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PRESS RELEASE

MONETARY POLICY COMMITTEE MEETING, 26TH FEBRUARY, 2015

SUSTAINING STABILITY IN THE MONETARY POLICY PATH

The Monetary Policy Committee (MPC) met on 26th February, 2015 to review market developments and the outcomes that arose from its previous decisions. The Committee noted that overall inflation remained within the Government target range and has continued to support macroeconomic stability. The Committee noted the following outcomes in the market since its meeting in January 2015:

- Overall month-on-month inflation declined from 6.02 percent in December 2014 to 5.53 percent in January 2015 mainly reflecting continued moderation in the prices of fuel, but has risen slightly as predicted to 5.61 percent in February 2015. However, the fall in fuel prices was partly offset by a rise in the prices of some food items. The month-on-month non-food-non-fuel inflation declined from 3.65 percent to 3.43 percent during the period, indicating that there were no significant demand-driven inflationary threats to the economy.
- The exchange rate of the Kenya Shilling against the US Dollar maintained its stable trend despite volatility in the global foreign exchange markets. These were partly occasioned in anticipation of further lowering of interest rates in the Eurozone following the introduction of Quantitative Easing (QE) by the European Central Bank (ECB) and the ending of the Swiss Franc cap against the Euro. The regional and major international currencies have continued to depreciate faster than the Kenya Shilling against the US Dollar and have also exhibited more volatility. The Kenya Shilling has continued to benefit from the strong investor confidence recently boosted by the approval of the International Monetary Fund (IMF) supported precautionary facility. This facility blends the Stand-By Arrangement (SBA) and the Stand-By Credit Facility (SCF) amounting to USD688.3 million and will allow the Government to access resources from the IMF to alleviate balance of payments shocks to the economy. In addition, the continued decline in international oil prices has resulted in a lower oil import bill and eased pressure on the exchange rate.
- The CBK's level of usable foreign exchange reserves stood at USD7,224.19 million (equivalent to 4.65 months of import cover) as at 26th February 2015. This level of foreign exchange reserves coupled with the precautionary IMF support facility is a robust cushion to the exchange rate against short-term shocks that could trigger excess volatility.
- The Central Bank Rate (CBR) continued to coordinate movements in the short-term interest rates during the period. In addition, the liquidity management operations by the CBK, through Open Market Operations (OMO), sustained the stability of the interbank market interest rate.
- The latest data and stress tests on the banking sector showed that it remains resilient, supported by a sound regulatory and supervisory framework and a stable macroeconomic environment. In addition, the introduction of a capital conservation buffer of 2.5 percent above the minimum regulatory core and total capital ratios from 1st

January 2015, has enhanced the resilience of the banking sector. The actual core and total capital ratios were 16.7 percent and 20.0 percent, respectively, at the end of January 2015. These ratios are significantly higher than the minimum core and total capital ratios.

- Updated data from all commercial and microfinance banks show that new and existing loans amounting to Ksh.719.80 billion, excluding the matured loans, had been converted to the Kenya Banks' Reference Rate (KBRR) framework by end of January 2015. The CBK will commence publication of bank specific data on the KBRR on the CBK website to ensure that banks are transparent with respect to the cost and pricing of their products.
- Confidence in the economy remains strong. The 12-month growth in private sector credit stood at 21.8 percent in January 2015. The credit was distributed to the key sectors of the economy. The diaspora remittances have averaged USD122.65 million per month in the six months to January 2015, compared to USD110.84 million per month in a similar period to January 2014. In addition, activity at the Nairobi Securities Exchange (NSE) remains buoyant; the NSE-20 share index rose from 4,971 at the end of December 2014 to 5,468 as at 25th February 2015. Furthermore, the MPC Market Perception Survey conducted in February 2015 showed that private sector firms expect inflation and the exchange rate to be stable, and growth to be stronger in 2015. In addition, the Survey showed that the private sector was optimistic that the business environment would improve in 2015.

On the global scene, the strong performance of the US economy, lower international oil prices and the QE announced by the ECB in January 2015 should provide some economic stimulus. Nevertheless the outlook for global economic growth is mixed. Global growth is projected to pick up from 3.3 percent in 2014 to 3.5 percent in 2015. However, the recovery of the Eurozone economies is expected to remain weak amid the risk of deflation that could slow down demand. Growth in emerging market economies such as Brazil, China, and Russia is projected to decelerate during the period, largely reflecting the impact of weaker commodity prices and vulnerabilities in the banking systems. Although growth in Sub-Saharan Africa is projected to remain almost flat, Kenya's main trading partners in the region are expected to record strong growth. This should benefit Kenya's exports and support exchange rate stability. However, the Committee noted that whilst the US has been contemplating monetary policy tightening, the ECB has embarked on QE, suggesting that there remain mixed signals for the global economy.

The Committee concluded that the monetary policy measures, coupled with the favourable impact of lower international oil prices continued to support price stability. However, the divergent monetary policy paths taken by the major advanced economies may cause volatility in the global foreign exchange markets. This could lead to spill-over effects on the domestic foreign exchange market and domestic inflation that should therefore be monitored. In view of these risks, the Committee decided to retain the CBR at 8.50 percent. The MPC will continue to monitor the key macroeconomic aggregates and any emergent risks from the external and domestic economies that may impact on price stability.

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

26th February, 2015