Governor

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PRESS RELEASE

MONETARY POLICY COMMITTEE MEETING, 7TH JULY, 2015

The Monetary Policy Committee (MPC) met on 7th July, 2015 to review market developments and the outcomes of its previous monetary policy decisions. Overall inflation increased in June 2015, but remained within the Government's target range of 2.5 percent on either side of the 5 percent target.

The Committee noted the following developments since its meeting in June 2015:

- Month-on-month overall inflation increased to 7.0 percent in June 2015 from 6.9 percent in May 2015 mainly reflecting increases in fuel prices, pass-through effects from the weakening Kenya Shilling against the US dollar and moderate demand pressures in the economy. Similarly, the month-on-month non-food-non-fuel (NFNF) inflation increased to 4.6 percent from 4.2 percent during the period. The seasonally-adjusted 3-month annualised measures for overall and NFNF inflation increased slightly during the period, indicating underlying inflationary pressures. Growth in broad money (M3) and credit to private sector were above their respective targets in May 2015.
- The Kenya Shilling has remained under pressure, mainly reflecting the strengthening of the US dollar against most currencies. In addition, the current account deficit widened in part due to increased imports of capital equipment and weak exports. However, diaspora remittances remain resilient. Interventions by Central Bank of Kenya (CBK) through direct sale of foreign exchange to commercial banks in periods of short-term exchange rate have dampened volatility. The CBK's level of usable foreign reserves remain adequate at USD6,630.9 million (equivalent to 4.2 months of import cover). The precautionary facility with the International Monetary Fund provides an additional cushion.
- Government borrowing in the Fiscal Year 2015/16 is anchored in the Medium-Term Debt Management Strategy which aims at maintaining public debt at sustainable levels. In addition, the increased budgetary allocations towards bolstering security and facilitating the recovery of the tourism sector will support the long-term stability of the exchange rate.
- Liquidity conditions in the interbank market changed in the course of the month reflecting drawdown of Government deposits towards the end of the Fiscal Year 2014/15.

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- The banking sector remains resilient and well capitalised. Updated data from all commercial and microfinance banks shows that new and existing loans amounting to Ksh.933.66 billion had been converted to the Kenya Banks' Reference Rate (KBRR) framework by end of May 2015 compared with Ksh.877.45 billion by the end of April 2015.
- The latest data from the Kenya National Bureau of Statistics shows that the economy remained robust in the first quarter of 2015. Growth improved to 4.9 percent in the first quarter of 2015 compared with a growth of 4.7 percent in similar period of 2014.
- The outlook for the global economy remains uncertain. In particular, the recent developments in Greece, possible turbulence in the global markets, and the uncertainty around the timing of increase in US interest rates are cause for concern.

The Committee noted elevated risks to the inflation outlook mainly attributed to pressures on the exchange rate over the last few months. The Market Perceptions Survey of June 2015 showed that private sector firms expected inflation to rise mainly on account of pass-through effects of past exchange rate movements, and increases in fuel prices. However, the Survey showed optimism for an improved business environment by private sector firms in the remainder of 2015 related to continued investment in infrastructure, credit growth to key sectors, and improved confidence in the economy.

In view of these developments, the emerging risks, and the consequent need to anchor inflationary expectations, the MPC decided to raise the Central Bank Rate (CBR) from 10.00 percent to 11.50 percent. Furthermore, the MPC decided to augment its instruments for liquidity management by introducing a 3-day Repo. The MPC will continue to monitor external and domestic developments and their implications on the risks to the overall price stability. In particular, the Committee noted the need to closely monitor liquidity conditions in the market.

In view of the new CBR, the CBK has revised the KBRR consistent with its commitment in January 2015 from 8.54 percent to 9.87 percent. This level of the KBRR will be effective from 7th July, 2015.

Patrick Njoroge

DR. PATRICK NJOROGE
CHAIRMAN, MONETARY POLICY COMMITTEE

7th July, 2015