.0% in the first three quarters of 2023 and 34.0% in the twelve months ending 30th September.

The domestic debt is composed of 85.8% treasury bonds and 12.6% T-bills as CBK overdrafts stands at 1.3%.

According to the 2023/24 budget, domestic borrowing is expected to be KES 688Bn with the government surpassing its first two months borrowing target at 109.6%.

Tax revenues at the exchequer were at 76.4% at KES 317.58Bn against a proportional target of KES 415.97Bn. Total government revenues stood at KES 502.38Bn in the month of July and August combined.





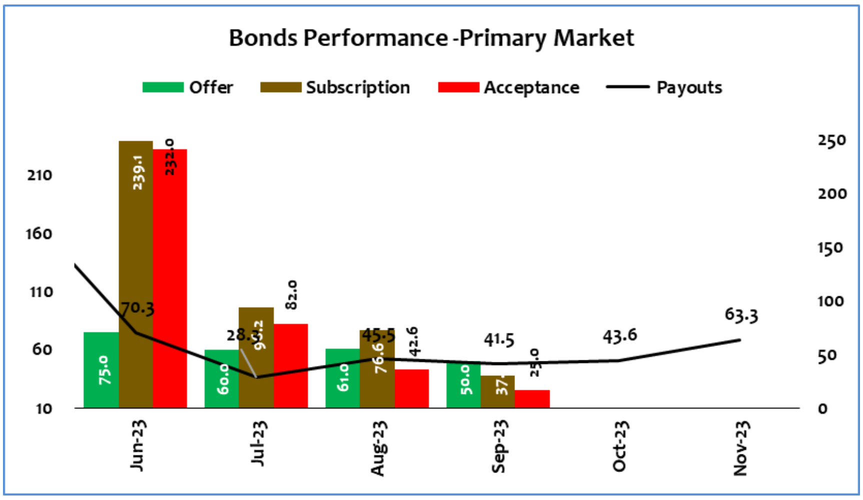
Revenues					
Source	**Original Estimate**	**Proportional**	**Actual receipt**	**% Receipt to Exchequer**	**% Receipt to Proportional**
Tax Revenues	2,495.83	415.97	317.58	12.72%	76.35%
Total Revenues	**4,132.74**	**688.79**	**502.38**	12.16%	72.94%
Expenditure					
Expenditure	**Original Estimate**	**Proportional**	**Actual receipt**	**% Receipt to Exchequer**	**% Receipt to Proportional**
Recurrent Exchequer Issues	1,302.80	217.13	148.98	11.44%	68.61%
Public Debt	1,751.07	291.85	267.04	15.25%	91.50%
CFS Exchequer	212.62	35.44	32.98	15.51%	93.05%
Development Exchequer Issue	480.82	80.14	14.48	3.01%	18.06%
Total Issues to National Gov'nt	3,747.32	624.55	463.47	12.37%	74.21%
Total Issues to County Gov'nts	385.42	64.24	39.27	10.19%	61.13%

Treasury Bonds

New government bonds continue attracting aggressive bidding with re-opens receiving low subscriptions on what we view as rejection of low coupon rates in the current macro-economic environment.

T-bond coupon payouts of KES 152.63 Bn is due in Q4-2023, where KES 43.62Bn, KES 63.27Bn and KES 45.74Bn in rea due October, November, and December respectively

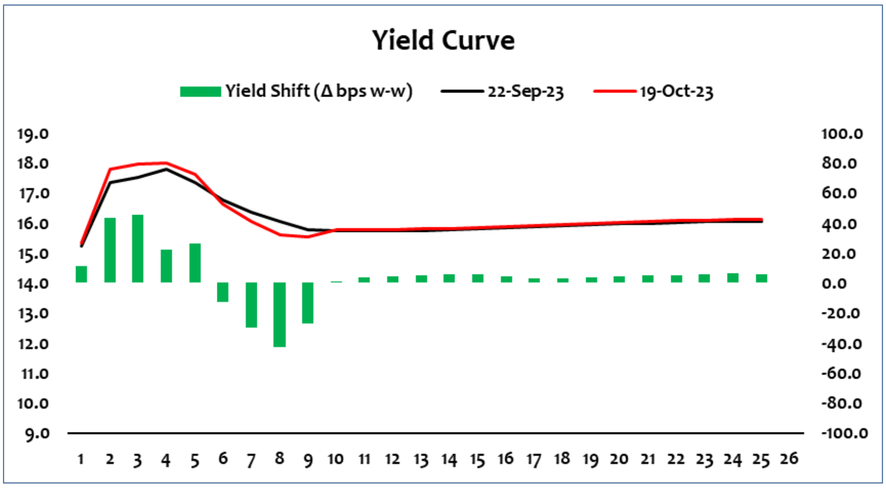
The market appears to be starved of new papers with many investors staying out of the market awaiting new papers for better returns on investment. We predict that if new papers are issued, they will be aggressively bided even as yields in the secondary market remain driven by tight liquidity.



Yield Curve

Tight liquidity continues pushing yields rates higher especially in the short-term papers on what we view as customer preference to short-term papers. The mid to long-end remains relatively stable, experiencing minimal activity.

Yield Key Rates %	06-Jan-23	22-Sep-23	19-Oct-23	(y-t-d) bps	(m-m) bps
2-Yr	12.196	17.3533	17.7895	-559.35	-43.62
5-Yr	13.5472	17.3637	17.6267	-407.95	-26.30
10-Yr	13.7798	15.7503	15.7627	-198.29	-1.24
15-Yr	13.9356	15.7962	15.8528	-191.72	-5.66
20-Yr	14.0586	15.9698	16.0138	-195.52	-4.39
25-Yr	14.2374	16.0583	16.1191	-188.17	-6.08

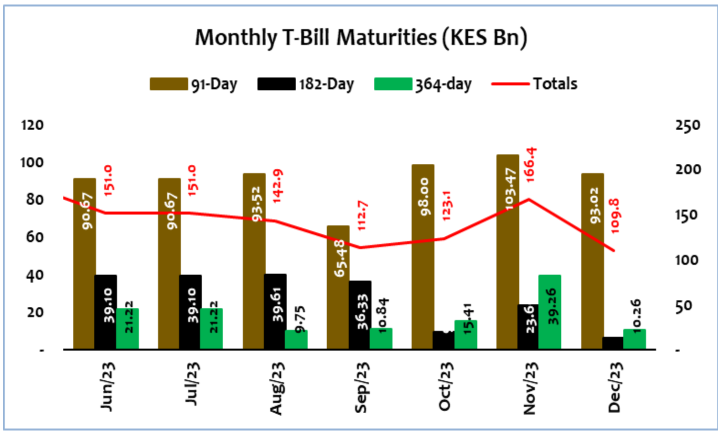


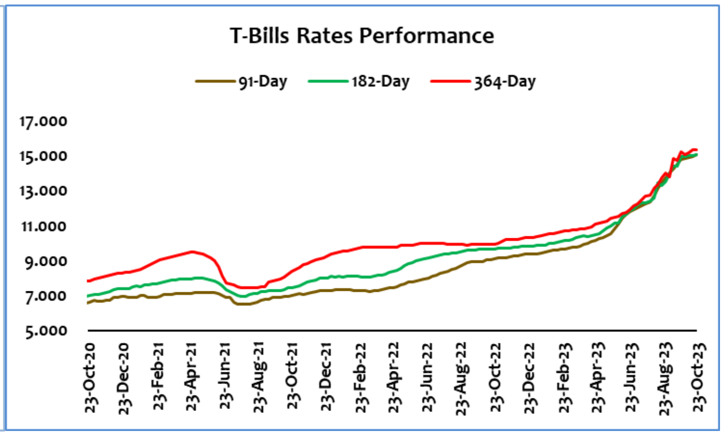
Treasury Bills

Returns on investment in the T-bills space continue flourishing accelerated by high liquidity appetite by the government towards the heavy maturities in the same papers amid the demand for budgetary support.

All the three papers touched the 15% mark as of 23rd October, with the 91- 182- and 364-day papers hitting new highs of 15.0458%, 15.0763% and 15.3405% respectively.

With the heavy maturities of KES 123.09Bn, KES 166.39Bn and KES 109.79Bn due in October, November, and December 2023 respectively, we expect the rates to remain on an uptrend till end of the year, with the 364-day paper expected to hit 16% levels.





Currency

Kenyan shilling has lost 21.6% 23.9% y-t-d and y-y respectively being held down by the global strengthening of the US dollar, heavy dollar demand to settle external debts, and high importation especially in the oil sector.

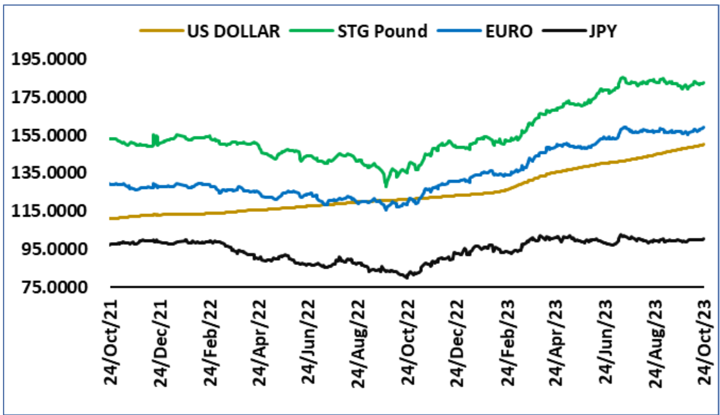
Strengthening of US dollar directly inflates Kenya's external debt by the same rate of depreciation putting more pressure on the forex reserves and ability of payment. Forex reserves stand at USD 6,833Mn, enough for 3.67 months of import cover against a 4.0-month import cover requirement.

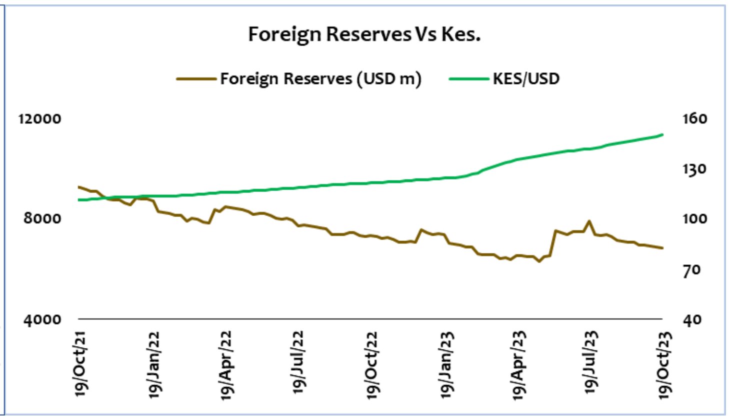
Globally, the US dollar has strengthened against some major currencies, gaining 0.93% in y-t-d.

If the shilling continues losing ground at the current rate of 0.1% per day, by 31st December, the shilling will have lost an additional KES 6.90 or 4.6% against the US dollar.

Against the British pound and Euro, the shilling has also lost 22.7% & 20.8% and 35.2% & 34.5% y-t-d and y-y respectively.

Currency	03/Jan/23	22/Sep/23	24/Oct/23	%D y-t-d	%D w-w
Dollar	123.42	147.36	150.07	-21.6%	-1.8%
STG Pound	148.73	181.02	182.54	-22.7%	-0.8%
Euro	131.66	156.94	159.09	-20.8%	-1.4%
JPY	95.24	99.84	100.27	-5.3%	-0.4%
US Dollar Index	104.52	105.58	105.41	0.9%	-0.2%





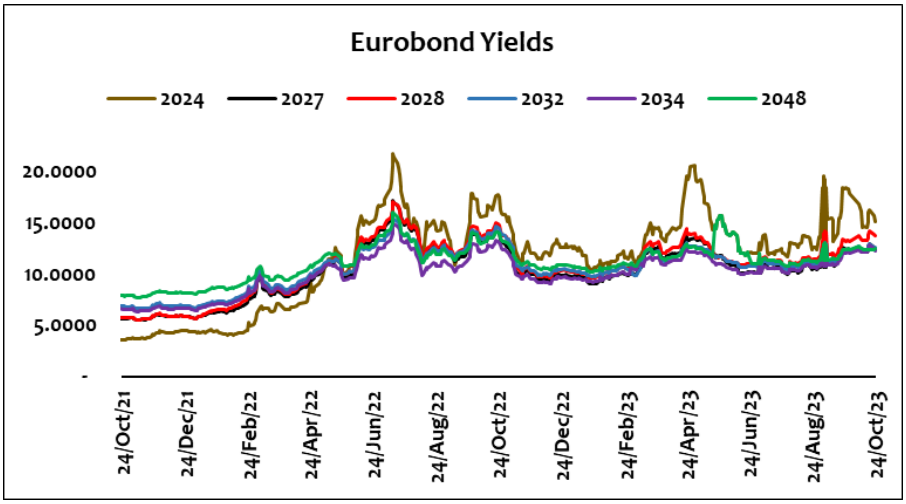
Eurobond

Eurobond yield rates remained on an up-trend since March 2022 locking out many emerging countries from the international capital markets but started slowing down on as from August 2023 on inflations slowing down. In June 2022, Kenya shelved its plan of issuing a new Eurobond due to high borrowing cost.

Kenya's international bonds' rates relaxed as from 12th October upon the governor Central Bank saying the country intends to buy back up to USD 500Mn from the market in an aim to reduce the liability of the bond. On his statement, Dr. Kamau Thugge said, the country is in talks with two commercial banks, Trade & Development Bank and the African Export-Import Bank to raise between USD 500 and USD 1Bn for the purpose of the e purchase and budgetary support, MARRAKECH, Morocco, Oct 12, Reuters.com.

We view that the yields will however remain high on the weakening Kenyan shilling and the depressed forex reserves even as the government works on boosting the forex through more exports.

Euro-bond Paper	03/Jan/23	22/Sep/23	24/Oct/23	Δ bps y-t-d	Δ bps w-w
Jun-2024	12.671	18.382	15.086	(241.50)	329.60
May-2027	9.724	12.629	12.372	(264.80)	25.70
Feb-2028	10.200	13.324	13.692	(349.20)	(36.80)
May-2032	10.314	12.167	12.526	(221.20)	(35.90)
Jan-2034	9.539	11.962	12.272	(273.30)	(31.00)
Feb-2048	10.708	12.299	12.433	(172.50)	(13.40)



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