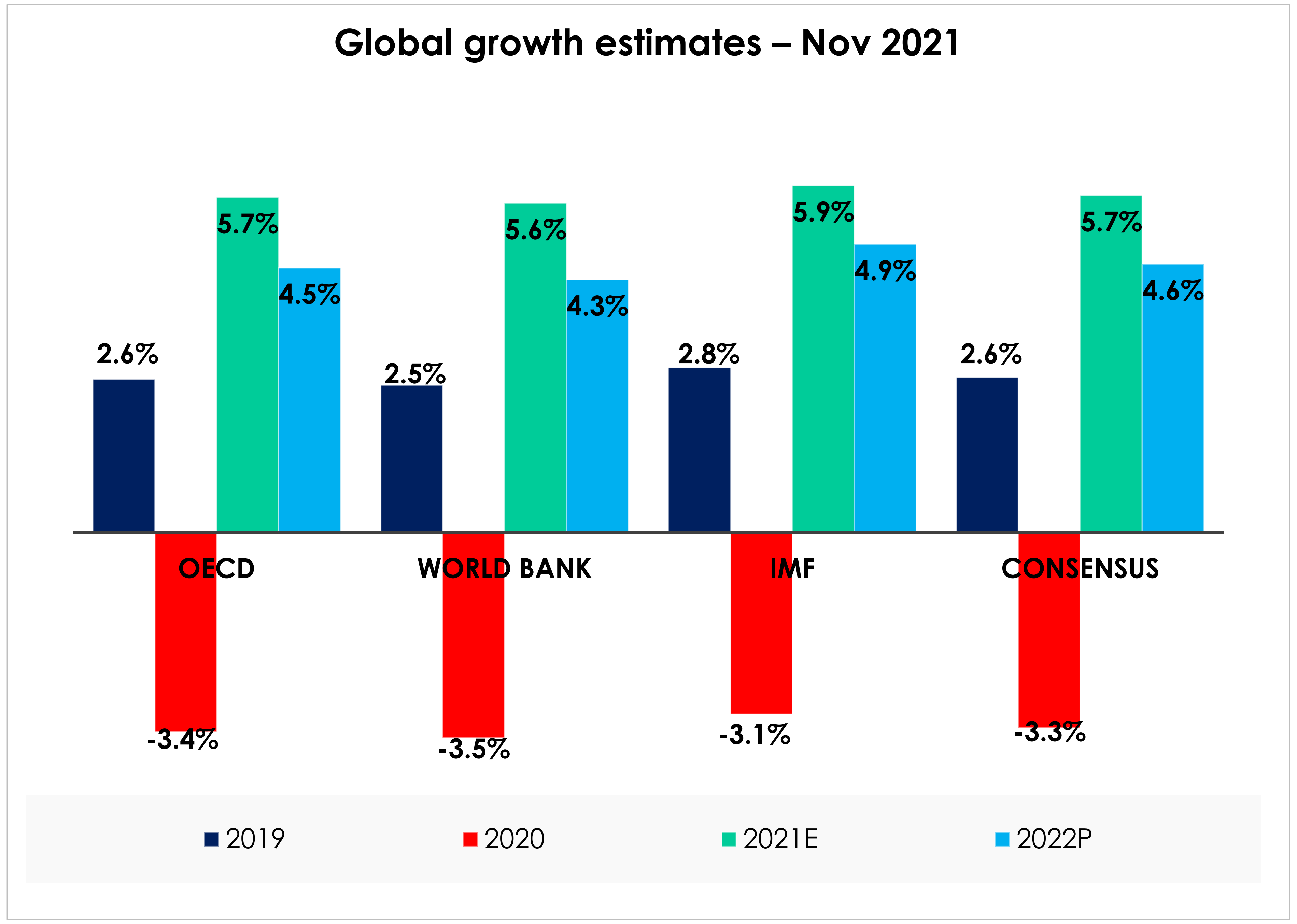
NCBA ECONOMIC FORUM

Kenya Economic Update 2022 – Uncertainty trinity?

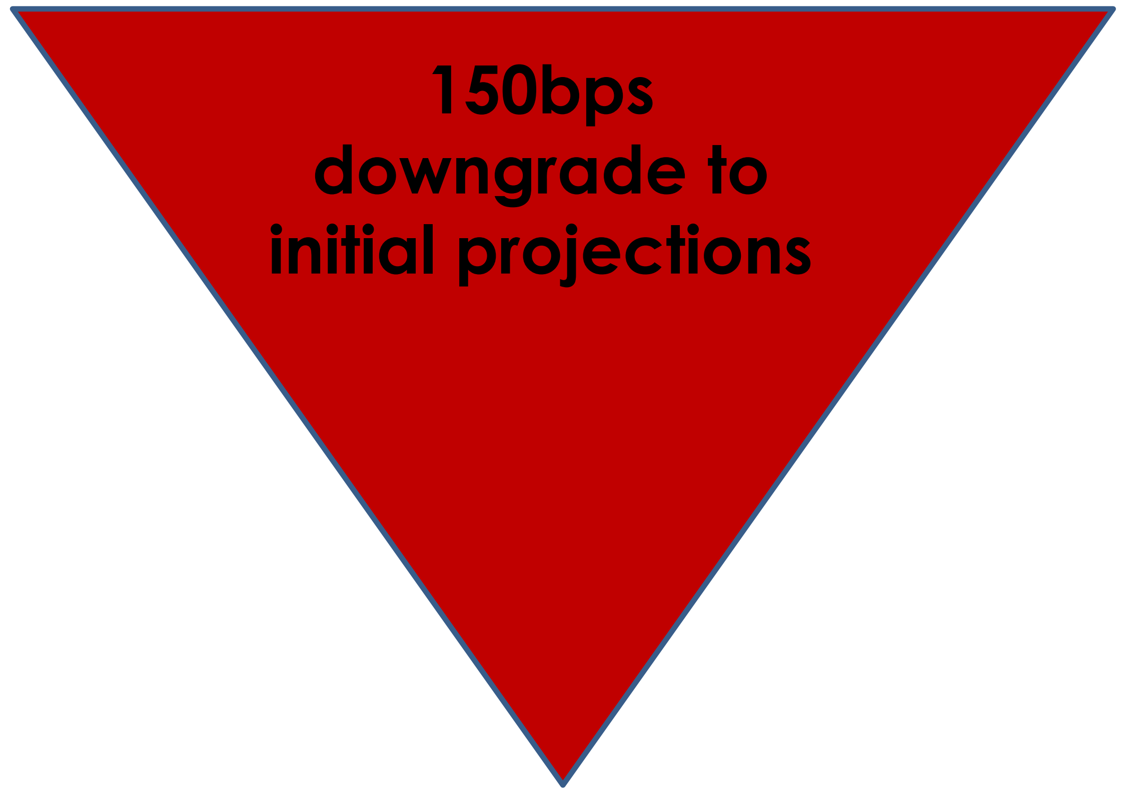
JUNE 2022

The World : Russia-Ukraine War Deflates the Post-Pandemic Economic Recovery

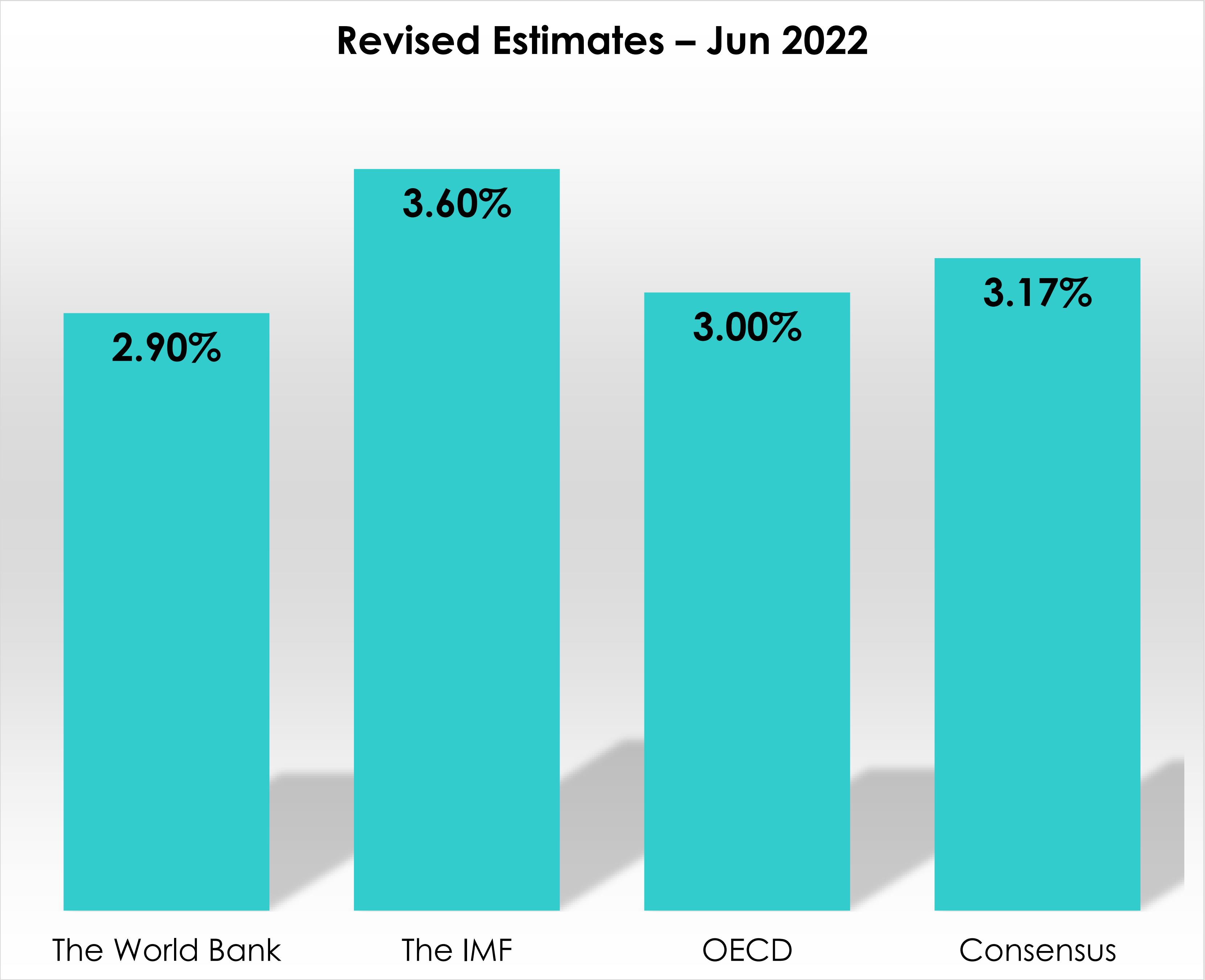
Prior to the war



Source: The IMF, The World Bank, OECD & NCBA Research



After the War



Source: The IMF, The World Bank, OECD & NCBA Research

- Prior to the war, the world was on course for a strong recovery underpinned by Covid Vaccines and the unprecedented policy support from governments and central banks.

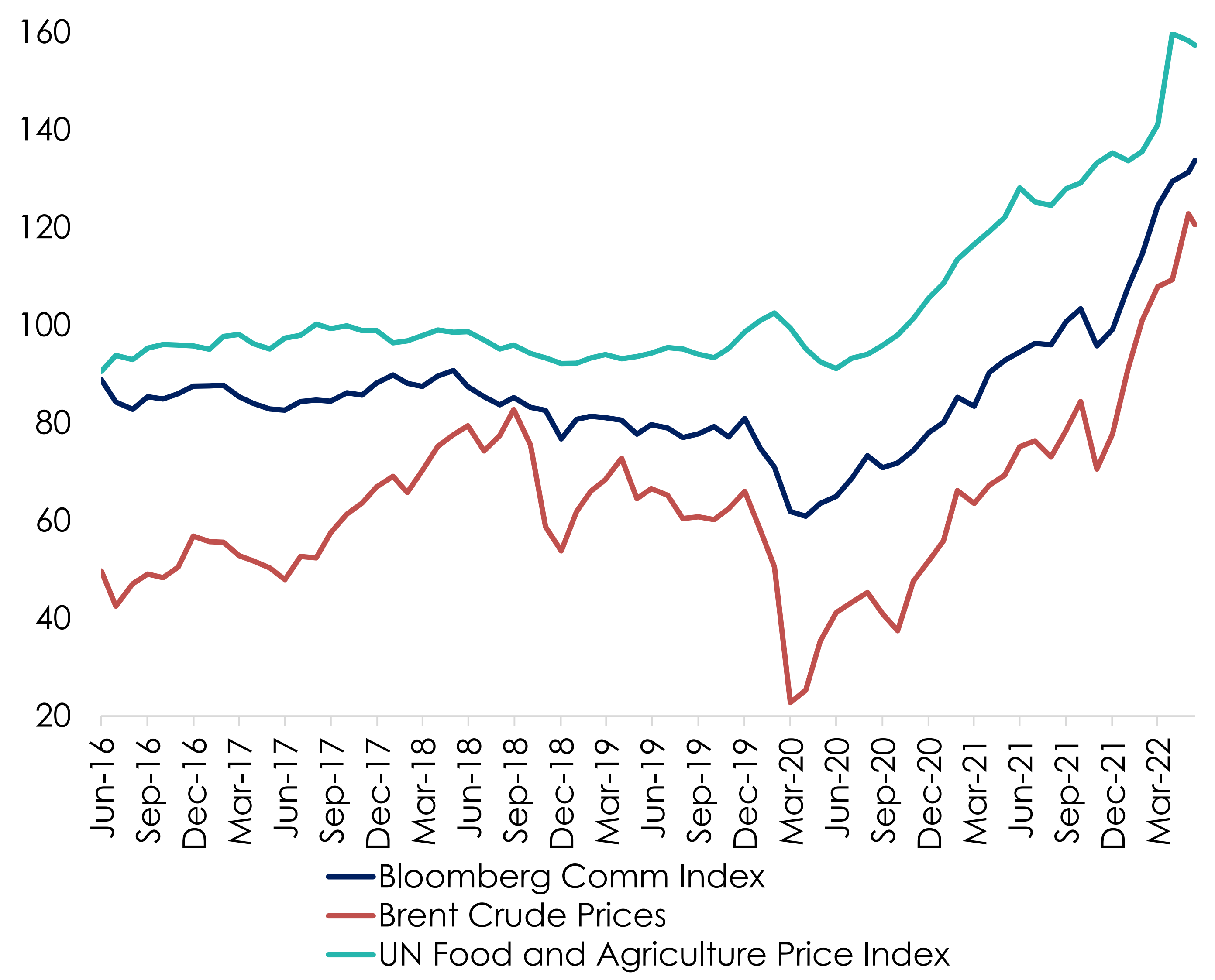
- The war has introduced fresh uncertainties and aggravated earlier supply shocks, nationalism threats as well as inflation and accelerated the pace of financial tightening by central banks.

The war has introduced new uncertainties and aggravated some earlier threats to growth

The war has added risk premium to commodity prices

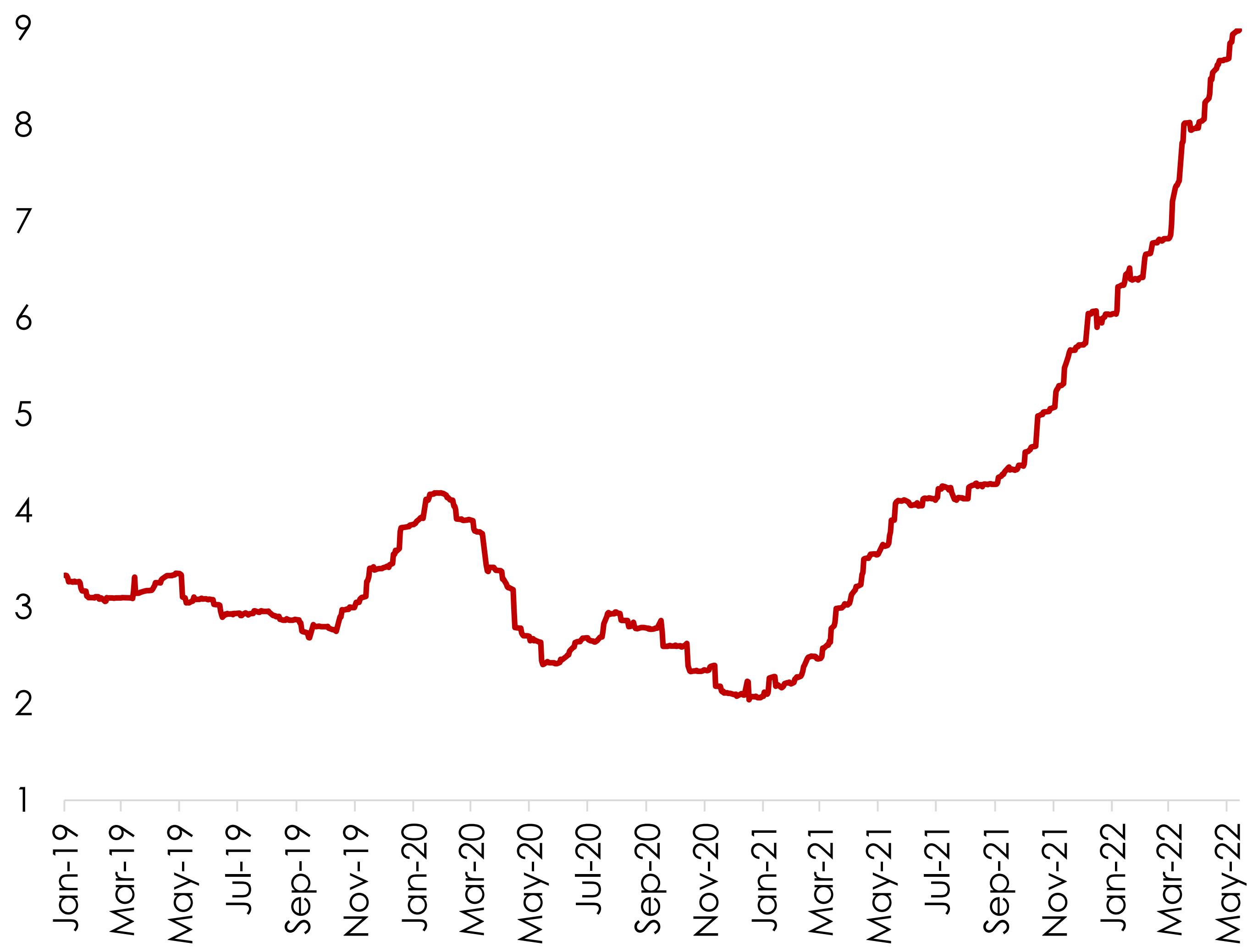
High commodity prices have turned up upward pressure on inflation

Record and rising inflation is accelerating financial tightening by central banks.

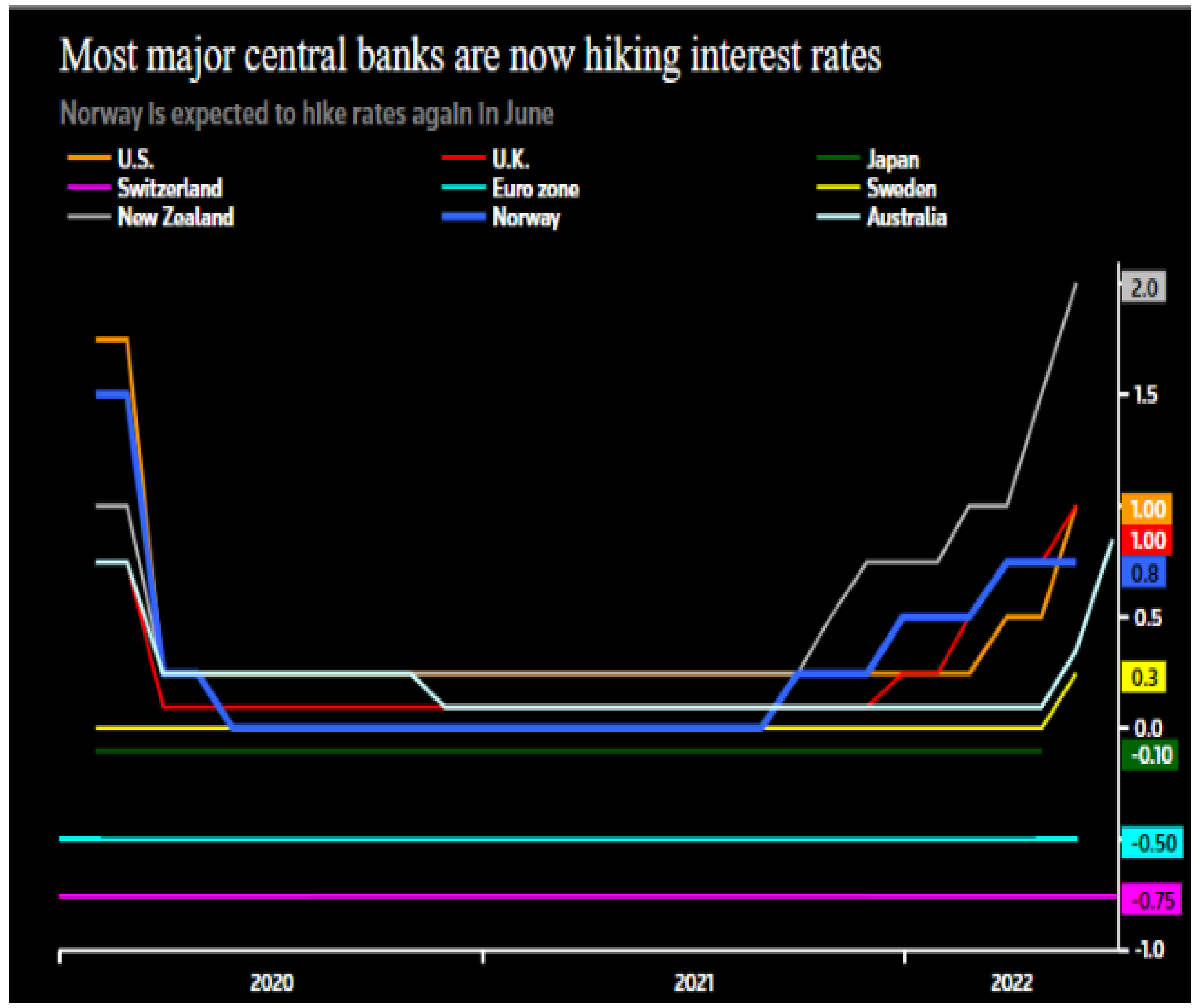


Source: Reuters

Global inflation



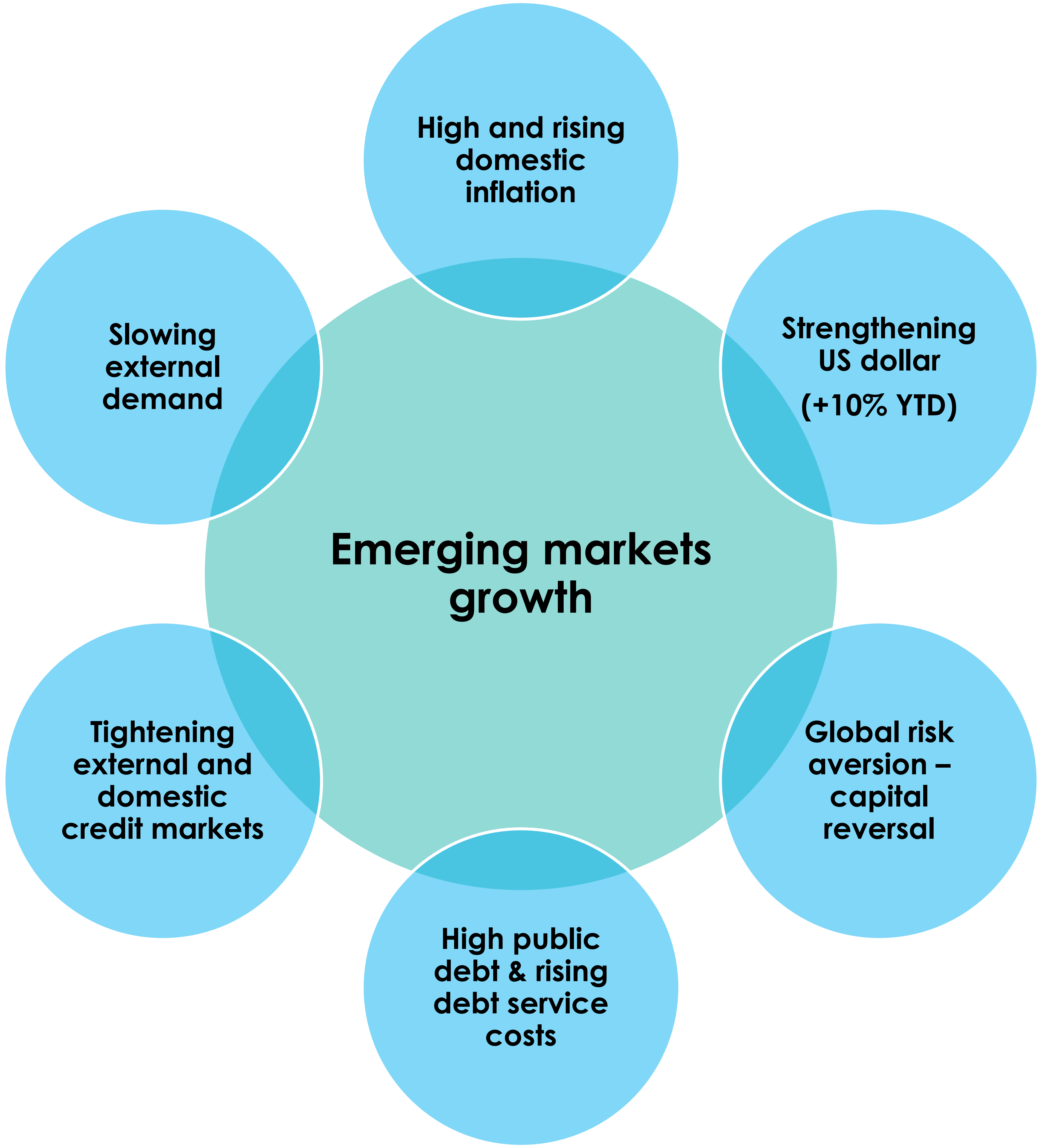
Source: Reuters

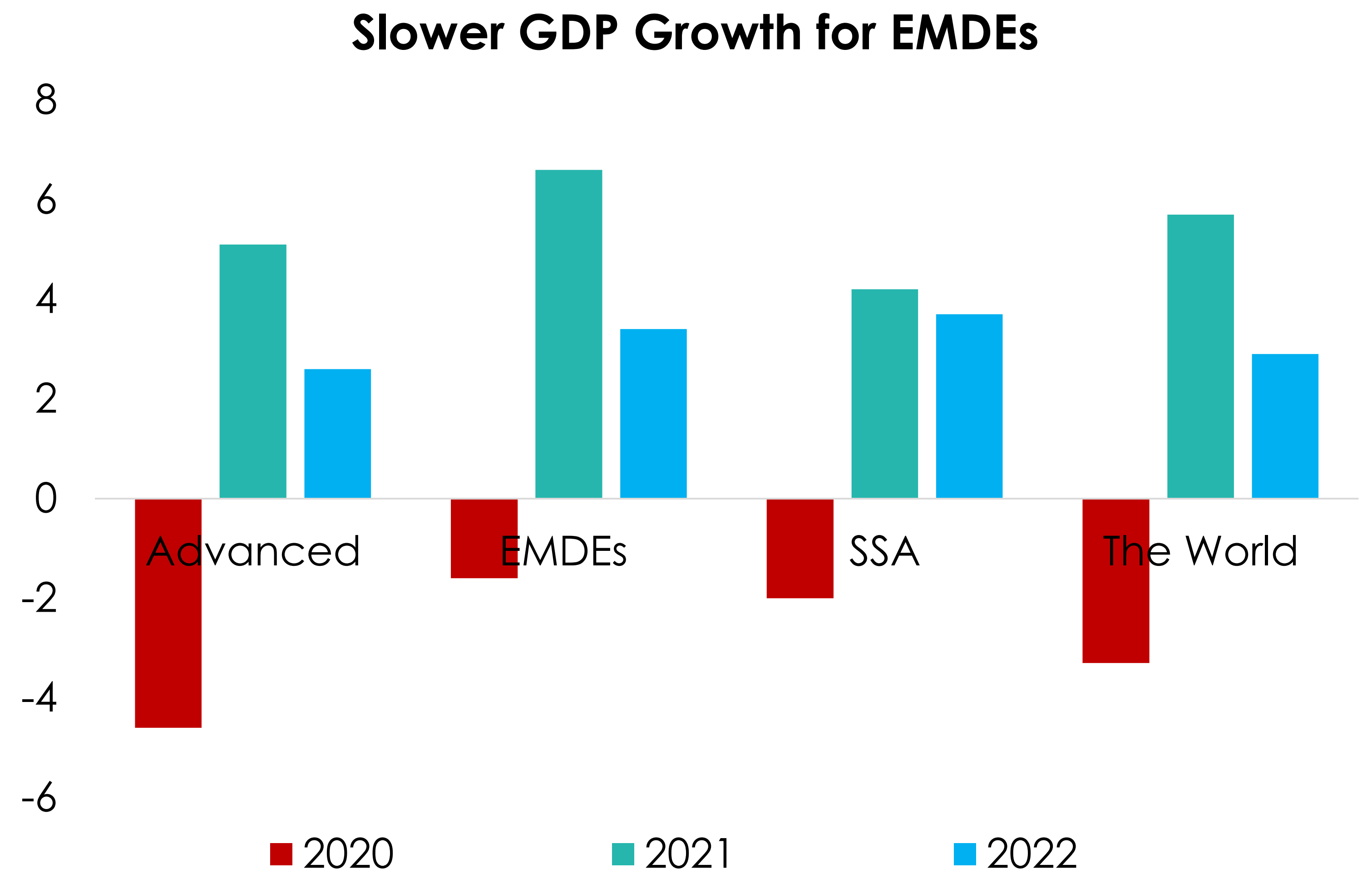


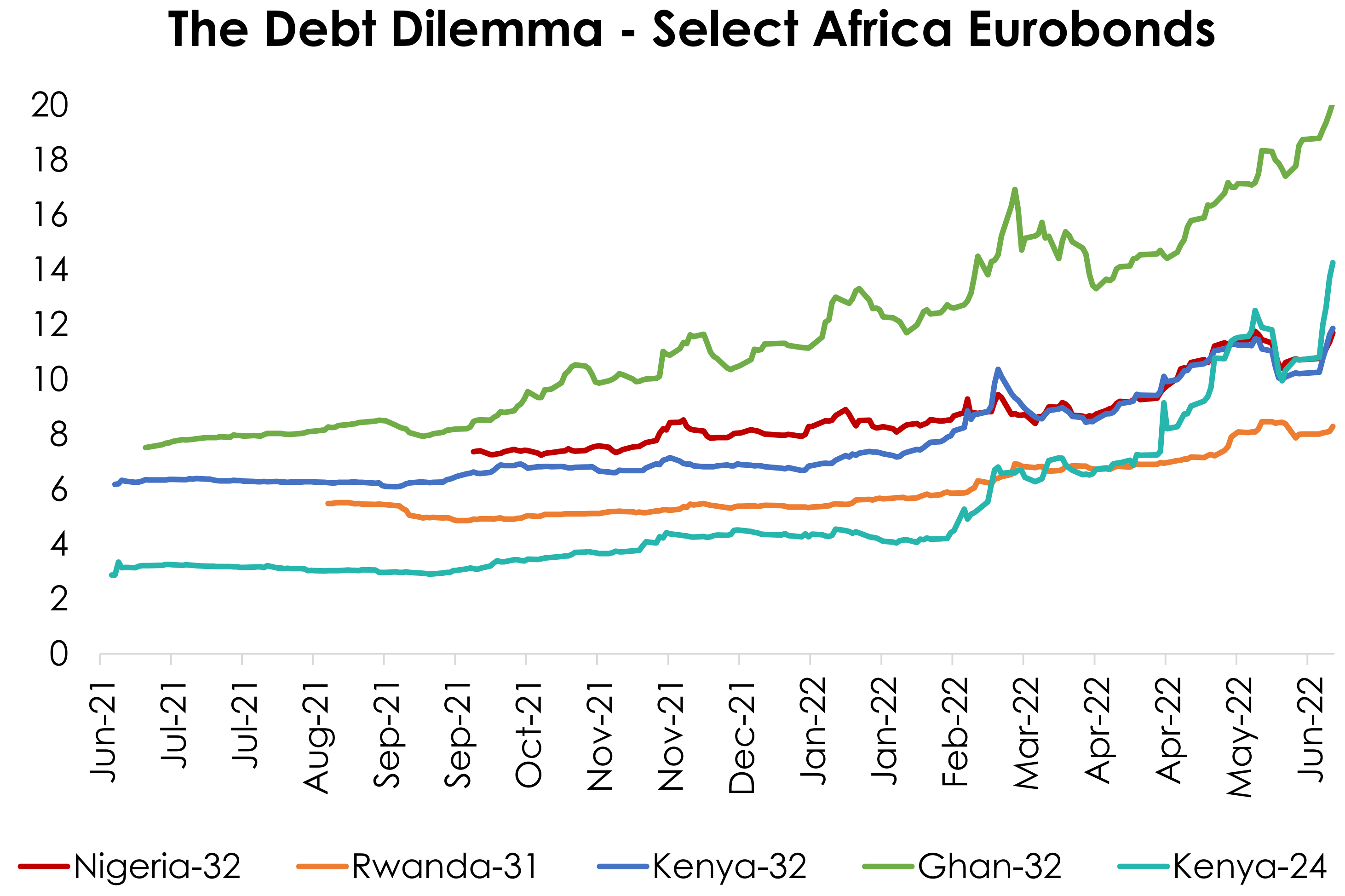
Source: Reuters

- Structural supply shocks from Russia-Ukraine conflict to keep energy and food prices near record highs
- Inflation will slow down marginally in the second half as demand slows but will remain uncomfortably above central banks target.
- Monetary policy will not address supply shocks but tightening signals are critical in containing further upside and broadening of inflation – expectation coefficient

Overlapping shocks have increased vulnerabilities for Emerging and Developing economies

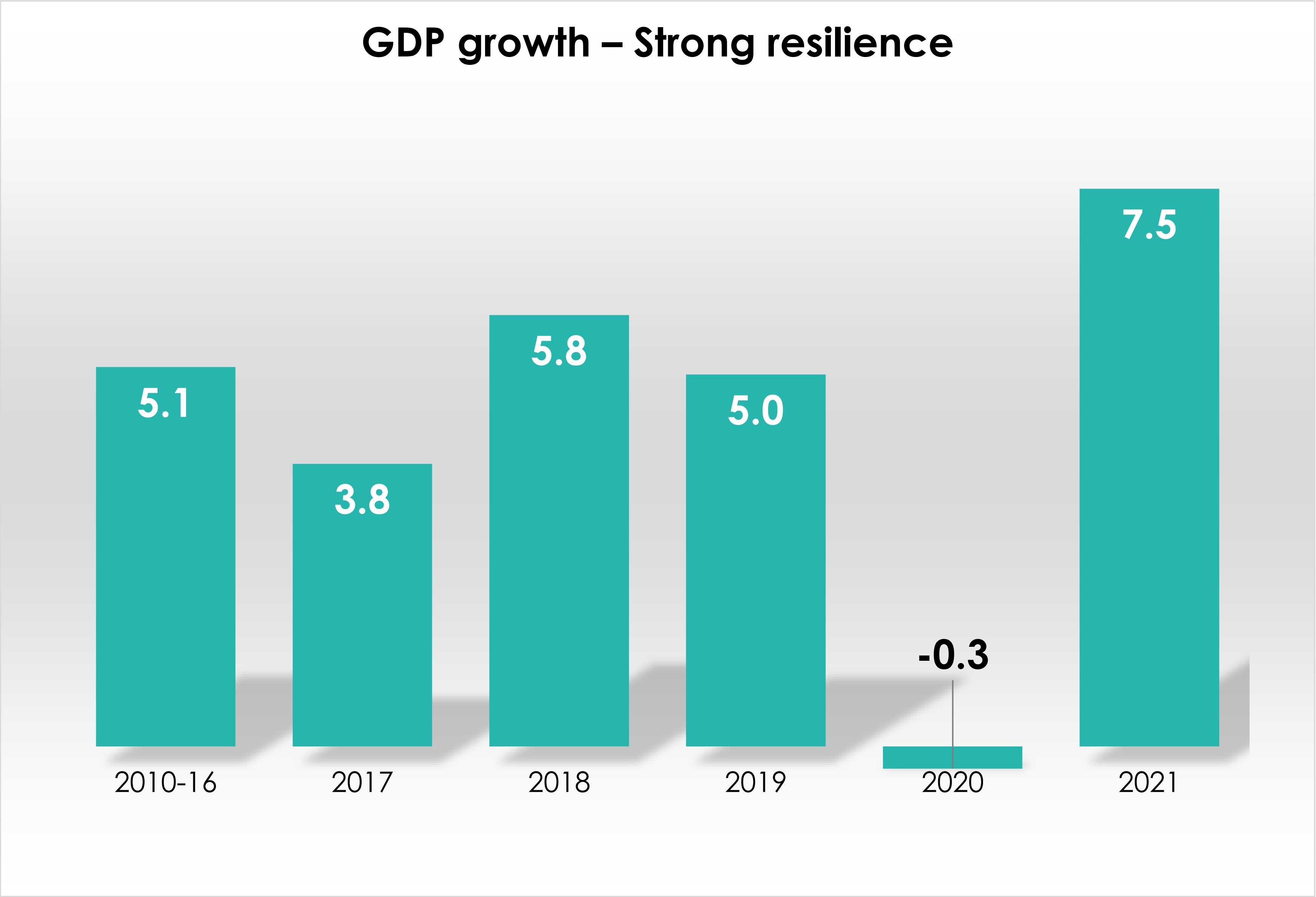


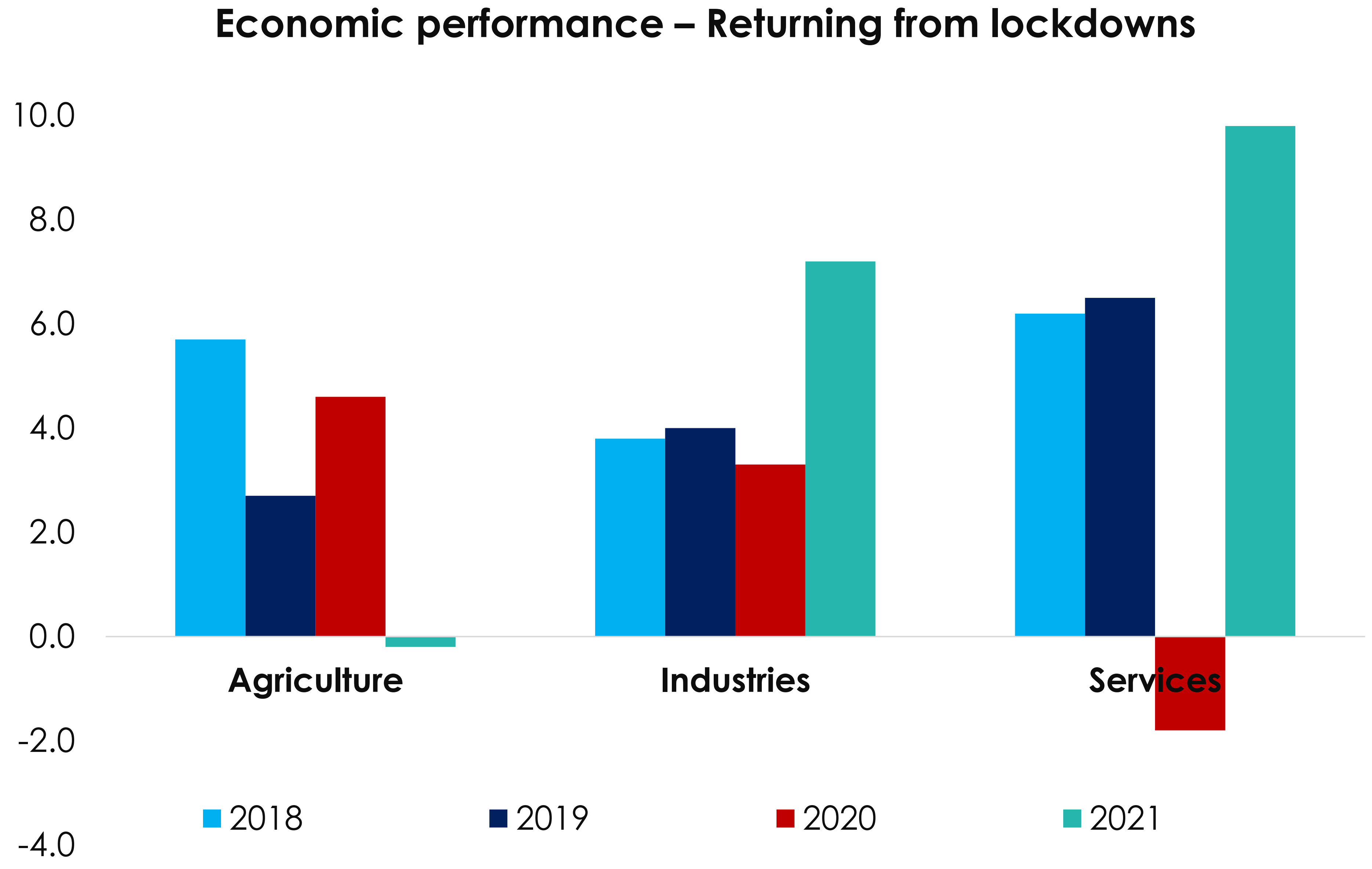




Source: Bloomberg

Kenya – Waning Pandemic Risks and Sound Domestic Spending Sustaining Economic Recovery



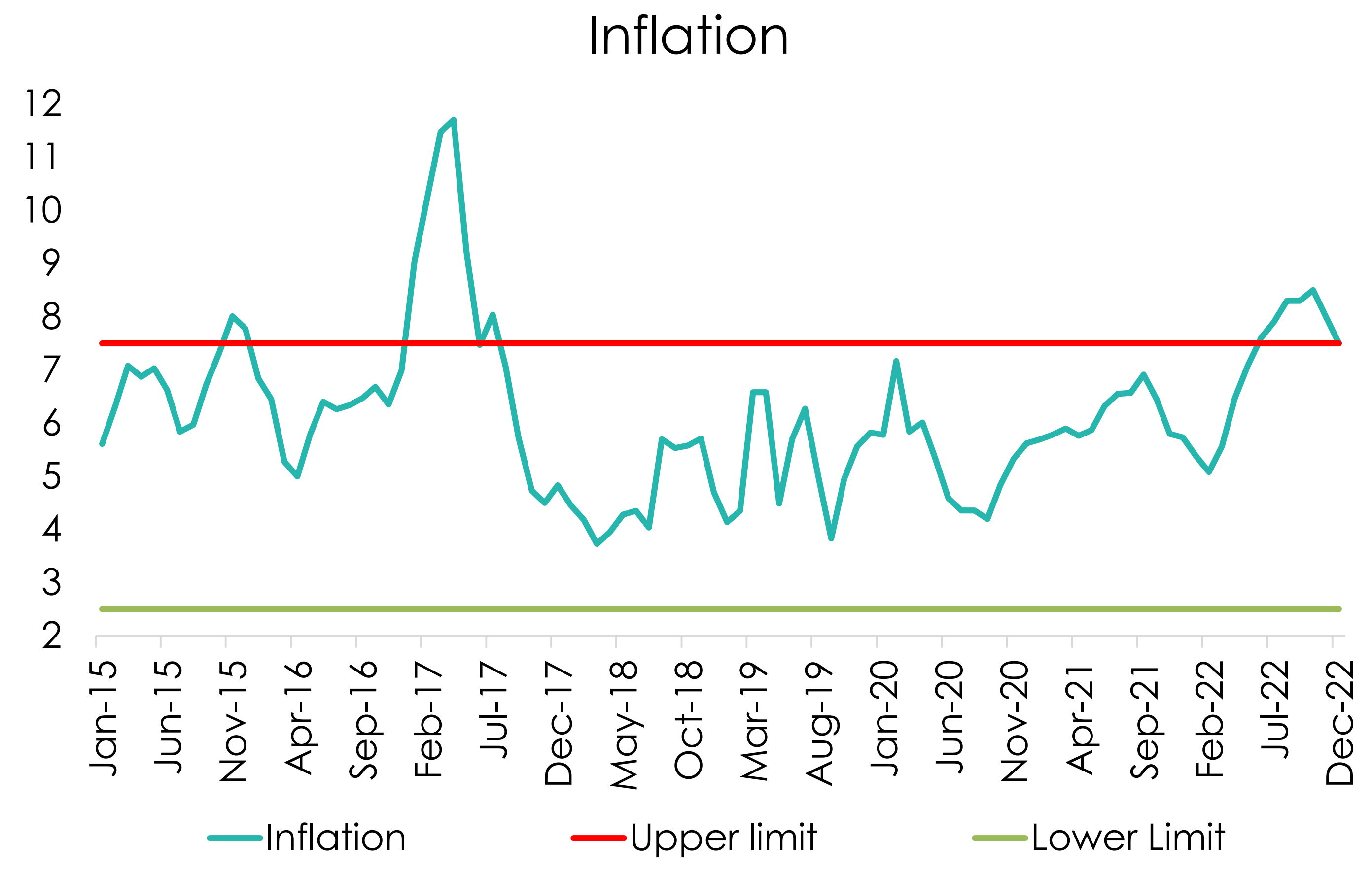


- Recovery from the pandemic still underway underpinned by sustained release of pent up corporate and household demand.
- Through 1H2022, there has been evidence of intrinsic economic vigor supported by sound domestic demand especially for services.

- Recovery in incomes, through job markets, healthy diaspora remittances is supporting household consumption of services.
- Improved domestic and regional demand, recovering global supply chains and spillover effects of sustained public spending have anchored the recovery in industries.
- However, agriculture is still beleaguered by a prolonged drought

Firming Downside Risks, High Base Effects to Shift Growth to a Slower Gear

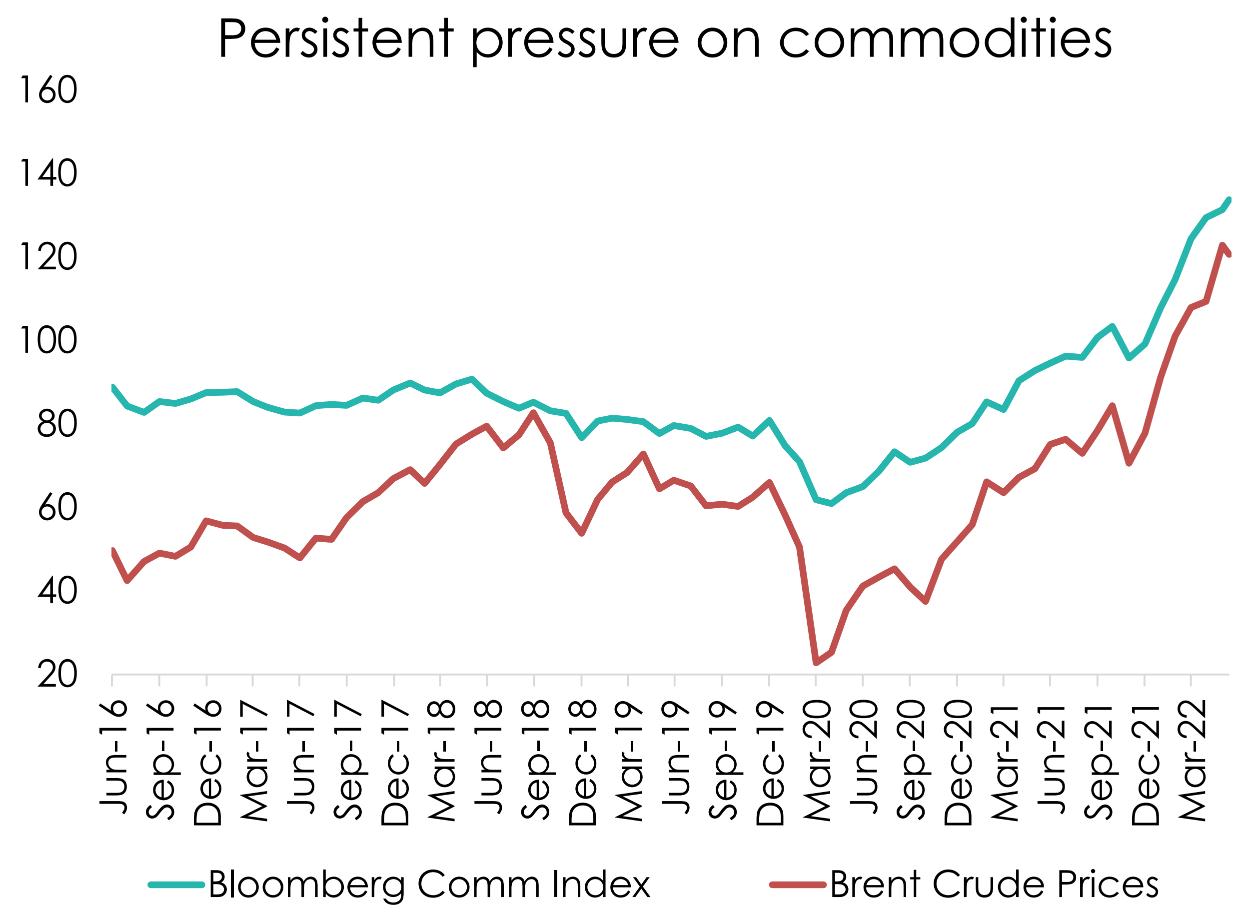
Slower consumer spending as inflation surges



Source: KNBS, NCBA Research

- Consumer spending in Kenya has been increasing by an average of6.0% annually to US$80Bn in 2021.
- Waning purchasing power, rising commodity prices, growing uncertainty will delay and/or dampen related spending.

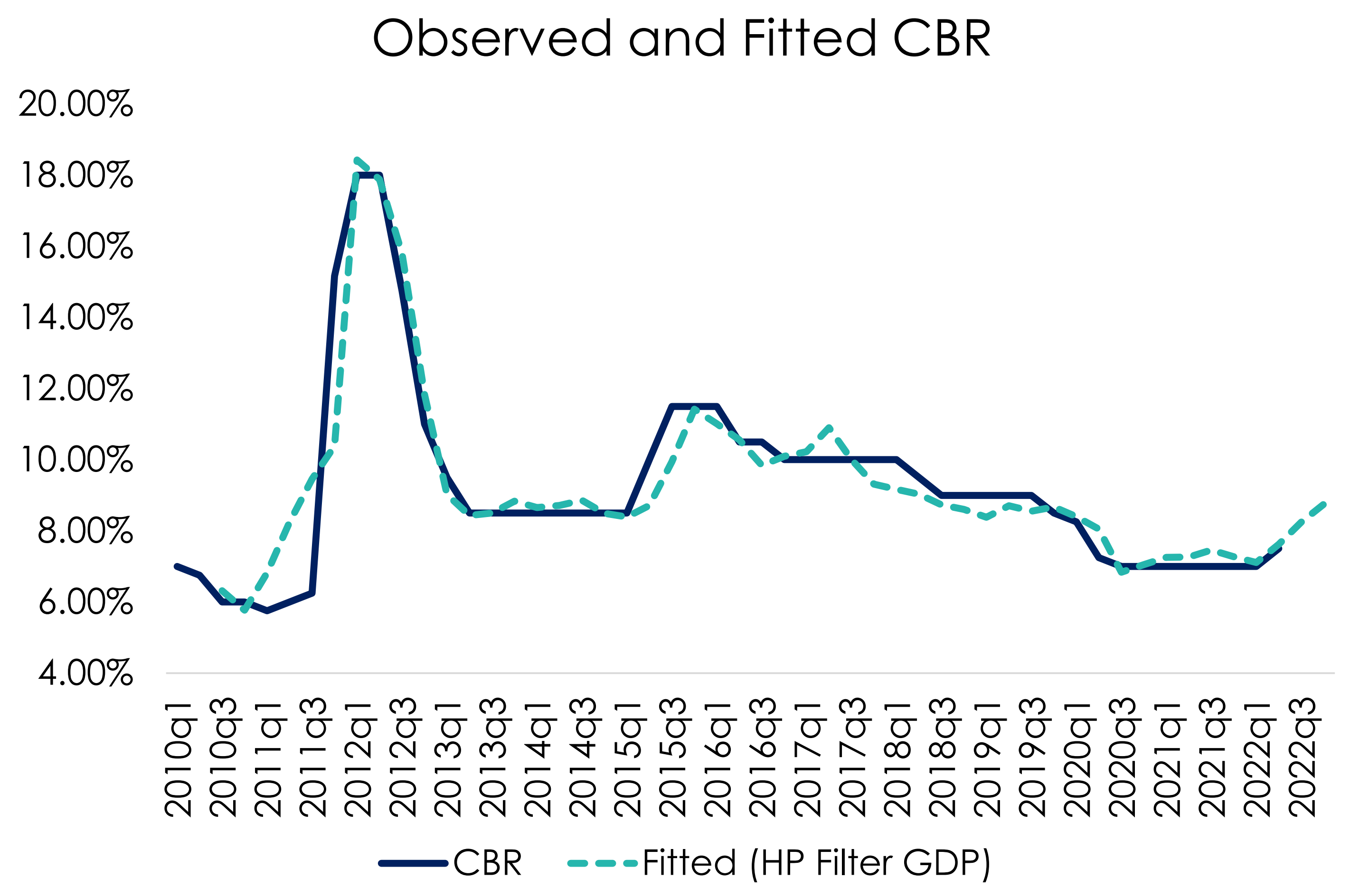
Rising energy and input costs to hurt industries, businesses



Source: Bloomberg

- High energy and input costs will dampen business investments and introduce inefficiencies in industries.
- Energy market outlook is subject to uncertainty surrounding Russia's oil output, OPEC+ production decision and the rate at which the US and other natural gas producers scale up output .

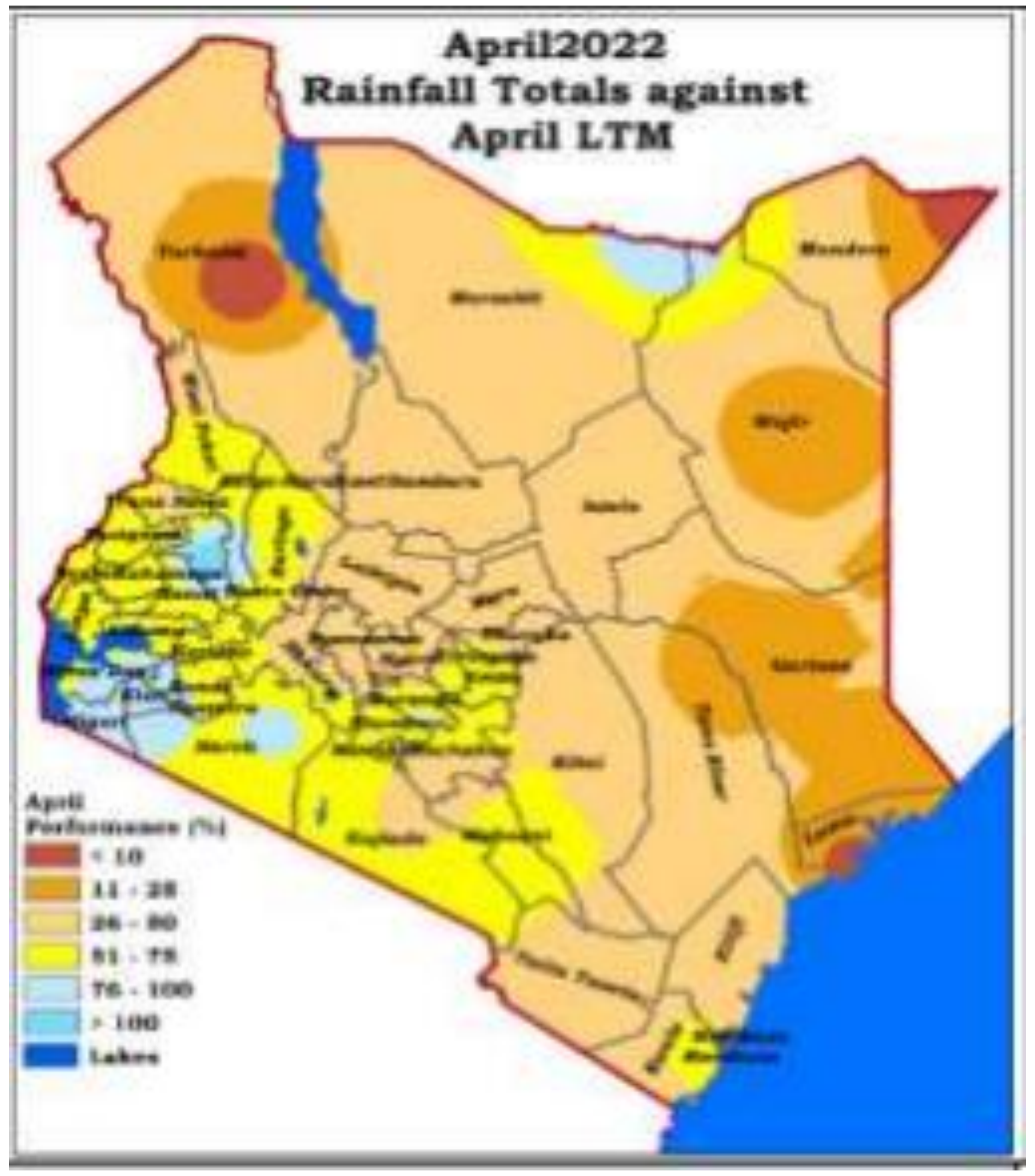
Tightening credit markets to dampen business investments and consumption



- We expect the Central Bank of Kenya to raise interest rates by a further 125bps to anchor inflation expectations.
- Higher interest rates, deteriorating credit risk environment will slowdown lending and demand.
- Increased local fiscal deficit financing risks crowding out of private sector. We expect private sector credit growth to fall back to single digits from 11.0% currently.

Firming downside risks, base effects to shift growth to a slower gear

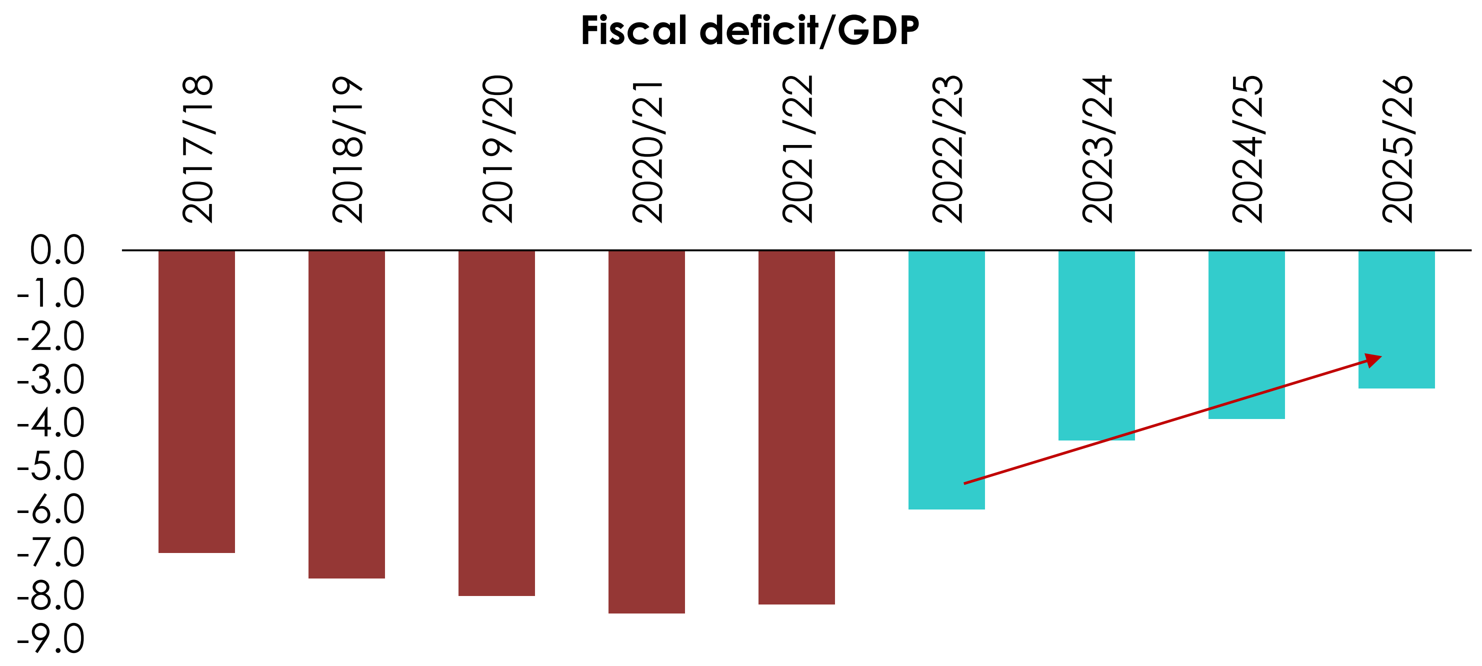
Prolonged Drought

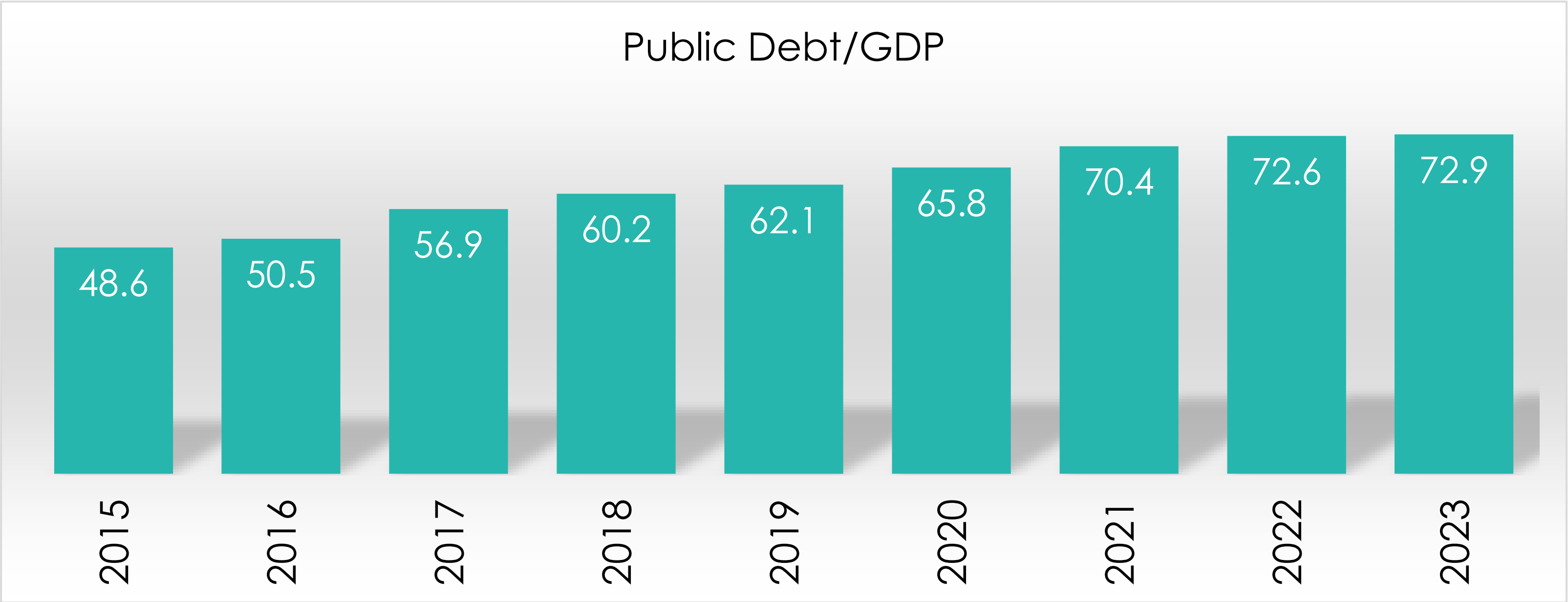


Source: Kenya Meteorological Department

- So far, rainfall has been below average and poorly distributed across 23 counties
- Further drag on agricultural output will have negative knock-on effects on agro-processing and exports

Public finances & Rising interest rates and Debt sustainability concerns

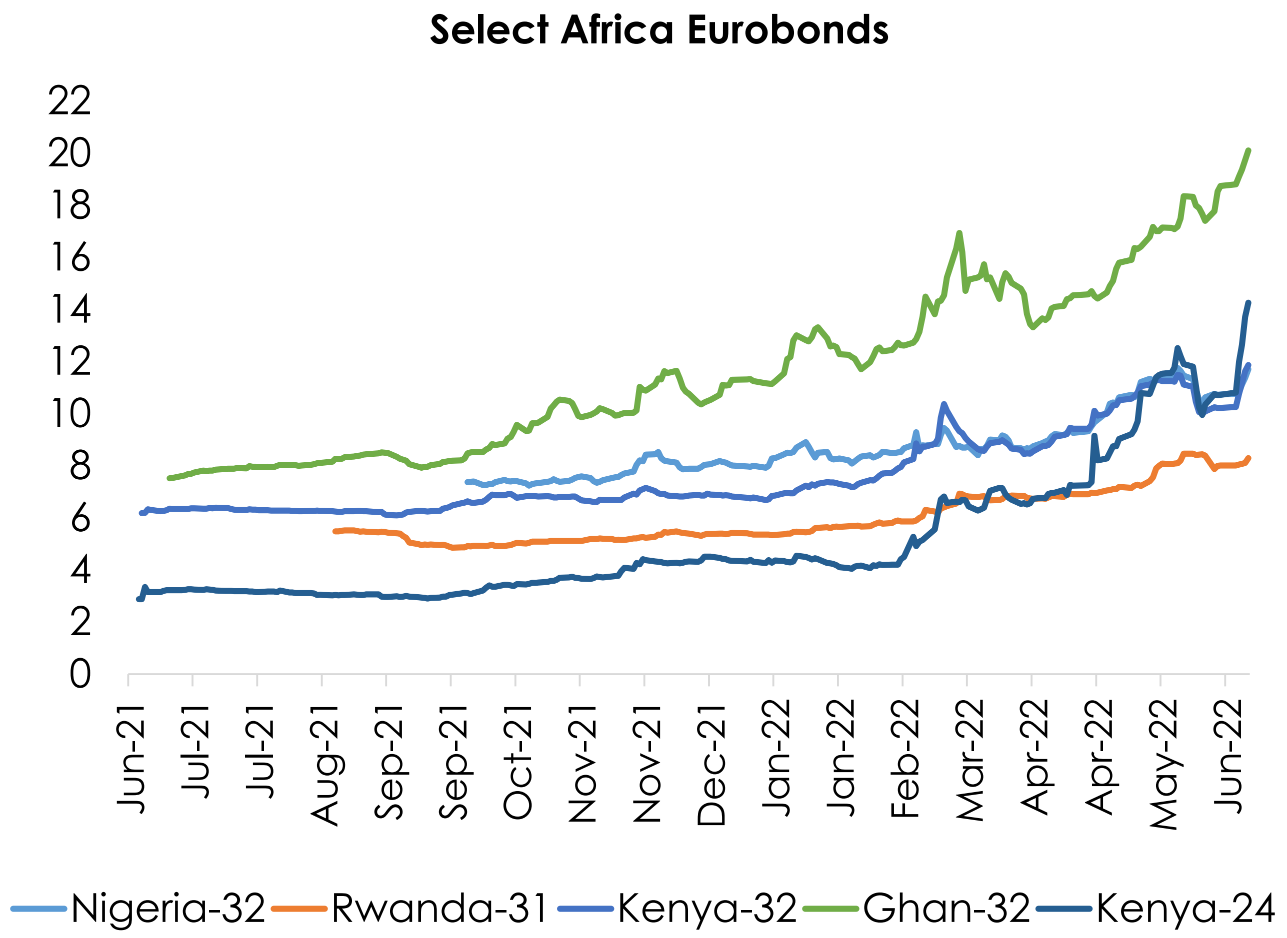




Source: The National Treasury, The IMF

- We expect debt to stabilize at around 70% of GDP in the near term in line with the outlined fiscal consolidation plan.
- However, risks to revenue performance from slower growth and potential social expenditure pressure could delay the reversal in debt/GDP trend.

	Expected Increase in policy Rate	Current rate
Fed	+200 bps	1.50-1.75%
ECB	+50bps	-0.50%
BoE	+100bps	1.00%
CBK	+125bps	7.50%



- Debt service pressure, refinancing costs to increase dramatically in the second half of 2022.
- This will affect sovereign ratings, portfolio flows and the quality of public spending- Crowding out the productive sectors.

Political uncertainty may delay but not reverse investments

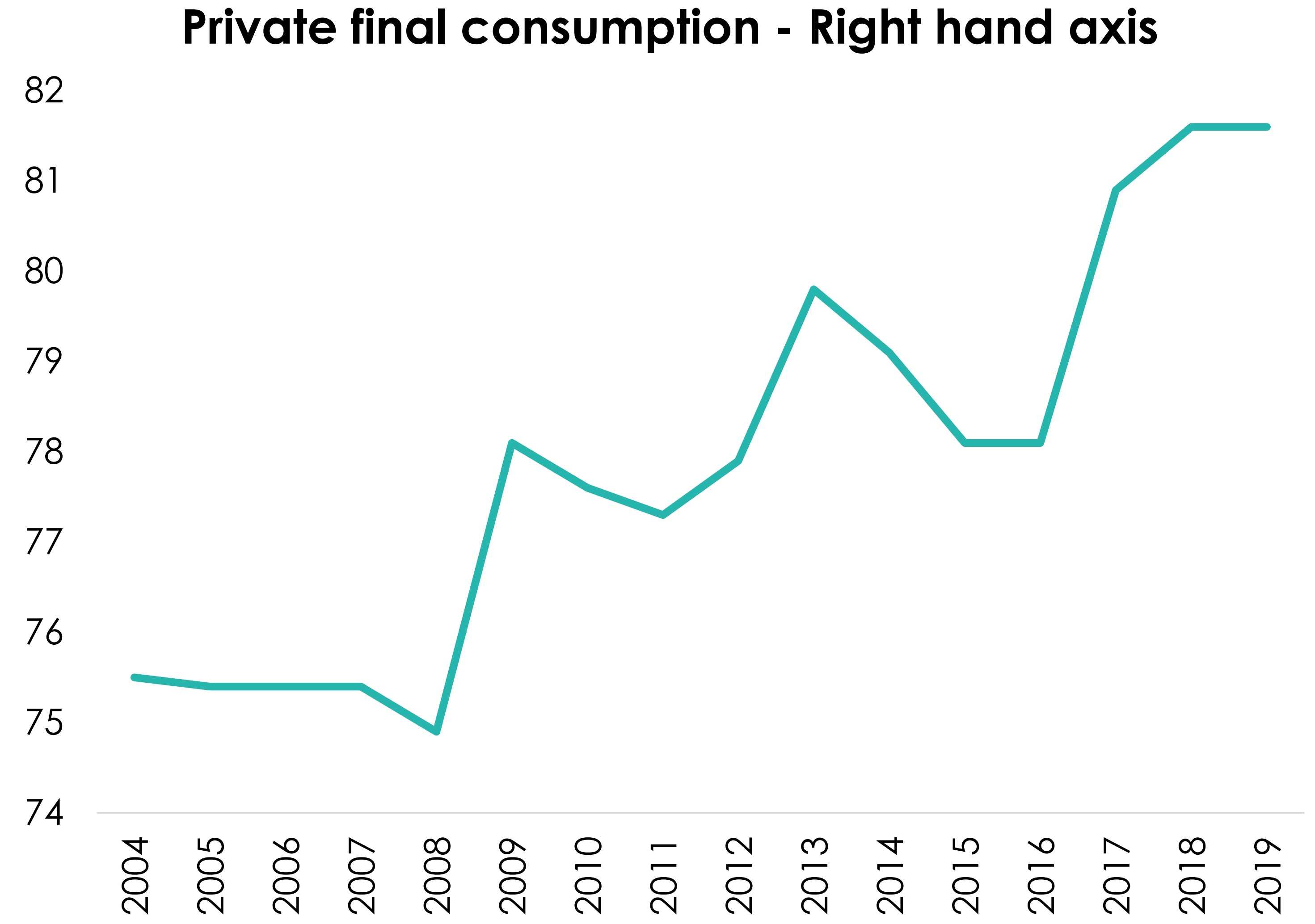
Early indicators point to a tight presidential contest

- Opinion polls, their efficacy notwithstanding suggest a tight contest between the top two presidential candidates.
- So far, campaign narratives for Kenya Kwanza and Azimio coalitions largely point to policy continuity.

Strong confidence in institutional capacity to resolve disputes, with minimal disruptions

Independent, stronger institutions anchoring confidence of a smooth regime change.

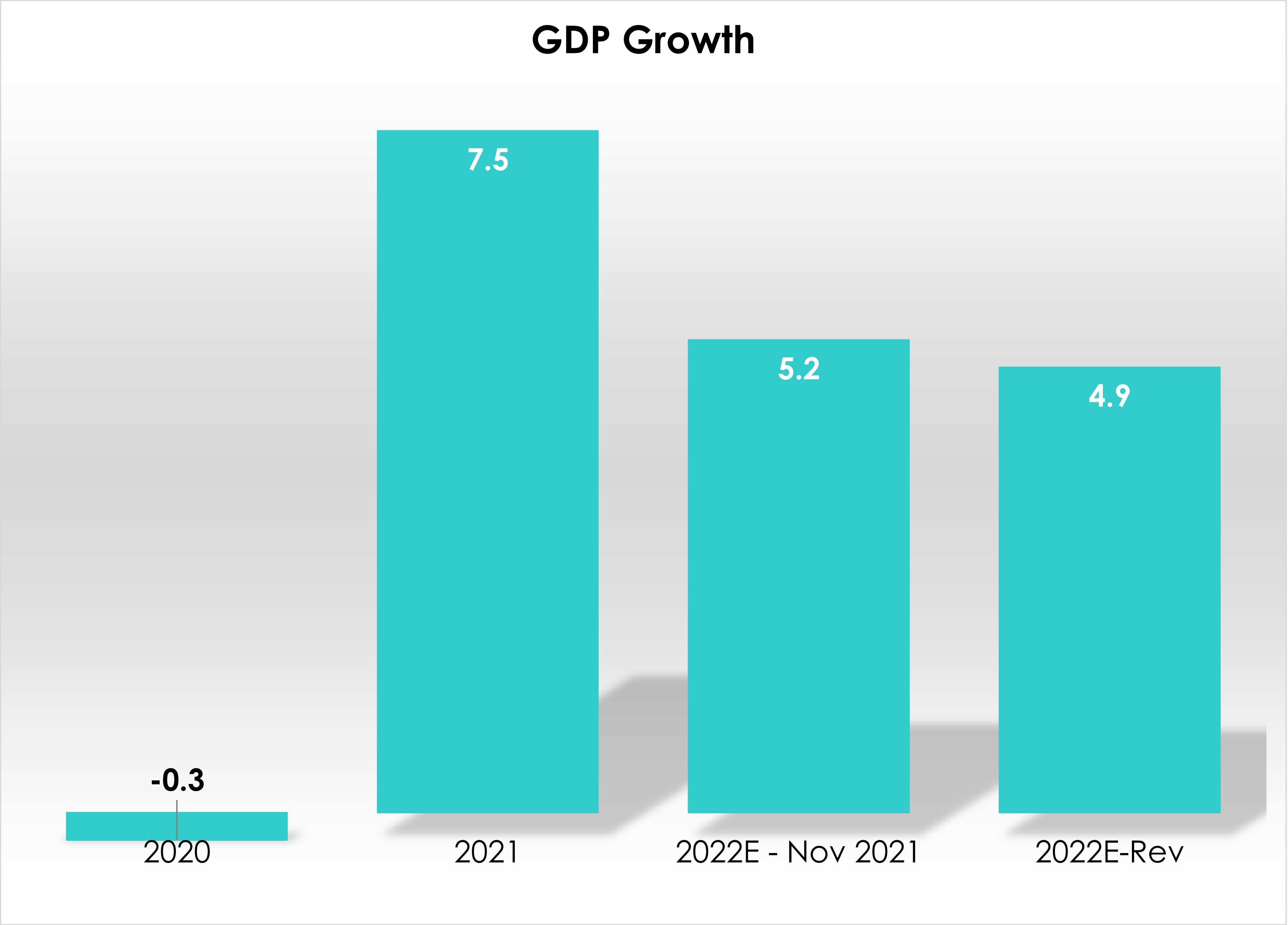
Private consumptions may temporarily slow down before riding the transition dividend wave back up.



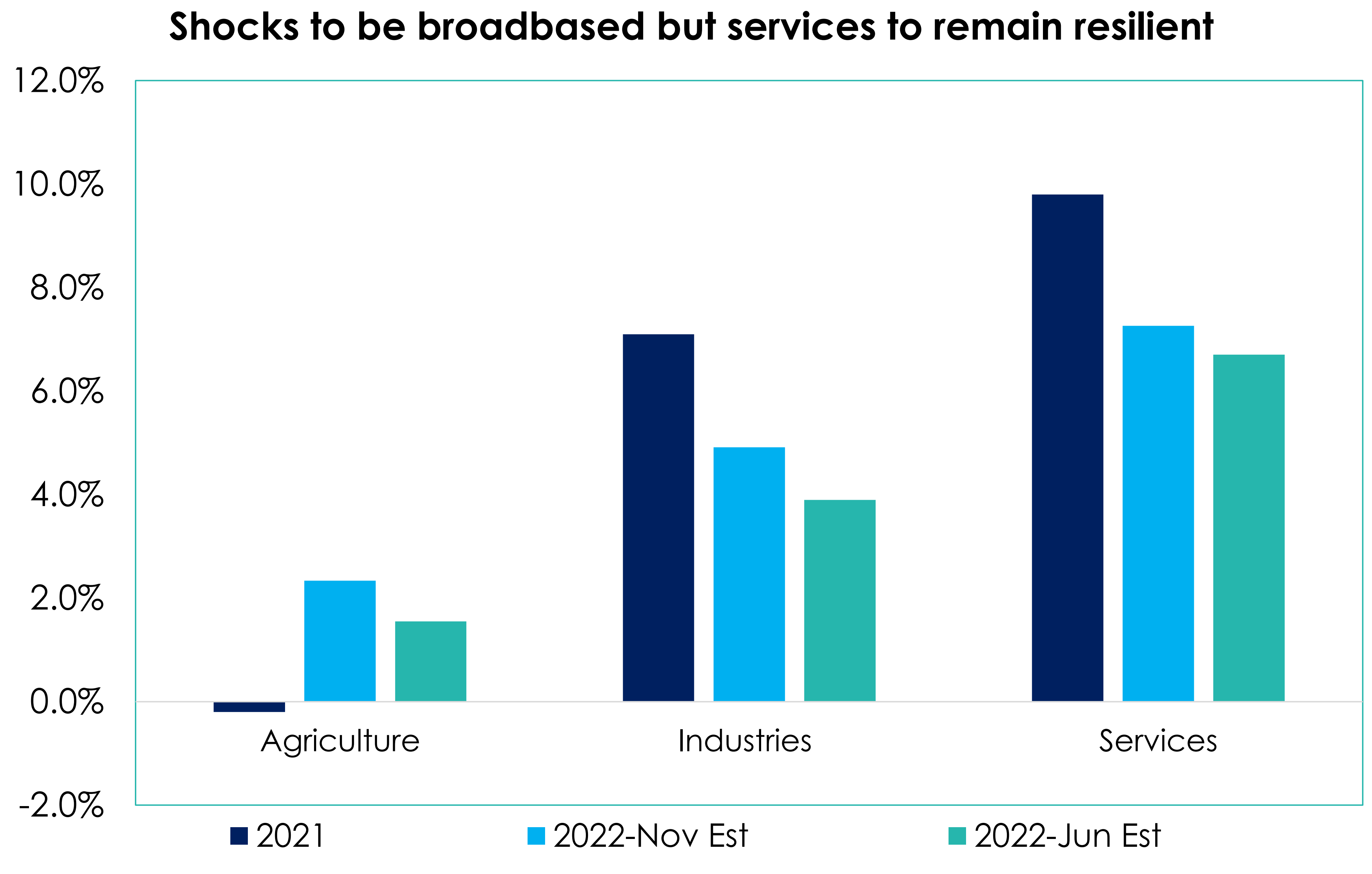
Source: KNBS, NCBA Research

- ✓ Private sector activity, personal consumption is somewhat indifferent to elections.
- ✓ Some mild and transitory volatility evident in highly uncertain election cycles (2007) but the trend reverses after elections.

Firming downside risks, base effects to shift growth to a slower gear - Downgrading our forecasts



Source: KNBS, NCBA Research



Source: KNBS, NCBA Research

- ✓ We expect growth to be 30bps slower than our initial projection with below trend growth in industries and agriculture sectors.

- ✓ Services will remain resilient, supported by sound domestic demand. However, deteriorating purchasing power portends significant risks to the sector.

THANK YOU

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