Kenya's Q1'2023 Balance of Payments Note

The Kenya National Bureau of Statistics recently released the Q1'2023 Quarterly Balance of Payment Report, highlighting that Kenya's balance of payments position recorded a 6.0% deterioration, with the deficit widening to Kshs 127.8 bn in Q1'2023, from a deficit of Kshs 120.6 bn recorded in Q1'2022 and a significant deterioration from the Kshs 29.1 bn deficit recorded in Q4'2022. In this note, we analyze the changes in the current account and the balance of payment before giving an outlook on both.

A. Current Account Balance

Kenya's current account deficit narrowed by 39.0% to Kshs 84.9 bn in Q1'2023 from Kshs 139.3 bn recorded in Q1'2022. The Q1'2023 deficit was also a significant decline of 30.7% from the deficit of Kshs 122.5 bn recorded in Q4'2022. The contraction during the quarter was driven by:

i. The contraction of the merchandise trade account deficit (the value of import goods exceeds the value of export goods, resulting in a negative net foreign investment) by 7.5% to Kshs 303.6 bn in Q1'2023, from Kshs 328.1 bn recorded in Q1'2022. On a q/q basis, the merchandise trade account deficit narrowed by 2.8% from a deficit of Kshs 312.5 bn recorded in Q4'2022, and,

ii. A 13.6% improvement in the services trade balance to a surplus of Kshs 56.0 bn from a surplus of Kshs 49.3 bn in Q1'2022. In addition, the services trade balance recorded a sharp q/q improvement of 174.6% from a surplus of Kshs 20.4 bn in Q4'2022, and

iii. A 19.2% improvement in the secondary income (transfer) balance to a surplus of Kshs 219.54 bn from a surplus of Kshs 184.1 bn in Q1'2022. Additionally, the secondary income balance recorded a marginal 1.9% q/q improvement from a surplus of Kshs 215.4 bn in Q4'2022.

The table below shows the breakdown of the various current account components on a year-on-year basis, comparing Q1'2022 and Q1'2023:

Cytonn Report: Current Account Balance					
Item	**Q4'2021**	**Q4'2022**	**Q1'2022**	**Q1'2023**	**Y/Y % Change**
Merchandise Trade Balance	(338.1)	(312.5)	(328.1)	(303.6)	(7.5%)
Services Trade Balance	67.3	20.4	49.3	56.0	13.6%
Primary Income Balance	(43.9)	(45.7)	(44.6)	(56.8)	27.3%
Secondary Income (transfer) Balance	184.7	215.4	184.1	219.54	19.2%
Current Account Balance	**(130.0)**	**(122.5)**	**(139.3)**	**(84.9)**	**(39.0%)**

All values in Kshs bns

Key take-outs from the table include;

i. Merchandise trade deficit (a scenario where imports are greater than exports of goods) narrowed by 7.5% to Kshs 303.6 bn in Q1'2023, from Kshs 328.1 bn in Q1'2022. This is attributable to the 12.0% growth in merchandise exports to Kshs 233.0 bn, from Kshs 208.1 bn in Q1'2022 which outpaced the 0.1% growth in merchandise imports to Kshs 536.6 bn from Kshs 536.2 bn recorded in a similar period in 2022. The increase in merchandise exports was mainly driven by a 9.4% increase in exportation of tea to Kshs 43.3 bn, from Kshs 39.5 bn recorded in Q1'2022. The increase in exports was also driven by the 103.4%, 41.4% and 30.6% growth in exports of edible products & preparations, iron & steel and titanium ores & concentrates, respectively. On the other hand, the slow growth in import bill is attributable to the 21.7% decline in importation of industrial machinery to Ksh. 51.3 from Kshs 65.5 reported in Q1'2022,

ii. Service Trade Balance (the difference between the imports and exports of services) recorded a 13.6% increase in Q1'2023 to a surplus of Kshs 56.0 bn, from a surplus of Kshs 49.3 bn in Q1'2022. The Q1'2023 surplus was a 174.6% improvement from a surplus of 20.4 bn recorded in Q4'2022 indicating an improved business environment globally. The improvement in service trade balance was mainly driven by the 54.3% growth in travel and transport services net receipts to Kshs 34.6 bn in Q1'2023, up from Kshs 22.5 bn recorded in Q1'2022,

iii. Primary income deficit (income that residents earn from, less that they pay to the rest of the world from working and from financial investments) widened by 27.3% to a deficit of Kshs 56.8 bn in

Q1'2023 from a deficit of Kshs 44.6 bn in Q1'2022, and widened further by 24.3% from a deficit of Kshs 45.7 bn recorded in Q4'2022,

iv. Secondary income/transfers surplus (the transactions recorded in the secondary income account pertain to those current transfers between residents and non-residents that directly affect the level of gross national disposable income and thus influence the economy's ability to consume goods and services) increased by 19.2% to Kshs 219.5 bn from Kshs 184.1 bn in Q1'2022. Additionally, it was a marginal increase of 1.9% from Kshs 215.4 bn recorded in Q4'2022,

v. Diaspora remittances recorded a 10.6% growth to Kshs 128.9 bn from Kshs 116.6 bn recorded in Q1'2022, and a marginal 1.2% increase from the Kshs 127.4 bn recorded in Q4'2022,

vi. Total exports grew by 11.9% in Q1'2023 to Kshs 232.6 bn, up from Kshs 207.8 bn recorded in Q1'2022. In terms of exports by region, Africa was the largest merchandise export recipient, accounting for 43.1% of total exports in Q1'2023 and registering a 21.9% increase in export earnings to Kshs 100.2 bn, from Kshs 82.2 bn in Q1'2022. The increase was mainly attributable to 50.3% increase in exports to Uganda, coupled with 44.5%, 42.2%, 40.2%, and 23.3% growth in exports to Somalia, Democratic Republic of Congo, Ethiopia, and Rwanda, respectively. Asia followed in second place, accounting for 25.0% of all exports and recording a growth of 9.8% in Q1'2023 to Kshs 58.2 bn, up from Kshs 53.0 in Q1'2022, and,

vii. Overall imports declined marginally by 0.5% in Q1'2023 to Kshs 589.8 bn from 592.7 bn recorded in Q1'2022. In terms of imports by region, Asia remained the largest merchandise import source, accounting for 66.8% of total imports, with the value of imports declining by 2.0% to Kshs 393.8 bn, down from Kshs 402.0 bn recorded in Q1'2022. The decline was mainly attributed to a 19.1% decrease in imports from China to Kshs 90.8 bn, from Kshs 112.3 bn recorded in Q1'2022, mainly driven by decreased imports of photosensitive semiconductor devices from the country. However, imports from the United Arabs Emirates(UAE) increased by 14.5% to Kshs 82.6 bn, up from Kshs 72.2 bn reported in Q1'2022 driven by gas oil and gasoline imports. The European Union accounted for 17.1% of total imports in Q1'2023, valued at Kshs 100.7 bn, a 29.2% growth from the Kshs 77.9 bn recorded in Q1'2022 mainly driven by the 72.3%, 48.7%, and 27.5% increases in imports from France, Netherlands, and Germany, respectively. In addition, the value of imports from Australia rose sharply by 266.7% to Kshs 3.1 bn in Q1'2023, up from Kshs 0.8 bn in Q1'2022, largely driven by increased importation of wheat and meslin.

B. Balance of Payment

Kenya's balance of payment position worsened by 6.0% in Q1'2023, coming in at a deficit of Kshs 127.8 bn, from a deficit of Kshs 120.6 bn in Q1'2022, and a 339.5% deterioration from the Kshs 29.1 bn deficit recorded in Q4'2022. The narrowing of the current account balance by 39.0% in Q1'2023 to a deficit of Kshs 84.9 from a deficit of Kshs 139.3 in Q1'2022 was not sufficient to offset the reversal of the financial account balance from a surplus of Kshs 82.9 bn in Q1'2022 to a deficit of Kshs 111.1 bn in Q1'2023, hence resulting in the overall deterioration of the balance of payment. The table below shows the breakdown of the various balance of payments components, comparing Q1'2023 and Q1'2022:

Cytonn Report: Quarterly Balance of Payment					
Item	**Q4'2021**	**Q4'2022**	**Q1'2022**	**Q1'2023**	**Y/Y % Change**
Current Account Balance	(130.0)	(122.5)	(139.3)	(84.9)	(39.0%)
Capital Account Balance	2.2	3.7	7.4	6.9	(5.9%)
Financial Account Balance	83.5	37.0	82.9	(111.1)	(234.0%)
Net Errors and Omissions	9.3	52.7	(71.6)	61.2	(185.5%)
Balance of Payments	**(35.0)**	**(29.1)**	**(120.6)**	**(127.8)**	**6.0%**

All values in Kshs bns

Key take-outs from the table include;

i. The current account deficit (value of goods and services imported exceeds the value of those exported) narrowed by a significant margin of 39.0% to Kshs 84.9 bn from Kshs 139.3 bn in Q1'2022, and by 30.7% from Kshs 122.5 bn recorded in Q4'2022. The narrowing of the current account was brought about by the

7.5% improvement in Merchandise trade deficit to Kshs 303.6 bn in Q1'2023, from Kshs 328.1 bn in Q1'2022 driven by the 12.0% growth in merchandise exports to Kshs 233.0 bn, from Kshs 208.1 bn in Q1'2022 which outpaced the 0.1% growth in merchandise imports to Kshs 536.6 bn, from Kshs 536.2 bn recorded in a similar period in 2022,

ii. The capital account balance (shows capital transfers receivable and payable between residents and non-residents, including the acquisition and disposal of non-produced non-financial items), which includes foreign direct investments (FDIs), decreased by 5.9% to a surplus of Kshs 6.9 bn in Q1'2023 down from a surplus of Kshs 7.4 bn in Q1'2022. However, relative to the Q4'2022 surplus of Kshs 3.7 bn, the capital account balance in Q1'2023 expanded by 88.5%,

iii. The financial account balance deficit (the difference between the foreign assets purchased by domestic buyers and the domestic assets purchased by foreign buyers) recorded a deficit of Kshs 111.1 bn in Q1'2023, a reversal from the surplus of Kshs 82.9 bn recorded in Q1'2022. In addition, the stock of gross official reserves declined by 5.0% to Kshs 921.3 bn in Q1'2023, down from Kshs 969.3 in Q1'2022 as a result of an increase in debt servicing costs and repayments, and,

iv. Consequently, the Balance of Payments (BoP) position deteriorated by 6.0% to a deficit of Kshs 127.8 bn in Q1'2023, from a deficit of Kshs 120.6 bn recorded in Q1'2022.

C. Public External Debt

During the period under review, the stock of external public and public guarantee debt increased by 15.5% to Kshs 4.7 tn in Q1'2023, up from Kshs 4.1 tn recorded in Q1'2022, mainly driven by a 23.5% increase in multilateral debt to Kshs 2.2 tn in Q1'2023, up from Kshs 1.8 tn recorded in Q1'2022. Notably, domestically issued debt held by non-residents increased by 14.6% to Kshs 1.0 tn in Q1'2023, up from Kshs 0.8 tn in Q1'2022. The table below shows the breakdown of the outstanding external public and publicly guaranteed debt, comparing Q1'2023 and Q1'2022:

Cytonn Report: Q1'2023 Public External Debt					
Debt Source	**Q4'2021**	**Q4'2022**	**Q1'2022**	**Q1'2023**	**Y/Y % Change**
Bilateral	1.1	1.1	1.1	1.2	9.2%
Multilateral	1.8	2.2	1.8	2.2	23.5%
Commercial Banks	0.3	0.3	0.3	0.3	(6.7%)
Suppliers Credit	0.01	0.01	0.01	0.01	13.5%
Debt Securities held by non-residents	0.8	0.9	0.8	1.0	14.6%
Total External Public Debt	**4.0**	**4.6**	**4.1**	**4.7**	**15.5%**

All values in Kshs tn

Key take-outs from the table include;

i. Multilateral debt increased by 23.5% to Kshs 2.2 tn in Q1'2023, up from Kshs 1.8 tn recorded in Q1'2022, accounting for 60.0% of the total external debt. On a quarterly basis, multilateral debt registered a marginal 1.4% growth from Kshs 2.2 bn recorded in Q4'2022, brought about by increased disbursement of programme loans from the International Monetary Fund (IMF) during the period of review.

D. Conclusion

The deterioration in the balance of payments performance is mainly due to the reversal of the financial account balance from a surplus to a deficit driven by debt servicing costs that have been on the rise given the continued depreciation of the Kenya shilling against the US dollar, given that 67.3% of Kenya's external debt as of March 2023 is denominated in USD. Consequently, the sustained depreciation of the shilling against hard currency continues to inflate the country's import bill. As such, we expect the high costs of imports to continue weighing down on the current account's performance in the medium term. However, we expect that the current administration's focus on fiscal consolidation will improve the balance of payments performance by minimizing the costs of servicing external debts through the adjustment of the public debt mix in the FY/2023/24 budget to comprise 18.3% foreign debt and 81.7% domestic debt, from 48.0% foreign financing and 52.0% domestic financing in FY'2022/23. Additionally, the introduction of the fertilizer subsidy program is set to reduce the costs of farm inputs, boost agricultural production in the country, increase exports of agricultural products, and support the current account. We also expect that multilateral trade partnership deals such as the Kenya-EU Trade Deal and the Tripartite Agreement between the EAC, SADC and COMESA will help stabilize the balance of payments by increasing the volume of exports demanded and providing export markets for the same.