

Cytonn Note on the 8th October 2024 Monetary Policy Committee (MPC) Meeting

The Monetary Policy Committee (MPC) is set to meet on Tuesday, 8th October 2024, to review the outcome of its previous policy decisions and recent economic developments, and to decide on the direction of the Central Bank Rate (CBR). In their [previous](#) meeting held on 6th August 2024, the committee noted that they would closely monitor the impact of the policy measures taken, as well as developments in the global and domestic economy, and stood ready to reconvene earlier if necessary. Additionally, the MPC decided to cut the CBR by 25.0 bps citing that its previous interventions successfully curbed inflation, mitigated exchange rate pressures, and stabilized inflationary expectations which came in at 4.4% and 3.6% in August and September 2024 respectively, remaining within the CBK target range of 2.5%-7.5%. This was in line with our [expectation](#) for the MPC to lower the CBR rate, with our view having been informed by:

- i. Inflation had remained within the bank's target of 2.5% -7.5% for the eleventh consecutive month on account of the relatively stable food prices being experienced in the country at the time as a result of the favorable weather conditions. Given that one of the main goals of monetary policy is to ensure price stability, we believed that the stable inflation rate which came in at 4.3% in the month of July would give the MPC room to loosen the central bank rate,
- ii. The need to maintain the then appreciation of Shilling and stabilize it from volatility as other Central Banks maintained high rate. Since the previous meeting, the Kenyan Shilling had appreciated by 0.8% against the US Dollar to Kshs 129.9 as at 31st July 2024, from Kshs 130.5 recorded on 5th June 2024 mainly attributable to eliminated credit risk from the Eurobond buyback, as well as increased dollar supply in the market. As such, a cut in the CBR rate would help support the economy, and
- iii. The need to support the economy by adopting an accommodative policy that would ease financing activities. The Purchasing Managers Index (PMI) had come in below the 50.0 threshold, with the June 2024 PMI coming in at 47.2, an indication the business environment was in the contraction zone. An cut in the CBR rate would help support the economy.

The Monetary Policy Committee noted that the current account deficit is estimated at 3.7% of GDP in June 2024, down from 4.2% in June 2023, and is projected at 4.0% of GDP in 2024, reflecting the expected recovery in exports, resilient remittances, and expected rebound in agricultural exports. Additionally, the Monetary Policy committee noted that Goods exports increased by 5.0% in the 12 months to June 2024, compared to a similar period in 2023, reflecting a rise in exports of agricultural commodities and re-exports. The increase in exports in 2024 was across several categories, including tea and vegetable & fruits and agricultural re-exports, which saw respective increases of 4.6%, 12.1% and 56.5%. Imports declined by 3.3% in the twelve months to June 2024 compared to a similar period in 2023, mainly reflecting lower imports across all categories except sugar, machinery and transport equipment, crude materials and miscellaneous manufactures. Tourist arrivals improved by 27.2% in the twelve months to June 2024 and were 12.9% higher compared to USD 4,017.1 million in a similar period in 2023. Remittances increased by 12.9% to USD 4,535.5 million in the twelve months to June 2024 from USD 4,017.1 million in a similar period in 2023.

Additionally, The Committee noted the ongoing implementation of the FY2024/25 Government Budget, which is expected to continue to reinforce fiscal consolidation. Notably, total revenue collected as at the end of August 2024 amounted Kshs 331.6 bn, equivalent to 12.6% of the revised estimates of Kshs 2,631.4 bn for FY'2024/2025 and is 75.6% of the prorated estimates of Kshs 438.6 bn. The total expenditure amounted to Kshs 439.9 bn, equivalent to 10.5% of the revised estimates of Kshs 4,207.9 bn, and is 62.7% of the prorated target expenditure estimates of Kshs 701.3 bn. Additionally, the net disbursements to recurrent expenditures came in at Kshs 162.4 bn, equivalent to 12.4% of the revised estimates of Kshs 1,307.9.

Below, we analyze the trends of the macro-economic indicators since the August MPC meeting, and how they are likely to affect the MPC decision on the direction of the CBR:

Indicators	Experience since the last MPC meeting in August 2024	Our Expectation Going forward	CBR Direction (August 2024)	Probable CBR Direction (October 2024)
Government Revenue Collection	<ul style="list-style-type: none"> Total revenue collected as at the end of August 2024 amounted to Kshs 331.6 bn, equivalent to 12.6% of the revised estimates of Kshs 2,631.4 bn for FY'2024/2025, and is 75.6% of the prorated estimates of Kshs 438.6 bn. Cumulatively, tax revenues amounted to Kshs 312.8 bn, equivalent to 12.6% of the revised estimates of Kshs 2,475.1 bn and 75.8% of the prorated estimates of Kshs 412.5 bn The government was unable to meet its prorated revenue targets for the second consecutive month of the FY'2024/2025, attaining 75.6% of the revenue targets in August 2024, mainly on the back of the tough economic situation exacerbated by the elevated high credit cost in the country, with the commercial banks weighted average lending rates for the month of August 2024 coming in at 16.8% remaining relatively unchanged from the figure recorded in June. The cost of living remains elevated in the country, which continues to impede revenue collection despite an improvement in business environment with the PMI coming in at 50.6 in August 2024 from the 43.1 recorded in July 2024. In light of this, the government is yet to fully benefit from the strategies put in place to improve revenue collection such as expanding the revenue base and sealing tax leakages, and suspension of tax relief payments. The coming months' revenue collection performance will largely depend on how quickly the country's business climate stabilizes. This stabilization is expected to be aided by the ongoing appreciation of the Shilling, which gained by 0.7% against the dollar in the since the last meeting in August, easing inflationary pressures, and, an ease in the monetary policy in the country, with the Monetary Policy Committee (MPC) announcing a downward revision of the Central Bank Rate (CBR) by 25 bps to 12.75% from 13.00% following their last meeting on 6th August 2024. 	<ul style="list-style-type: none"> In the short term, we expect the revenue collections to be affected as a result of the withdrawal of the Finance Bill 2024. We expect a revenue shortfall for the FY2024/2025 budget, and will likely result in Kenya missing the 4.7% fiscal deficit target this year. The proposed raft of tax changes in the Finance Bill 2024 were geared towards expanding the tax base and raising revenues to meet the government's budget for the fiscal year 2024/2025 of Kshs 3.9 tn. The government's continued efforts to broaden the tax base will have been hampered. Among the key provisions in the Act included a removal of VAT exemption for several financial services, making them subject to the standard VAT rate of 16.0%, introduction of a new 2.5% tax on the value of motor vehicles, payable when issuing insurance cover, and taxing income from digital marketplaces or platforms and digital content monetization at 20.0% for non-residents and 5% for residents. As such, we expect the tax collections to be hindered in the long-term and thus impede the government's efforts to meet its revenue collection targets Nevertheless, given the improving general business environment which is underpinned by the appreciation of the Kenyan shilling, easing liquidity in the money market, and easing inflationary pressures, we expect these to support the tax revenue, but remain wary of the unpredictable tax regime that may weigh down the collections. 	Negative	Negative
Government Borrowing	<ul style="list-style-type: none"> The government, as at 27th September 2024, was 121.2% ahead its prorated net domestic borrowing target of Kshs 102.1 bn having borrowed Kshs 225.9 bn of the total borrowing target of Kshs 408.4 bn. The government 	<ul style="list-style-type: none"> Kenya's rising debt sustainability remains a significant concern with the government's borrowing appetite remaining high given the subdued economic environment coupled with an ever-present fiscal deficit. While 		

	<p>currently has domestic maturities worth Kshs 918.7 bn and will have to borrow Kshs 121.9 bn monthly to meet the upcoming domestic maturities and the budget deficit in the FY'2024/2025</p> <ul style="list-style-type: none"> e. Total Borrowings as at the end of August 2024 amounted to Kshs 105.3 bn, equivalent to 6.9% of the revised estimates of Kshs 1,571.8 bn for FY'2024/2025 and are 40.2% of the prorated estimates of Kshs 262.0 bn. The cumulative domestic borrowing of Kshs 978.3 bn comprises of Net Domestic Borrowing Kshs 408.4 bn and Internal Debt Redemptions (Rollovers) Kshs 569.9 bn Kenya has continued to receive financing from the World Bank and other bilateral lenders such as the International Monetary Fund (IMF). Recently, the Executive Board of the IMF announced that it had reached a staff-level agreement on a set of comprehensive policies and reforms needed to complete the seventh reviews of Kenya's Extended Fund Facility (EFF) and Extended Credit Facility (ECF) arrangements and the second review under the Resilience and Sustainability Facility (RSF) arrangement. Notably, upon completion of the seventh review of Kenya's economic program under the Extended Fund Facility (EFF) and Extended Credit Facility (ECF) arrangements, the total IMF financial commitment during the duration of the EFF/ECF program to about USD 3.60 bn (KES 466.1 bn). In addition, the completion of the second Review under the Resilience and Sustainability Facility (RSF), approved on July 17, 2023, would unlock USD 120 mn (KES 15.5 bn). 	<p>credit risk was significantly reduced with the Eurobond buyback in February, and subsequent June maturity payment, the debt servicing costs are expected to remain high. This has led to Credit rating agencies such as Moody's Credit Rating Agency, S&P Global Rating and Fitch to downgrade Kenya's credit. Notably, Kenya's latest rating by Moody was at Caa1 for both local issuer and foreign currency issuer an indication of a high credit risk, while the outlook remained negative. In addition, Fitch Ratings revised Kenya's credit score, downgrading it to B- from a credit rating of B while also revising the outlook to stable, from a negative outlook affirmed on 16th February 2024. Additionally, &P Global Ratings announced its revision of Kenya's long-term sovereign credit rating, downgrading it to B-, and a stable outlook from a credit rating of B and a negative outlook</p>	Negative	Negative
Inflation	<ul style="list-style-type: none"> Year on year (y/y) inflation rate for September 2024 decreased by 0.8% points to 3.6%, from the 4.4% recorded in August 2024. This was in line with our expectation of a decrease. Our projection was mainly driven by the reduction in electricity prices and the stability of fuel prices. With fuel and electricity being major production inputs, we projected that this reduction would lead to a decrease in the inflation rate Super Petrol, Diesel and Kerosene remaining unchanged from the prices announced for the previous period. Consequently, Super Petrol, Diesel and Kerosene will continue to retail at Kshs 	<ul style="list-style-type: none"> We expect inflation rates to remain within the CBK's target range of 2.5% - 7.5% supported by the current fiscal stance as CBR is expected to remain elevated in the medium term, as the MPC continues to implement its scope on easing the CBR. Additionally, the recent appreciation of the Kenyan shilling against major currencies, which has so far appreciated by 17.7% on YTD against the dollar is expected to keep inflationary pressures in the country down as manufacturers get relief with the lower importation costs of inputs 	Positive	Positive

	<p>188.8, Kshs 171.6 and Kshs 161.8 per litre respectively.</p> <ul style="list-style-type: none"> Notably, August's overall headline inflation was on the rise for the first time in two months. Furthermore, it has remained within the Central Bank of Kenya (CBK) target range of 2.5% to 7.5% for the fourteenth consecutive month. 			
Currency (USD/Kshs)	<ul style="list-style-type: none"> Since the last meeting, the Kenyan Shilling has appreciated by 0.7% against the US Dollar to Kshs 129.2 as at 3rd October 2024, from Kshs 130.1 recorded on 6th August 2024 mainly attributable to improved foreign reserves which are currently above the statutory requirement In addition, the Forex Reserves have increased significantly by 10.4% to USD 8.0 bn (equivalent to 4.1 months of import cover) as of 27th September 2024 from USD 7.3 bn (equivalent to 3.8 months of import cover) recorded on 2nd August June 2024. Notably, the forex reserves are above the statutory requirement of maintaining at least 4.0 months of import cover and lower than the EAC region's convergence criteria of 4.5 months of import cover 	<ul style="list-style-type: none"> We expect the Kenyan Shilling to be supported by Diaspora remittances standing at a cumulative USD 4,645.0 mn in the 12 months to August 2024, 12.7% higher than the USD 4,120.0 mn recorded over the same period in 2023, which has continued to cushion the shilling against further depreciation. In the August 2024 diaspora remittances figures, North America remained the largest source of remittances to Kenya accounting for 56.0% in the period Additionally, the shilling performance and strength is expected to be supported by the sufficient forex reserves currently at USD 8.0 bn (equivalent to 4.1 months of import cover) as of 27th September 2024 from USD 7.3 bn (equivalent to 3.8 months of import cover) recorded on 2nd August 2024. Moreover, tourism inflow receipts which came in at USD 352.5 bn in 2023, a 31.5% increase from USD 268.1 bn inflow receipts recorded in 2022, and owing to tourist arrivals that improved by 27.2% in the 12 months to June 2024, from the arrivals recorded during a similar period in 2023 	Positive	Positive
GDP Growth	<ul style="list-style-type: none"> Kenyan's economy recorded a 5.0% growth in Q1'2024, slower than the 5.5% growth recorded in Q1'2023, pointing towards a slower economic growth. The performance was driven by; <ul style="list-style-type: none"> i. The positive growth recorded in all sectors except Mining and quarrying, with most sectors recording a decline compared to Q1'2023 with Accommodation & Food Services, Mining & Quarrying and Construction Sectors recording the highest declines of 19.1%, 3.8%, and 2.9% points, respectively. Other sectors that recorded a contraction in growth rate, from what was recorded in Q1'2023 were Transport and Storage, Other Services and Public Administration sectors, of 2.8%, 2.1% and 1.8% points respectively; 	<ul style="list-style-type: none"> We expect Kenya's GDP to continue growing at a slower pace in line with the global economy trends. However, the economy will be supported by sustained recovery in sectors like accommodation and food services sector, as well as recent fiscal policies such as subsidizing costs of crucial farm inputs such as fertilizer that are expected to support growth in the agriculture sector, which remains to be Kenya's largest contributor to GDP, The continued appreciation of the Kenya shilling has continued to support the business environment, by reducing the cost of imported inputs and decreasing the finance cost of the foreign currency denominated debts Notably, the country's PMI for the month of August 2024 increased to 	Neutral	Neutral

	<p>ii. The slowed growth in the Agricultural Sector with Agriculture and Forestry recording a growth of 6.1% in Q1'2024. The performance was a decrease of 0.3% points, from the expansion of 6.4% recorded in Q1'2023. The slower growth recorded during the quarter was mainly attributable to decline in exports of coffee, fruit and cut flowers. Coffee exports declined by 13.8% to stand at 9,722.3 metric tonnes in Q1'2024 from the 11,284.9 metric tonnes recorded in Q1'2023.</p>	<p>50.6, up from 43.1 in July, to move into the expansion zone, an indication of a improved business environment in the country. Likewise, according to CEO's survey- July 2024 report, the growth prospects for the Kenyan economy are moderate, but easing inflation, stability of the Shilling, and expectations of future rate continue to support growth. The survey however notes that July protests negatively affected the growth prospects, but the country has been relatively stable since</p>		
Private Sector Credit Growth	<ul style="list-style-type: none"> The latest data from CBK indicates that private sector credit growth declined to 4.0% in June 2024 from 4.5% in May 2024, mainly attributed to exchange rate valuation effects on foreign currency-denominated loans due to the appreciation of the Shilling. Notably, the 4.0% growth rate recorded in June 2024 is the lowest recorded figure in 31 months. 	<ul style="list-style-type: none"> We anticipate continued adoption of the risk-based pricing model in the banking sector to continue to unlock access to credit to individuals and businesses who were not captured by the previous frame works due to being considered too risky, However, the increased government borrowing is expected to continue crowding out the private sector in the short term as seen by the weighted average yield for T-Bonds coming at 17.1% in the month of September effectively edging out majority of the corporate bonds currently in the trading in market Additionally, banks have started to adjust their lending rates in line with the CBR rate which was cut to 12.75% in the August MPC meeting. This is expected to revitalize the private sector credit demand 	Positive	Positive
Liquidity	<ul style="list-style-type: none"> Liquidity levels in the money markets eased significantly, with the average interbank rate since the previous MPC meeting decreasing significantly by 0.4% points to 12.7% on 27th September 2024 from the 13.1% as of 6th August 2024, partly attributable to tax remittances that offset Government payments. 	<ul style="list-style-type: none"> We expect liquidity in the money markets to be supported by the domestic debt maturities that currently stand at Kshs 601.6 bn worth of T-bill maturities for FY'2024/2025. 	Positive	Positive

Conclusion

Out of the seven factors that we track, four are positive, one is neutral and two are negative. Notably, most of the Central Banks of developed economies around the world have cut their rates with the aim of supporting economic activities and growth going forward.

The main goal of monetary policy is to maintain price stability and support economic growth by controlling the money supply in the economy. We expect the MPC to cut the Central Bank Rate (CBR) to the range of 12.25%-12.50% with their decision mainly being supported by:

- i. Rate cuts by global giant economies. In their last sitting on September 18th 2024, the US Federal Reserve [announced](#) their decision to cut its benchmark interest rate by 50 bps, to a range of 4.75%-5.00% from a range of 5.25%-5.50%. This followed the European Central Bank [rate cut](#) by 25 basis points to 3.5% from 3.75% earlier in the month. As such, we expect the MPC to follow through with this set precedence of loosening the monetary policy and cut the rate further,
- ii. The continued stability of the Shilling against major currencies, despite the August rate cut in the CBR gives room for a moderate cut without reversing the Shilling's gain. Since the last meeting, the Kenyan Shilling has appreciated by 0.7% against the US Dollar to Kshs 129.2 as at 29th September 2024, from Kshs 130.1 recorded on 6th August 2024 mainly attributable to improved foreign reserves which are currently at 4.1 months of import cover, above the statutory requirement of 4.0 months cover, and,
- iii. The need to support the economy by adopting a more accommodative policy that will ease financing activities. The Purchasing Managers Index (PMI) has come in above the 50.0 threshold for the first time in three months, with the August 2024 PMI coming in at 50.6, an indication the business environment is in the expansionary zone. A cut in the CBR rate will help spur economic growth, increase money supply and improve business activities in the country, and,

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