KPMG

Kenya Economic Snapshot H2, 2017

Trade & Investment SWOT

Strengths	Weaknesses
Strong tax regulatory environment; high literacy rate benefits the labour force; growing mobile banking sector will improve access to banking services in rural areas.	High cost of energy makes locally produced goods less competitive against imported products.
Nairobi is a financial hub in the region and businesses in Kenya benefit from good access to local and international credit.	Burdensome bureaucratic procedures make setting up a business an arduous and costly process - Kenya is ranked in the bottom 40% of countries worldwide for the ease of starting a business.
Kenya's strong trade platform and strategic location make it an attractive trade hub.	Corruption represents a major operational risk in the country, increasing business costs and the risk of reputational damage.
Improving road, rail, air and shipping liner connections to neighbouring countries facilitate regional and international trade.	Weak judicial system - the country is ranked 100th out of 113 countries in the World Justice Project (WJP) Rule of Law Index 2016.
Opportunities	**Threats**
Further efforts to enhance the independence of the judiciary will improve court proceedings.	The capacity of anti-counterfeit forces requires improvement in order to better protect intellectual property.
Reforms to the legal framework regulating foreign direct investment (FDI) mean the business environment in Kenya has become more transparent and favourable to foreign investors.	More needs to be done regarding corruption and transparency in order to create a more open and competitive business environment.
Growing demand for consumer imports will impact on local manufacturers.	Borders regions near Somalia and South Sudan carry risks to business operations/logistics due to the prevalence of conflict.
Planned investments in infrastructure, including new highways, railways, ports and airport terminals, will enhance logistics options, and improve Kenya's ability to capture regional transit trade.	The threat of terrorism lingers and continues to have a negative impact on the tourism industry, albeit much less since 2015.

Source: Business Monitor International (BMI), KPMG research

Economic structure - The primary sector is dependent on 20% of the country's land area which is arable, with almost half of this under cultivation at present. Farming activity includes both livestock and crop farming, with the latter including export-focused production of coffee, tea, flowers and vegetables. Small-scale farming is focussed on food crops like maize, potatoes and beans. The secondary sector includes a maturing manufacturing compared to other African countries. Factories produce a diverse range of goods though its output – used both locally and exported – is dominated by food processing and consumer goods manufacturing. The tertiary sector is sizeable in an African context and includes a vibrant tourism industry, developing banking system, and growing retail market. Rising household income is supporting domestic tourism and retail formalisation.

Recent economic developments – Kenya's foreign direct investment (FDI) inflows have been on a declining trend over the past five years, and were in 2016 less than half of what was expected by the Kenya Investment Authority (KenInvest). One of the reasons for the lower-than-expected FDI inflows is the economic strains in the UK due to Brexit. Nonetheless, S&P Global Ratings affirmed Kenya's "B+" sovereign rating during September 2017, commenting that the Supreme Court ruling to nullify the August presidential election results pointed to "signs of improving judicial independence and checks and balances among the arms of government". The fiscal deficit will narrow only slightly as percentage of gross domestic product (GDP) in 2017 due to increased expenditure associated with elections in August and a re-run during October. Some analysts believe that more than $600 million will be spent on elections during the year. Consumer price inflation increased from 6.9% y-o-y in January 2017 to almost 12% y-o-y by the middle of the year. Inflation generally increases in the run-up to elections in Kenya. This is often attributed to a wait-and-see approach taken by farmers and businesses given political uncertainty.

Mega trends

Population	2017	Total: 48.47 million; female: 24.25 million; male: 24.22 million; age 0-14: 41.38% of total; age 15+: 58.62% of total; age 65+: 2.92% of total
Population growth rate	2015	2.56%
Life expectancy at birth	2015	Total: 66.65 years; female: 69.12 years; male: 64.29 years
HIV/AIDS	2016	Total number of people living with HIV: 1.6 million; total adult prevalence: 5.4%; HIV AIDS orphans (age 0-17): 0.66 million
Adult literacy rate	2015	Total population: 78.02%; female: 74.97%; male: 81.11%
Urbanisation	2016	Urban population: 26.06% of total; annual urban population growth: 4.24%; rural population: 73.95% of total
Population below $1.90/day poverty line	2005	33.6%
Unemployment rate	2017	Total: 10.8%; female: 13%; male: 9%; youth (15 - 24): 21.8%
Employment	2017	Agriculture: 61.9% of total; industry: 8.6% of total; services: 29.5% of total
Labour participation rate	2017	Total (ages 15+): 67.34% of total population
Business languages	n/a	English (official), Kiswahili (official)
Telephone & internet users	2013; 2016	Fixed telephone subscriptions: 0.07 million (2016); wired internet subscriptions: 0.09 million (2013); cell phone subscriptions: 38.98 million (2016)
Quality of infrastructure (1 = underdeveloped, 7 = developed)	2017	4.3

Sources: UNESCO Institute for Statistics, World Telecommunication/ICT indicator database, World Bank, UNAIDS, International Labour Organisation, Analyse Africa

Business Environment									
Human Development Index (HDI) 2015		Index of Economic Freedom 2017		Global Competitiveness Index (GCI) 2017-18		Doing Business 2018		Corruption Perceptions Index 2016	
146th	out of 188 countries	135th	out of 180 countries	91st	out of 137 countries	80th	out of 190 countries	145th	out of 176 countries

Source: World Bank, The Heritage Foundation, World Economic Forum (WEF), Transparency International

Economic policy – Vision 2030 is the national long-term development policy that aims to transform Kenya into a newly industrialising, middle-income country by 2030. The economic pillar of the scheme aims to achieve an average economic growth rate of 10% per annum, and is focussed on infrastructure, tourism, agriculture, trade, manufacturing, information technology and financial inclusion. The social pillar of Vision 2030 seeks to build a just and cohesive society with social equity. The political pillar aims to realise a democratic political system founded on issue-based politics that respects the rule of law and protects the rights and freedoms of every individual in Kenyan society. The implementation of the Vision 2030 is a progressive process with goals and milestones that will be achieved over time. It is implemented in successive five-year cycles called Medium Term Plans (MTPs). The first MTP was implemented during 2008-2012 and the second MTP is being implemented in 2013-2017.

Sovereign Risk Ratings		
S&P Global Ratings	Fitch Ratings	Moody's Investors Service
B+/Stable	B+/Negative	B1/Under Review

Source: Trading Economics

S&P Global Ratings affirmed their "B+" long-term foreign sovereign credit rating on Kenya in September 2017. The outlook was also kept at stable. The agency commented that, while the Supreme Court's ruling to nullify the presidential election results – unprecedented in Africa - extended political uncertainty over the short-term, it also pointed to "signs of improving judicial independence and checks and balances among the arms of government". S&P expected that the time that strong growth in the short-term would facilitate fiscal consolidation and contain increases in external debt despite a backdrop of uncertainty surrounding the presidential election re-run. Credit positive factors outside the current realm of political uncertainty include monetary policy flexibility, a history of strong economic growth, liquid domestic capital markets and an increasingly diversified economic base. S&P also believes that the new government that emerges following the election re-run will continue with economic policies that foster sustainable public finances.

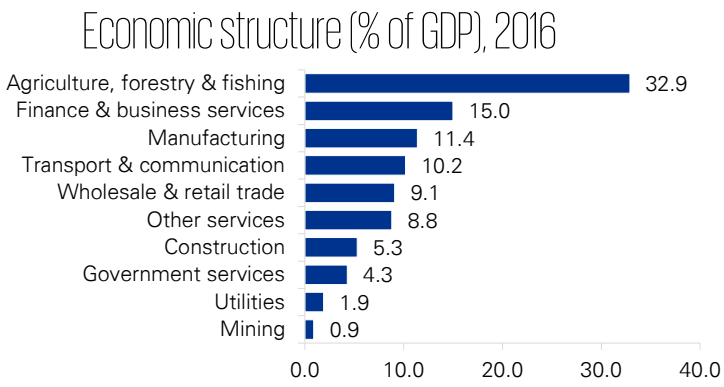
Fitch Ratings affirmed Kenya's long-term foreign currency IDRs at "B+" with a negative outlook in July 2017. The assessment included the view that the country will see only limited disruptions after the August 8th elections and that fiscal consolidation will be visible in 2018. Jan Friederich, a Fitch analyst for the Middle East and Africa, said in a statement during September that the outlook could return to stable if the election re-run "goes relatively smoothly" and if the government can achieve a decline in its debt/GDP ratios via fiscal consolidation. Public debt reached an equivalent 56% of GDP in the 2016/17 fiscal year which was comparable to other "B" rated sovereigns. However, "debt servicing costs consume an outsized portion of Kenya's revenue". According to Fitch, total debt and interest payments equal 262% and 16.5%, respectively, of fiscal revenue, compared to the "B" medians of 227% and 9.6%.

Moody's Investors Services placed Kenya's "B1" rating on review for a downgrade in October 2017. The downgrade review was prompted by persistent and large fiscal deficits, high borrowing costs driving government indebtedness higher, government liquidity pressures from payment obligations, and uncertainties over the direction of economic and fiscal policy due to political dynamics after the August 8th elections. Moody's review will focus on reassessing medium-term fiscal trends and the likely policy response to ongoing budgetary pressures and the effectiveness of the medium-term fiscal financing plan in managing liquidity risks. The agency warned that it would downgrade the rating "if the review were to conclude that Kenya's government debt and financing needs, and hence its fiscal strength and liquidity position, have eroded to levels no longer consistent with "B1" rated peers."

Finance & Banking				
Central bank	Number of commercial banks	Bank branches per 100 000 adults	ATMs per 100 000 adults	Deposit accounts per 1 000 adults
Central Bank of Kenya (CBK)	43	5.85	9.27	1315.63
Stock market	**Listed companies**	**Market capitalisation***	**Largest sectors**	**Weekly trading value***
Nairobi Securities Exchange (NSE)	64	$21.3 billion	Banking, food, beverages	$9 million
Capital market	**Level of development**	**Maturity range**	**Municipal bonds**	**Corporate bonds**
Yes	Advanced in an African context	91 days to 30 years	No	Yes

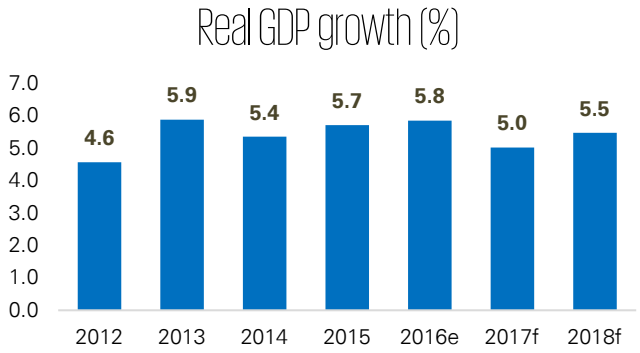
Sources: World Bank, African Alliance, Analyse Africa, KPMG research
**Week ending 27 October 2017*

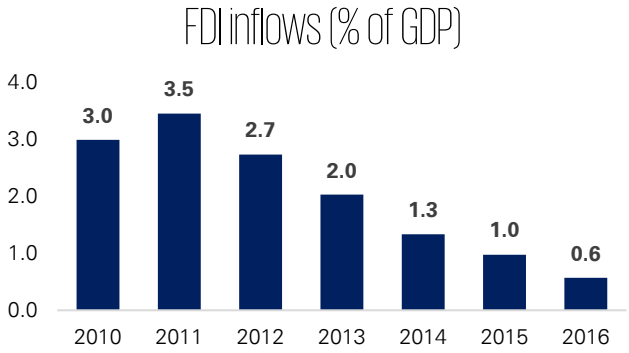
Macroeconomic overview



Source: African Economic Outlook (AEO)

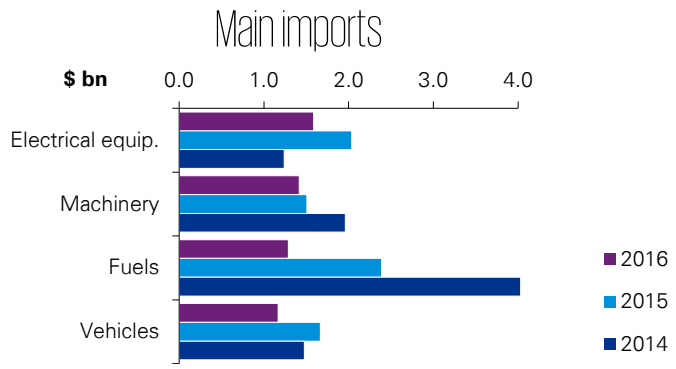
Economic growth - The services sector has been a major driver of growth for Kenya, and will continue to do so during 2018. The International Monetary Fund (IMF) believes that the Kenyan economy will grow by 5% in 2017 and 5.5% in 2018. These growth forecasts are slightly lower than the growth seen in 2016 due to some political tension in the country. The working-age population in the country is growing, which contributes to the positive growth outlook over the long-term. (The country's diverse economy and the thriving services sector is expected to be able to accommodate this workforce.) Despite a recent decrease in foreign investment inflows (as percentage of GDP), Kenya has robust long-term growth prospects due to increasing productivity, a rapidly growing technology sector and favourable demographics.

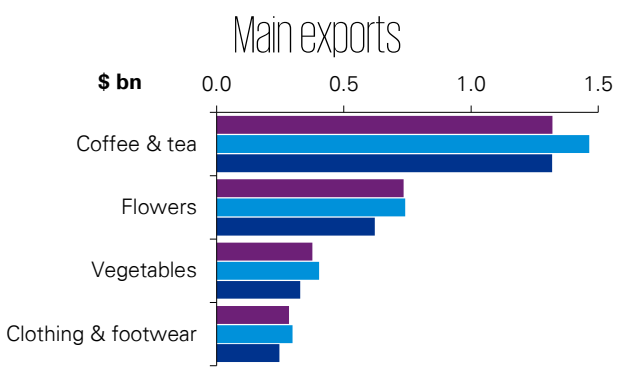




Sources: IMF, United Nations Conference on Trade and Development (UNCTAD)

Foreign investment – Kenya's FDI inflows have been on a declining trend over the past five years, and were in 2016 less than half of what was expected by the Kenya Investment Authority (KenInvest). One of the reasons for the lower-than-expected FDI inflows is the economic strains in the UK due to Brexit. The US, UK and India are the top FDI sources for the country, and manufacturing, construction, energy and ICT are the most attractive sectors. There are numerous new initiatives aimed at driving FDI growth in these areas, including the establishment of special economic zones (SEZs). The new Dongo Kundu SEZ in Mombasa expected to be operational by early 2018, and government incentives including corporate tax cuts and tax allowances.

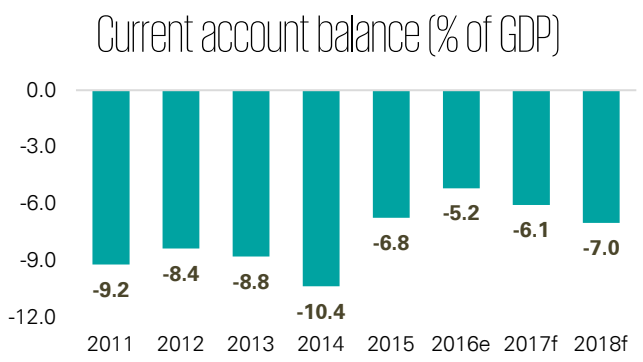


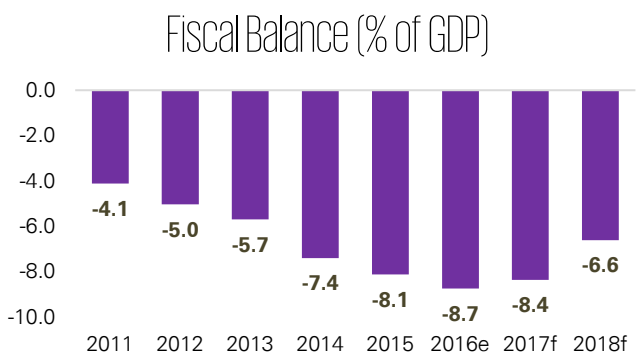


Main Imports: % share of total	2014	2015	2016	Main Exports: % share of total	2014	2015	2016
Electrical equip.	6.7%	10.4%	10.4%	Coffee & tea	21.6%	25.9%	27.5%
Machinery	10.7%	7.7%	9.2%	Flowers	10.2%	13.1%	15.3%
Fuels	22.1%	12.3%	8.4%	Vegetables	5.4%	7.1%	7.8%
Vehicles	8.0%	8.5%	7.6%	Clothing & footwear	4.0%	5.3%	5.9%

Source: Trade Map

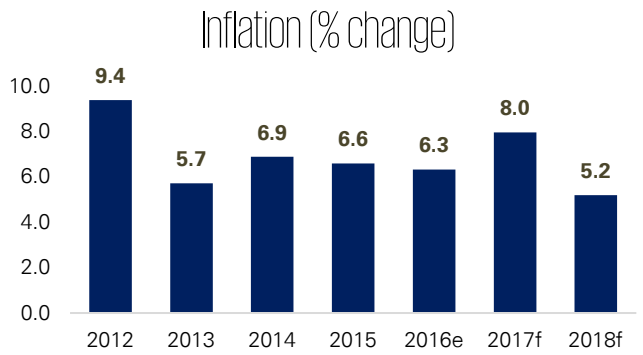
External trade – Kenya has a structural current account deficit which is mainly financed by foreign debt. Investment into the country's infrastructure network has kept it reliant on foreign debt for financing, effectively keeping the current account in a deficit despite substantial exports from the diversified economy. The export capacity in the country is expected to improve over time with the development of the infrastructure network – helping to narrow, albeit not eliminate, the deficit in the future. A high reliance on imported petroleum products, food and capital goods will ensure that Kenya's current account will remain in deficit over the medium term, with the IMF predicting a current account deficit equal to 7% of GDP in 2018. Over the long-term, the deficit is however expected to narrow with the conclusion of the infrastructure projects, allowing exports to outweigh the capital investment requirements. Import cover - the number of months of imports covered by a country's foreign reserves - is projected by BMI to equal 3.5 months in 2018, compared to a global benchmark of at least three months.

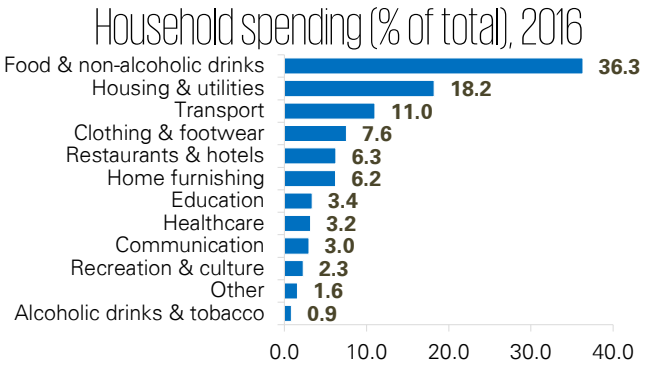




Source: IMF

Fiscal policy – Fiscal deficit in Kenya can pose risks for the country, especially in terms of declining investor sentiment. According to the IMF, the government is attempting to reduce the fiscal deficit by limiting the growth of recurring expenditures and through its success in increasing revenue collections. However, the fiscal deficit will narrow only slightly in 2017 due to increased expenditure associated with elections in August and a re-run during October. (Some analysts believe that more than $600 million will be spent on elections during the year, while donor aid could be negatively affected by the political uncertainty surrounding the elongated electoral process.) Kenya does not currently have a strict fiscal rule in Kenya, though the government does want to bring the deficit down towards a target of 3% of GDP. It is therefore expected that the deficit will narrow over the next few years, with the IMF predicting it to be equal to 6.6% of GDP in 2018, compared to the recent peak deficit in 2016 of 8.7% of GDP. Reaching the deficit target of 3% of GDP will require significant reductions on recurring expenditure and improved revenue collections.





Source: IMF, BMI, country statistics agencies

Monetary policy - Consumer price inflation increased from 6.9% in January 2017 to almost 12% y-o-y by the middle of the year. Inflation generally increases in the run-up to elections in Kenya. This is often attributed to a wait-and-see approach taken by farmers and businesses given political uncertainty. Headline inflation declined during the third quarter of the year, and most recently declined from 7% y-o-y in September 2017 to 5.7% y-o-y in October, and it is expected that price growth will moderate further towards the start of 2018 as the imminent grain harvest will boost food supplies. The IMF believes that the average inflation rate for 2017 will be 8%, which is slightly outside the CBK's target band of 5% y-o-y +/- 2.5%. Nonetheless, the CBK kept its benchmark interest rate unchanged at 10% for the 13th consecutive policy meeting in September 2017. Next year will potentially see lower inflation as weather conditions are expected to normalise.

Contact details

KPMG Kenya	KPMG South Africa Economics
Josphat Mwaura, Senior Partner & CEO +254 20 280 6100 jmwaura@kpmg.co.ke	**Lullu Krugel, Director** +27 (0) 82 712 4049 lullu.krugel@kpmg.co.za

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