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PRESS RELEASE

MONETARY POLICY COMMITTEE MEETING

The Monetary Policy Committee (MPC) met on March 27, 2017, to review the outcome of its policy decisions and recent economic developments. The meeting was held against a backdrop of a sharp increase in food prices due to the prevailing drought in some parts of the country, the continued depressed growth of private sector credit, and uncertainties in the global economy.

- Month-on-month overall inflation rose to 9.0 percent in February from 7.0 percent in January 2017, almost entirely due to increases in food prices. Inflation for all other categories in the CPI basket was below 5 percent. Food inflation rose to 16.5 percent in February from 12.5 percent in January, as a result of the drought conditions. The main food items driving inflation in February were tomatoes, kales (*sukuma wiki*), sugar, maize, oranges, cabbages, Irish potatoes, and milk. Food prices are expected to remain elevated in March and April due to the dry weather conditions, but ease with the long rains. The 3-month annualised non-food-non-fuel inflation remained relatively stable, suggesting that demand pressures were muted.
- The foreign exchange market has remained stable. This has been supported by a narrower current account deficit mainly due to lower imports of petroleum products, machinery and transport equipment. Additionally, inflows from horticulture, tourism, and diaspora remittances are resilient.
- The CBK’s foreign exchange reserves currently stand at USD7,762 million (5.1 months of import cover) compared to USD6,963 million (4.6 months of import cover) at the end of January 2017. The increase is largely due to inflows of planned external loans of the Government. These reserves, together with the Precautionary Arrangements with the International Monetary Fund (IMF), equivalent to USD1.5 billion, continue to provide an adequate buffer against short-term shocks.
- The banking sector remains resilient. Average commercial banks’ liquidity and capital adequacy ratios stood at 43.2 percent and 19.7 percent respectively in February 2017. However, the ratio of gross non-performing loans to gross loans increased to 9.7 percent in February 2017, largely due to tighter credit standards and slower credit growth.

- The Committee noted that the slowdown in credit growth largely reflected sector developments in trade, manufacturing, real estate, and private households, which account for 60 percent of total credit to the private sector. The contribution of these sectors to total credit growth declined gradually to 4.6 percentage points in February 2017, from 13.6 percentage points in July 2015. This was partly due to: a slowdown in exports by the manufacturing sector, delays in registration of land titles and building approvals, and, availability of alternative external financing for key private sector projects.
- The MPC reviewed preliminary analyses of the impact of the Banking (Amendment) Act 2016 that was implemented in September 2016. While the growth of private sector credit has stabilized at 4.0 percent, the share of loans to corporates has increased relative to business and personal loans. The average maturity of loans has also shifted to short term lending. The number of loan applications increased between September and December 2016, but has stabilized to February 2017. However, loan approvals declined by 6 percent between December 2016 and February 2017. Lending to Micro, Small, and Medium Enterprises (MSMEs) has declined in value terms, reflected in reduced lending by large and medium banks. A survey of commercial bank credit officers indicates that their expectations are that while demand for credit would increase with the interest rate caps, actual credit granted would remain constant as a result of tighter credit standards. While these are the early indications of the impact of the interest rate caps, banks are still adjusting their business models to ensure that they remain competitive in the new environment.
- The MPC Market Perception Survey conducted in March 2017 showed that private sector respondents expect a decline of growth in 2017, on account of the prevailing drought conditions and slowdown in private sector credit growth. However, the respondents expect the ongoing public investment in infrastructure to continue to be supportive growth.
- The outlook for global growth in 2017 remains uncertain largely due to the economic policies of the new U.S. administration, the Brexit outcome, and the pace of normalizing monetary policy in the advanced economies.

The Committee concluded that overall inflation is expected to remain outside the Government target range in the near term due to the elevated food prices, even as demand pressures remain subdued. The Committee remains concerned about the prevailing uncertainties, including the impact of the interest rate caps on the effectiveness of monetary policy. The MPC therefore decided to retain the Central Bank Rate (CBR) at 10.0 percent. The Committee will continue to closely monitor developments in the domestic and global economies, and stands ready to take additional measures as necessary.

Dr. Patrick Njoroge
CHAIRMAN, MONETARY POLICY COMMITTEE

March 27, 2017