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PRESS RELEASE

MONETARY POLICY COMMITTEE MEETING, 9TH JULY, 2013

MANAGING RISKS TO MAINTAIN PRICE STABILITY

The Monetary Policy Committee met on 9th July, 2013 to review market developments and evaluate the outcomes of its monetary policy stance since its May 2013 meeting. The Committee noted that inflation had remained within the medium-term target set by the Government while the exchange rate was stable. The Committee also considered the implications of the Budget Policy Statement for the Fiscal Year 2013/14 on monetary policy, and analysed the following positive outcomes in the market since its last meeting:

- Both overall and non-food-non-fuel month-on-month inflation rates remained within the allowable margin of 2.5 percent on either side of the Government's medium-term target of 5 percent. Overall month-on-month inflation increased from 4.05 percent in May 2013 to 4.91 percent in June 2013 reflecting an increase in food prices coupled with the impact of the base effect attributed to the decline in the Consumer Price Index in mid-2012. However, non-food-non-fuel inflation, which measures the impact of monetary policy, declined from 3.91 percent to 3.86 percent during the period. This reflects reduced demand pressure in the economy. In addition, the 3-month annualised overall and non-food-non-fuel inflation rates declined from 8.87 percent to 4.81 percent and from 4.69 percent to 3.48 percent, respectively, in the period. These developments suggest no significant immediate underlying inflation pressure. Furthermore, the declining international oil prices coupled with non-inflationary credit growth support a low and stable short-term outlook for inflation.
- The exchange rate remained stable: it fluctuated within a narrower range of between Ksh.85.29 and Ksh.86.06 for the US Dollar in June 2013 compared with a range of Ksh.83.72 and Ksh.84.88 in May 2013. Exchange rate continuous adjustment to stability in the period was supported by effective liquidity management and rising foreign exchange inflows through diaspora remittances and through foreign investors buying into Government securities. The CBK level of usable foreign exchange reserves increased from USD5,654.74 million (equivalent to 4.18 months of import cover) in April 2013 to USD5,810.60 million (equivalent to 4.22 months of import cover) in June 2013. This level of foreign exchange reserves is above the statutory minimum requirement of 4 months of import cover.
- The Committee noted that the Government's domestic borrowing target of Ksh.106.47 billion for the Fiscal Year 2013/14 was significantly below the Ksh.165.7 billion for the previous Fiscal Year. This borrowing, coupled with the planned issuance of a Sovereign Bond during the Fiscal Year, should ensure that domestic borrowing does not exert pressure on interest rates on Government securities.

- The gradual easing of the monetary policy stance adopted by the Committee coupled with sustained Open Market Operations has resulted in improved liquidity conditions and stability in the interbank market. Consistent with the monetary policy stance, commercial banks' average lending interest rates continued on a gradual downward trend in April and May 2013. Commercial banks have also continued to announce reductions in their base lending rates. The Committee noted that the number of loan applications increased by 36.6 percent from 65,113 in April 2013 to 88,973 in May 2013 across all the bank peer groups.
- The data presented to the Committee on the banking sector and the stress tests conducted on commercial banks indicated that the sector remains solvent and resilient. The Committee observed that gross loans increased by 1.6 percent from Ksh.1,420.5 billion in April 2013 to Ksh.1,442.85 billion in May 2013.
- The latest data from the Kenya National Bureau of Statistics shows that the economy registered a strong growth rate of 5.2 percent in the first quarter of 2013. This mainly reflected the current macroeconomic stability characterised by a low and stable inflation rate and a stable exchange rate, and a strong performance of the agricultural sector which grew at 8.3 percent compared with 2.1 percent in the first quarter of 2012.
- The Committee noted that confidence in the economy has been sustained. The latest World Bank Country Policy and Institutional Assessment rating places Kenya as one of the top two countries in Sub-Saharan Africa. In addition, diaspora remittances increased from USD105 million in April to USD110 million in May 2013. Further, the MPC Market Perceptions Survey conducted in June 2013 showed that the private sector expects inflation and the exchange rate to remain stable in the remainder of the year, and sustained optimism for a strong recovery in growth in 2013.

Despite these developments, the Committee noted that there remain risks to the macroeconomic outlook. These risks emanate mainly from the high current account deficit, and the current instability in the Middle East and North Africa (MENA) and Eurozone which are a threat to the general stability of prices. Previous experience had shown that disturbances in the MENA region could affect the price of oil and tea exports. This could have balance of payments and inflation implications.

The Committee concluded that the monetary policy measures continue to deliver the desired results. However, in view of the above considerations, and the need to provide time for previous MPC decisions to work through the economy, the Committee decided to retain the CBR at 8.50 percent. It will continue to monitor the outcomes on the key macroeconomic aggregates, implementation of the new fiscal programme as well as any emergent risks to ensure that the policy stance continues to deliver price stability.



PROF. NJUGUNA NDUNG'U, CBS
CHAIRMAN, MONETARY POLICY COMMITTEE

9th July, 2013