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PRESS RELEASE

MONETARY POLICY COMMITTEE MEETING

The Monetary Policy Committee (MPC) met on July 24, 2019, to review the outcome of its previous policy decisions and recent economic developments. The meeting was held against a backdrop of domestic macroeconomic stability, increased optimism on the economic growth prospects, and increased global uncertainties.

- Month-on-month overall inflation remained relatively stable and within the target range in May and June 2019. The inflation rate stood at 5.7 percent in June compared to 5.5 percent in May. However, food inflation rose to 6.6 percent in June from 6.0 percent in May, reflecting increases in the prices of non-vegetable food crops particularly maize, due to uncertain supply. Non-food-non-fuel (NFNF) inflation remained below 5 percent, indicative of muted demand pressures and spillover effects of the recent rise in fuel prices. Overall inflation is expected to remain within the target range in the near term largely due to expectations of lower food prices following improved weather conditions, and lower electricity prices with the reduced reliance on expensive power sources. The effect of the July 1, 2019, excise tax indexation is expected to have a moderate impact on inflation.
- The foreign exchange market has remained relatively stable, supported by the narrowing of the current account deficit to 4.2 percent of GDP in the 12 months to June 2019 from 5.4 percent in May 2018. The narrowing reflects strong growth in diaspora remittances, resilient performance of exports particularly horticulture, higher receipts from tourism and transport services and slower growth in imports of food and SGR-related equipment. The current account deficit is expected to narrow to 4.5 percent of GDP in 2019 from 5.0 percent in 2018.
- The CBK foreign exchange reserves, which currently stand at USD9,568 million (6.0 months of import cover), continue to provide adequate cover and a buffer against short-term shocks in the foreign exchange market.
- Private sector credit grew by 5.2 percent in the 12 months to June, compared to 4.4 percent in May. Strong growth in credit to the private sector was observed in the following sectors: manufacturing (11.4 percent); consumer durables (21.3 percent); and private households (7.6 percent). Private sector credit growth is expected to continue to strengthen in the remainder of 2019, partly due to the rollout of innovative, bank-initiated credit products targeting Micro Small and Medium Enterprises (MSMEs).
- The banking sector remains stable and resilient. Average commercial banks' liquidity and capital adequacy ratios stood at 50.6 percent and 18.2 percent, respectively, in June. The ratio of gross non-performing loans (NPLs) to gross loans stood at 12.7 percent in June compared to 12.9 percent in April, partly due to decreases in NPLs in the manufacturing, building and construction, financial services and electricity and water sectors. Banks have continued with mitigation measures against NPLs, including enhanced recovery efforts. This has been supported by the recent payments of pending bills by the Government.

- The economy remained strong in the first quarter of 2019, despite the effects of the delayed long rains on agricultural production. Real GDP growth stood at 5.6 percent, reflecting a stronger than expected performance of agriculture and a resilient services sector, particularly information and communication, accommodation and restaurants, and transport and storage. Leading indicators of economic activity point to stronger growth in the second quarter of 2019. Consequently, growth in 2019 is expected to remain strong, supported by agricultural production, strong growth of MSMEs and the service sector, foreign direct investment, and a stable macroeconomic environment. Additionally, the alignment of the FY2019/20 Government Budget to the *Big 4* priority sectors is expected to boost economic activity in manufacturing, agriculture, construction and real estate, and health sectors.
- The MPC Private Sector Market Perception Survey conducted in July 2019 indicates that inflation expectations remain well anchored within the target range, mainly due to expectations of lower food prices following improved weather conditions. The Survey also shows increased optimism that economic growth will remain strong in 2019 due to, among other factors, continuing payment of pending bills, implementation of the *Big 4* projects, improved weather conditions, ongoing public infrastructure investments, expected growth in tourism, and a stable macroeconomic environment. However, the optimism is tempered by the slow growth in private sector credit and concerns on the volatility of international oil prices.
- The Committee noted the gradual demonetisation (withdrawal of the older KSh. 1,000 notes) and the close monitoring by CBK will ensure that the process is not disruptive to the economy.
- The MPC noted increased uncertainties in the global economy. Global economic growth in 2019 is likely to be weaker than previously anticipated, largely due to escalating trade tensions between the U.S. and China, increased concern with regard to the resolution of Brexit, and volatility in international oil prices partly due to heightened geo-political tensions. These developments may result in increased instability in the global financial markets.

The Committee noted that inflation expectations remained well anchored within the target range, and that the economy was operating close to its potential. However, there is need to be vigilant on the possible effects of the recent increases in fuel prices, the ongoing demonetisation, and the increased uncertainties in the external environment. The MPC concluded that the current policy stance remains appropriate, and therefore decided to retain the CBR at 9.00 percent.

The MPC will continue to closely monitor developments in the global and domestic economy, including any perverse response to its previous decisions, and stands ready to take additional measures as necessary.

Dr. Patrick Njoroge
CHAIRMAN, MONETARY POLICY COMMITTEE

July 24, 2019