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PRESS RELEASE

MONETARY POLICY COMMITTEE MEETING

The Monetary Policy Committee (MPC) met on August 9, 2023, against a backdrop of continued global uncertainties, high but easing inflationary pressures, a weak global growth outlook, geopolitical tensions, and measures taken by authorities around the world in response to these developments. The MPC reviewed the outcomes of its previous decisions and measures implemented to mitigate the adverse economic impact and financial disruptions.

- The global growth outlook is expected to decelerate from 3.5 percent in 2022 to 3 percent in 2023, reflecting the impact of the tightening of monetary policy, and escalation of geopolitical tensions particularly the ongoing war in Ukraine. Additionally, headline inflation rates in advanced economies have continued to ease, but have remained above the respective targets with persistent core inflationary pressures. Commodity prices in the global markets, particularly of oil and food, remain below the peak levels witnessed in 2022.
- Overall inflation in Kenya declined to 7.3 percent in July 2023 from 7.9 percent in June, driven by lower food and non-food non-fuel (NFNF) inflation. The inflation rate, therefore, returned to the target range of 5 ± 2.5 percent. Food inflation eased to 8.6 percent in July from 10.3 percent in June, reflecting declines in prices of key vegetable and non-vegetable food items following improved supply attributed to the long rains, and lower global food prices. Fuel inflation rose to 14.5 percent in July from 12.9 percent in June, mainly reflecting the impact of the increase in electricity prices and implementation of the 16 percent VAT on petroleum products. Nevertheless, fuel inflation was moderated by lower prices of cooking gas following the zero-rating of VAT on liquefied petroleum gas (LPG). The NFNF inflation declined to 3.8 percent in July from 4.1 percent in June, indicating the easing of inflationary pressures attributed to the monetary policy measures. Overall inflation is expected to moderate further in the near term, supported by lower food prices attributed to improving supply of key food items particularly maize, and the implementation of Government measures to improve the supply of sugar through imports.
- A Survey of the Agriculture Sector conducted ahead of the MPC meeting showed that prices of key food items, except sugar and onions, had declined. Additionally, respondents expect the supply of key food items to increase in the coming months with onset of harvests in some regions of the country. Nevertheless, respondents identified weather conditions, transport costs, and high input costs as the major factors impacting output and prices of key food items. The Survey revealed that banks and the Hustler Fund are among the main sources of credit for farmers.

- The recently released GDP data for the first quarter of 2023 showed continued strong performance of the Kenyan economy, with real GDP growing by 5.3 percent. This performance reflects a strong rebound in the agriculture sector due to favourable weather conditions and resilient performance of the services sector. Leading indicators of economic activity pointed to continued strong performance in the second quarter of 2023. Despite the global uncertainties, the economy is expected to continue to strengthen in 2023, supported by resilient services sector, the rebound in agriculture, and implementation of measures to boost economic activity in priority sectors by the Government.
- Goods exports have remained resilient, increasing by 2.1 percent in the 12 months to June 2023 compared to a similar period in 2022. Receipts from tea and manufactured exports increased by 7.0 percent and 23.0 percent, respectively. The increase in tea export receipts reflects higher prices due to demand from traditional markets. Imports declined by 6.1 percent in the 12 months to June 2023 from a growth of 20.2 percent in a similar period in 2022, reflecting lower imports of infrastructure related equipment due to completed projects as well as manufactured goods. Oil prices have continued to ease since the fourth quarter of 2022. Receipts from services exports increased reflecting improvement in international travel and transport. Remittances totalled USD4,017 million in the 12 months to June 2023, and were 0.1 percent higher compared to a similar period in 2022. The current account deficit is estimated at 4.2 percent of GDP in the 12 months to June 2023 and is projected to improve from the 5.1 percent of GDP in 2022 to 4.8 percent of GDP in 2023.
- The CBK foreign exchange reserves, which currently stand at USD7,338 million (4.01 months of import cover), continue to provide adequate cover and a buffer against any short-term shocks in the foreign exchange market.
- The banking sector remains stable and resilient, with strong liquidity and capital adequacy ratios. The ratio of gross non-performing loans (NPLs) to gross loans stood at 14.5 percent in June 2023 compared to 14.9 percent in May. Decreases in NPLs were noted in the transport and communication, agriculture, manufacturing, and personal and household sectors. Banks have continued to make adequate provisions for the NPLs.
- Growth in private sector credit stood at 12.2 percent in June 2023 and 13.2 percent in May. Strong credit growth was observed in manufacturing (18.0 percent), transport and communication (19.9 percent), trade (12.5 percent), and consumer durables (11.8 percent). The number of loan applications and approvals remained strong, reflecting resilience in economic activities.
- The Committee noted the outcome of the FY2022/23 Government Budget operations, which resulted in a lower budget deficit of 5.3 percent of GDP from 6.2 percent of GDP in FY2021/22. Additionally, the MPC noted the ongoing implementation of the FY2023/24 Government Budget, which continues to reinforce fiscal consolidation. The MPC welcomed the efforts by the National Treasury to source new external financing for the Budget. The Committee noted that as a result of the identified new external financing, the projected net domestic borrowing by the Government had been reduced from Ksh.586.5 billion to Ksh.316 billion, which is consistent with our economic programme. The MPC observed that the revised borrowing requirements should exert downward pressure on domestic interest rates, while the additional external financing will bolster the foreign reserves of the CBK.

- In line with the reforms outlined in the White Paper on *Modernisation of the Monetary Policy Framework and Operations*, the MPC also considered and approved a new monetary policy implementation framework designed to enhance monetary policy transmission. This new framework is based on inflation targeting and introduces an interest rate corridor around the Central Bank Rate (CBR) set at ± 250 basis points. Henceforth, the monetary policy operations will be aimed at ensuring the interbank rate, as an operating target, closely tracks the CBR. In addition, to improve access to the Discount Window, the Committee agreed to reduce the applicable interest rate from the current 600 basis points above CBR to 400 basis points above CBR.

The MPC noted that inflation is already within the target band and is expected to decline further as food inflation is expected to come down. The Committee also noted that inflationary pressures had eased as NFNF inflation declined. The Committee further noted that the impact of the tightening of monetary policy in June 2023 to anchor inflationary expectations was still transmitting in the economy. In view of these developments, the MPC decided to retain the Central Bank Rate (CBR) at 10.50 percent.

The Committee will closely monitor the impact of the policy measures, as well as developments in the global and domestic economy, and stands ready to take further action as necessary. The Committee will meet again in October 2023.

Dr. Kamau Thugge, CBS
CHAIRMAN, MONETARY POLICY COMMITTEE

August 9, 2023