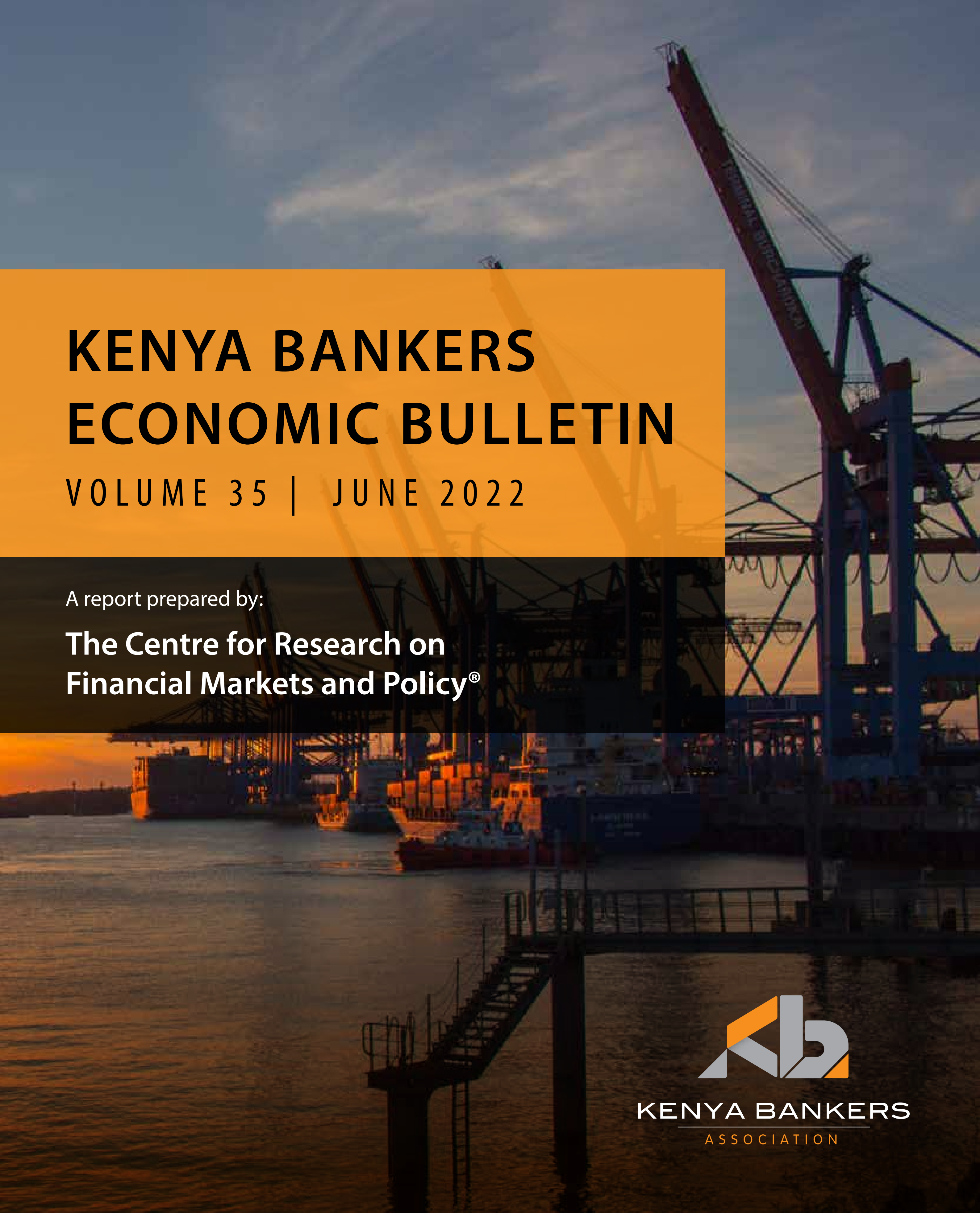

KENYA BANKERS ECONOMIC BULLETIN

VOLUME 35 | JUNE 2022

A report prepared by:

The Centre for Research on Financial Markets and Policy®

KENYA BANKERS
ASSOCIATION

CENTRE FOR RESEARCH ON
FINANCIAL MARKETS AND POLICY®

About this Report

This *Bulletin* reviews Kenya's economic performance in the first quarter of 2022, drawing on the recent performance and developments to provide perspectives on the year's outlook. The *Bulletin* covers trends in selected activities in the real economy, government fiscal operations, public debt, inflation and interest rates, the balance of payments and exchange rate, activity at the Nairobi Securities Exchange and banking sector performance..

About the Centre for Research on Financial Markets and Policy®

The Centre for Research on Financial Markets and Policy® was established by the Kenya Bankers Association in 2012 to offer an array of research, commentary, and dialogue regarding critical policy matters that impact on financial markets in Kenya. The Centre sponsors original research, provides thoughtful commentary, and hosts dialogues and conferences involving scholars and practitioners on key financial market issues. Through these activities, the Centre acts as a platform for intellectual engagement and dialogue between financial market experts, the banking sector and the policy makers in Kenya. It therefore contributes to an informed discussion that influences critical financial market debates and policies.

CENTRE FOR RESEARCH ON
FINANCIAL MARKETS AND POLICY®

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Distributed by	Kenya Bankers Association

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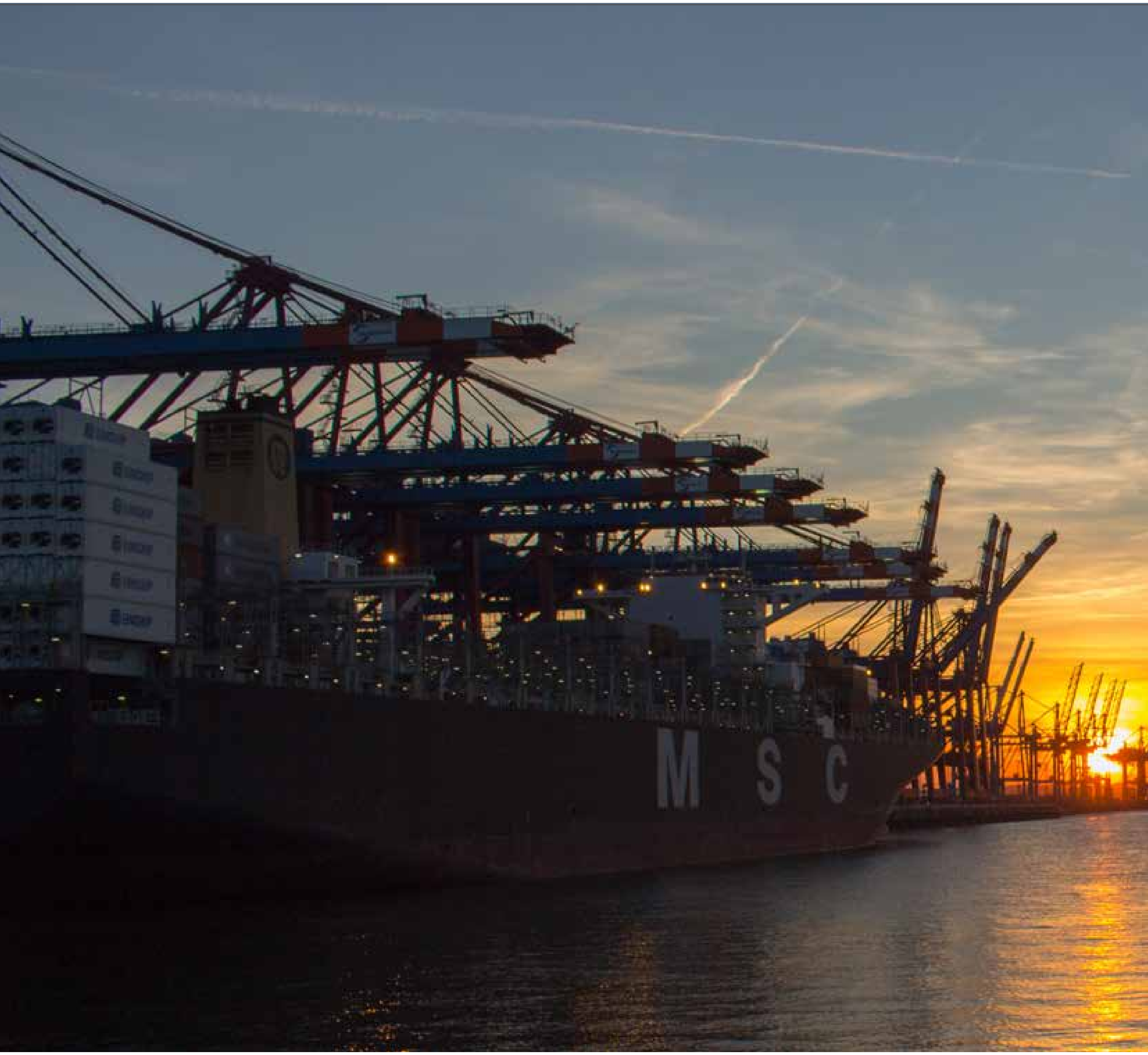
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FOREWORD

From the CEO's Desk

It is my pleasure to present to you the 35th issue of the *Kenya Bankers Economic Bulletin* focusing on the first quarter of 2022. The beginning of year 2022 marked a stronger recovery from the effects of the pandemic that presented widespread disruption of economic activities not only in the country but across the globe in 2020 and 2021. In this issue, we discuss the state of the Kenyan economy during the first quarter of 2022, highlighting the patterns of economic recoveries across sectors and economic activities.

As noted in the *Bulletin*, the economy posted robust growth of 6.8 percent was registered in the domestic economy during the period on account of sustained recovery in manufacturing, construction, transport and storage, education, accommodation and food services, financial and insurance services, and wholesale and retail trade sectors, that more-than-offset the contraction in agriculture.

Leading economic indicators depicted a strong recovery in the economy, though with sustained fragilities. Concerns during the quarter were on rising inflationary pressure driven by oil which has strong pass-through effects to other consumer goods prices, muted credit growth, and weakening currency.

It is my hope that you will find this issue of the *Kenya Bankers Economic Bulletin* insightful and useful. While we seek to discuss specific topical issues in the economy with relevance to banking, we are open to receive and consider for publications incisive commentaries on any related topics of interest to the banking sector. For guidelines on such submissions, please get in touch with the *Bulletin's* Editor at ***research@kba.co.ke***.

We welcome feedback on the content of this Bulletin as we continually seek to improve its relevance to you.

Dr. Habil Olaka, EBS
Chief Executive Officer, Kenya Bankers Association

COMMENTARY

Fragile Economic Recovery: Inflation and Credit Risks

By Samuel Tiriongo, PhD

The economy in early 2022 was reeling from the effects that the pandemic and its containment measures that depressed activities across most sectors in 2020 and most of 2021. Policymakers across the globe were keen to structure policies to spring back economies. While the policies were largely customized to country contexts, concerns remained on the persistent unequal levels of access to vaccinations against the COVID-19 infections that continued to hinder a faster reopening of global trade and supply chains, and the emergence of new energy-driven inflationary pressures arising from the onset of war in Ukraine.

At the beginning of 2022, four critical developments continued to shape the policy debates. First, the economy posted strong economic recovery, growing by 6.8 percent during the first quarter of 2022 - compared with 2.7 percent growth over a similar quarter in 2021 - driven by a strong resumption of activity in the services and industrial sectors attributed to the reopening of the economy. Concerns, however, remained on the depressed activity in agriculture sector due to unfavourable weather conditions across the country. In addition, uncertainty continued to linger during the quarter on whether the recovery would be sustained, given the lack of a clear foresight on the containment of the pandemic at a global scale, and the emerging seasonal investor jitters associated with upcoming general elections in August 2022.

“ The economy posted strong economic recovery, growing by 6.8 percent during the first quarter of 2022 - compared with 2.7 percent growth over a similar quarter in 2021

Second, despite inflation remaining within the target range during the quarter, concerns were rising expectations of higher inflation in the subsequent periods in the wake of rising global oil prices arising from the disruptions caused by the war in Ukraine. Given the strength of the pass-through effects of inflation on other commodity prices, policymakers would need to be alert to the trend of global oil prices and thus shift policy levers to address it before it slows down the impressive economic recovery.

Nairobi city skyline at dusk

Third, the short-term interest rates had eased reflecting ample liquidity conditions in the market. However, commercial banks' lending rates remained sticky mirroring the challenges with effective pricing of risk by banks, which was associated with delays in the approvals - and thus implementation, of risk-based pricing models. This, coupled with the suspension of listing of negative credit information that was constraining customer credit assessment by banks, continued to impede a stronger growth in credit in the economy and limit the financing of a strong economic recovery process.

Fourth, was the widening of the current account deficit that, in part, continued to exert pressure on the exchange rate to weaken; a trend sustained during the quarter from July 2021. This may pose risks on the overall price stability I particular and the pace of economic recovery by driving down demand for imports some of which are capital goods targeted at supporting economic recovery.

Amidst these developments, and policy concerns, the banking sector remained stable and resilient over the period; depicting strong liquidity and capital positions well above regulatory minimum limits. However, credit risk rose driven by a faster growth in gross non-performing loans than the growth in gross loans extended by the industry. This going forward, may trigger a tightening of lending conditions with the implication of driving a slower growth in credit which may have ramifications on the magnitude and pace of economic recovery.

Dr. Samuel Tiriongo is the Director, KBA Centre for Research on Financial Markets and Policy

Significant improvements in the number of tourists' arrivals continue to be registered, signifying a recovery of a sector that had been depressed by to the impact of the pandemic containment measures.

State of the Economy

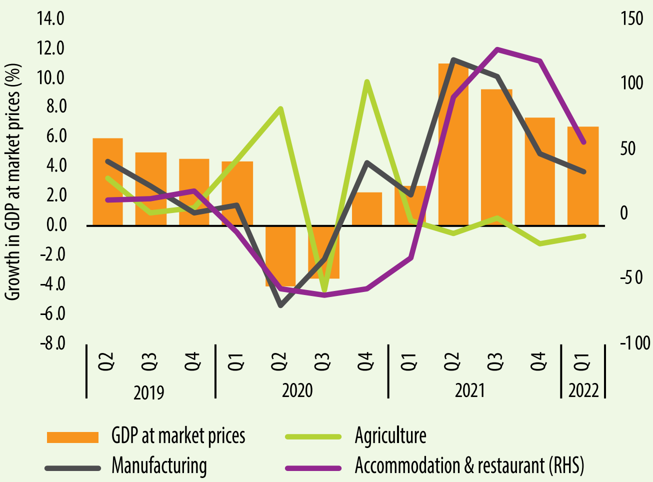
The global economic growth projection in April 2022 was revised downward to 3.6 percent for both 2022 and 2023, down from 4.4 percent and 3.8 percent respectively, in January. The downward revision highlights the continued slowdown in global economic recovery caused by the commodity prices' spike induced by the Russia-Ukraine war that has triggered severe disruptions to commodities' supply and aggravated inflation pressures in Advanced Economies as well as Emerging and developing Markets.

In addition, production challenges in Malaysia and export bans in Indonesia; the world's leading producers of palm oil, and drought in Latin America have strained global food supplies. The spill-overs effects from the global developments have also adversely affected growth in Sub-Saharan Africa (SSA), that is expected to slow down to 3.8 percent in 2022 but slightly recover to 4.0 percent in 2023, compared to 4.5 percent in 2021.

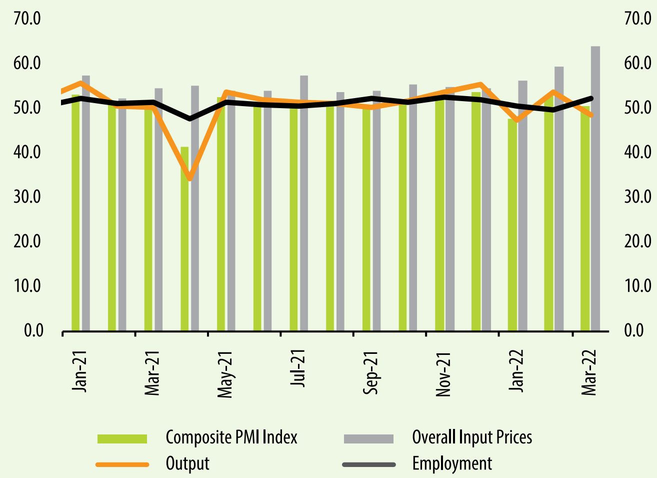
Robust growth of 6.8 percent was registered in the domestic economy during the first quarter of 2022 relative to 2.7 percent growth in the first quarter of 2021 (**Figure 1A**), on account of sustained recovery in manufacturing, construction, transport and storage, education, accommodation and food services, financial and insurance services, and wholesale and retail trade sectors. In contrast, the agriculture sector, which is one of the largest sectors of the Kenyan economy, contracted by 0.7 percent, on account of unfavourable weather conditions that persisted during the quarter. Moreover, the Purchasing Managers Index (PMI) showed strong recovery in economic activities during the period. In fact, the PMI composite index closed the quarter at 50.6 percent; suggesting an expansion of private-sector economic activity after losing momentum earlier on the quarter where it stood at 47.6 in January 2022. Even so, the evolution of the sub-indices registered mixed patterns (**Figure 1B**).

Figure 2:
GDP Performance and Economic Outlook

1(A) Domestic Economic performance



1(B) Trends in PMI



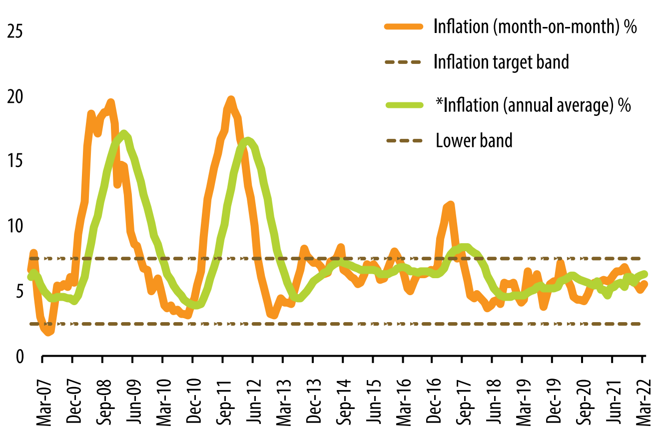
Source: KNBS and IHS Markit®

Inflation expectations were heightened during the quarter, mainly on the back of rising global commodity prices (mainly oil) triggered by the war in Ukraine and the materialisation of sanctions imposed on Russia. Consequently, the month-on-month headline inflation rose from 5.39 percent in January to close the quarter in March at 5.56 percent, as the annual average inflation rate rose to 6.29 percent in March up from 6.08 percent in January 2022 (**Figure 2A**). The Murban oil prices responded to the global supply disruptions by rising drastically, from USD 85 per barrel in January 2022 to USD 113 per barrel by March 2022 (**Figure 2B**).

The pass-through effects of the rising international prices filtered into domestic inflation through increased domestic fuel prices following upward revisions of the domestic pump prices by the Energy and Petroleum Regulatory Authority.

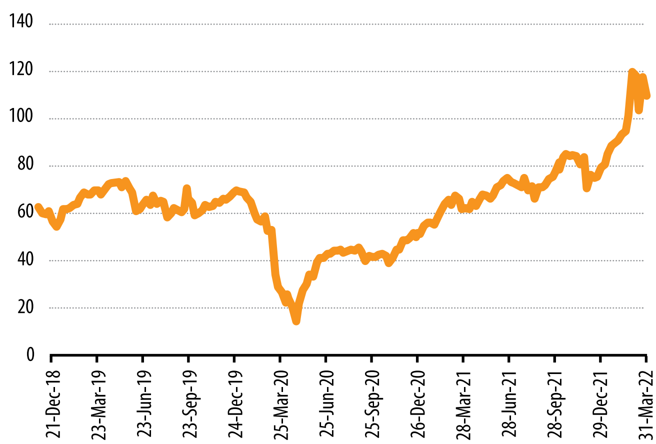
Figure 2: Trends in Inflation and Murban Crude oil prices

2(A) Inflation trends



Source: Central bank of Kenya

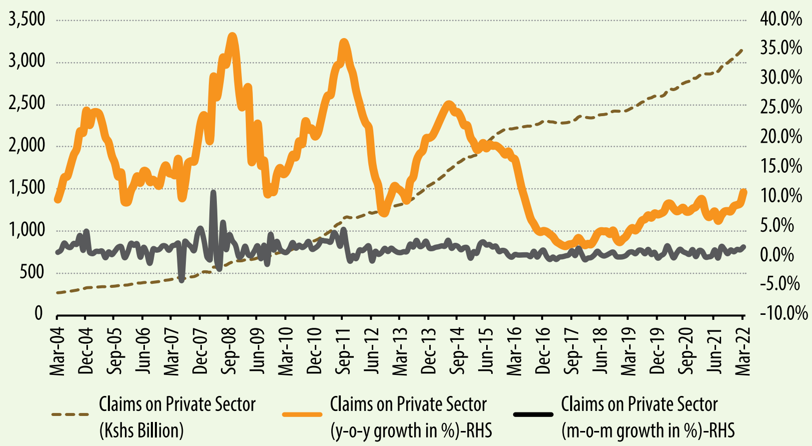
2(B) Trends in Murban oil price



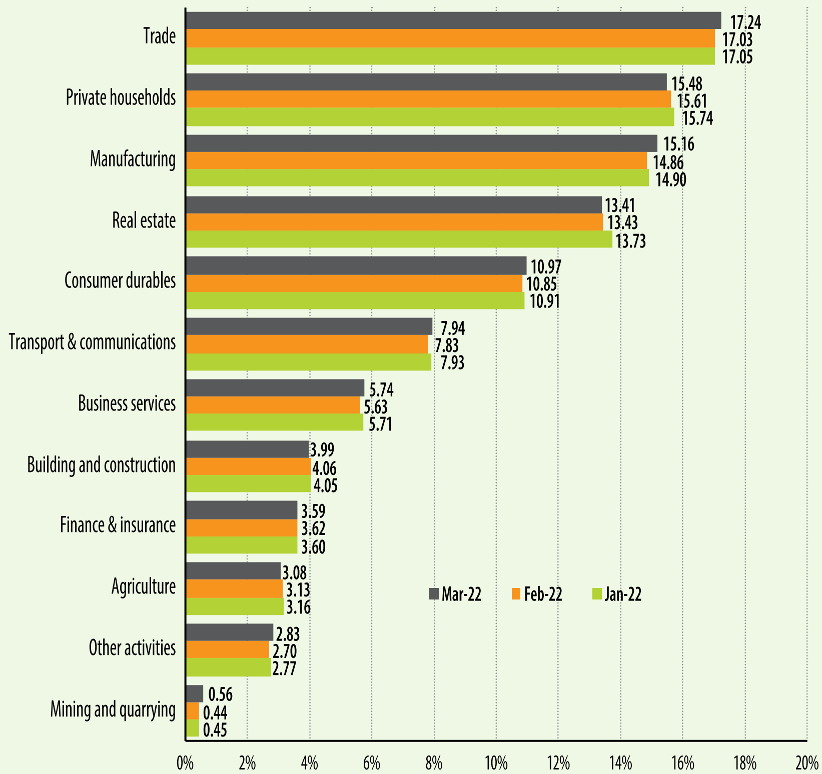
Source: Oil price.com

Figure 3:
Private Sector Credit and Growth Dynamics

3(A) Private Sector Credit and Growth Dynamics



3(B) Sectoral private sector credit growth, Quarter 1 2022



Source: Central Bank of Kenya

> **Inflation expectations were heightened during the quarter, mainly on the back of rising global commodity prices (mainly oil) triggered by the war in Ukraine and the materialisation of sanctions imposed on Russia.**

Credit growth remained largely muted, with a single-digit growth recorded in the first two months of the quarter, on account of banks inability to effectively price the borrowers' risk. However, there was increasing adoption of risk-based pricing by banks. As at mid-March 2022, approximately 27 percent of the banking industry loan portfolio had transitioned to risk-based pricing environment.

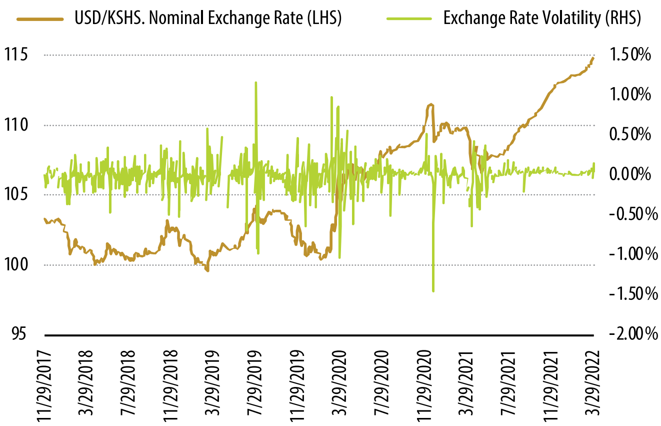
Nevertheless, the overall private sector credit rose on a year-on-year basis by 8.8 percent in January, and 9.0 percent in February before closing the quarter at 10.9 percent in March 2022 (**Figure 3A**). This sustained credit growth is attributed to the increased extension of credit to consumer durables, transport and communication sector, manufacturing, business services and trade (**Figure 3B**).

There were also notable developments in the exchange rate over the period. As depicted in **Figure 4A**, the Kenya Shilling weakened by 3.7 percent and exchanged at an average of Ksh.113.7 in the first quarter of 2022 compared with Ksh.109.7 in a similar period in 2021. The weakening bias is attributable to a widening current account deficit, a decline in foreign exchange reserves and rising jitters in global financial markets as the Russia-Ukraine conflict escalated.

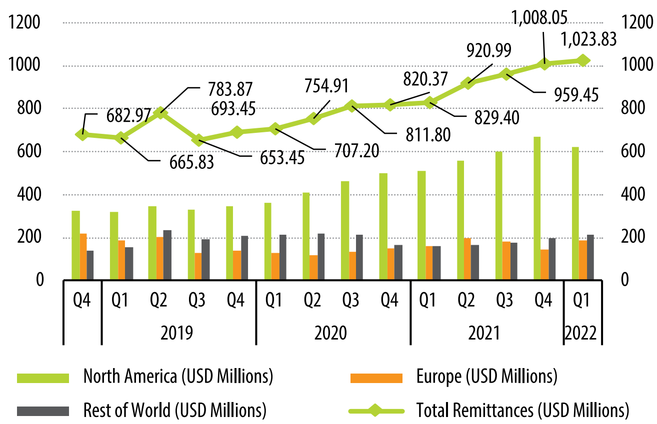
The official usable foreign exchange reserves holdings decreased to USD 7,856 million (equivalent to 4.85 months of import cover) at the end of the first quarter of 2022 from USD 8,556 (5.23 months of import cover) at the end of 2021. Additionally, the remittances remained on an upward trajectory, rising to USD 1,023.8 million during the first quarter of 2022 compared to USD 829.40 million over a similar period in 2021 (**Figure 4B**).

Figure 4: Kenya Shilling -US Dollar Exchange Rate dynamics and Remittances inflow

a) Kenya Shilling -US Dollar Exchange Rate Dynamics



b) Trends in remittances flow by regions

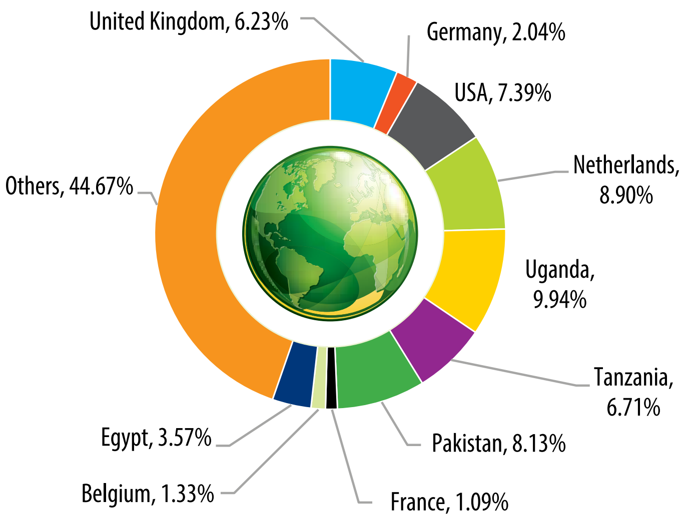


Source: Central Bank of Kenya

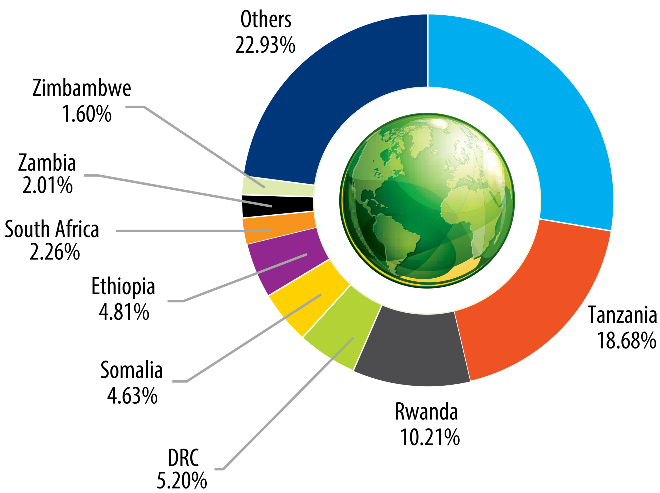
Trends in trade flows between Kenya and its partners remains largely unchanged in terms of share rankings. In terms of export flows, Uganda and Pakistan were at the top of the chart as the leading destinations in Africa and globally, by accounting for 9.94 percent and 8.13 percent of Kenya's total exports during the quarter, respectively. The quarter recorded 25.38 percent growth in tea export to Pakistan, rising from Ksh. 13,470.5 million in the first quarter of 2021 to Ksh. 16,888.8 million in the first quarter of 2022. On the other hand, total exports to Uganda declined by 9.2 per cent to Ksh 20.8 billion in the first quarter of 2022 on account of decline in exports of crude palm oil and cement clinkers. The bulk of import in the first quarter originated from Asia, and it accounted for 67.8 per cent of the import bill, with China remaining the dominant source. Imports from Africa registered an increase of 24.7 percent from Ksh 54.0 billion in the first quarter of 2021 to Ksh 67.3 billion in the period under review. The increase was partly occasioned by increase in imports from South Africa and Tanzania, which exhibited an increase of 64.0 percent and 23.7 percent, respectively.

Figure 4: Kenya's Intra-African and Global Trade Developments

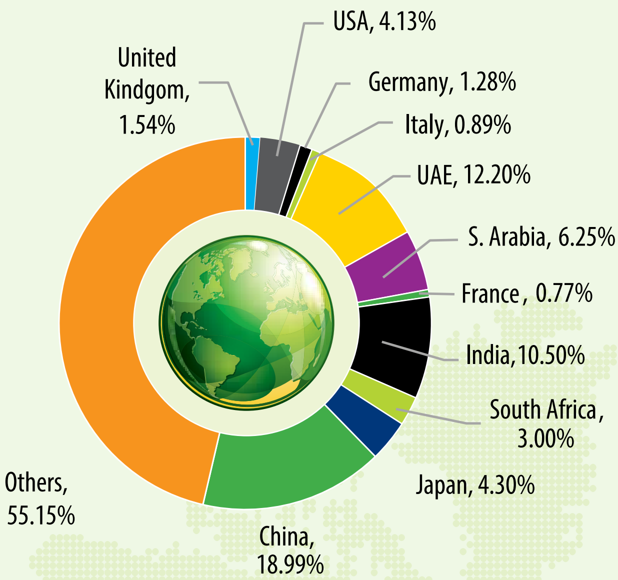
a) Share of exports of goods by trading partners



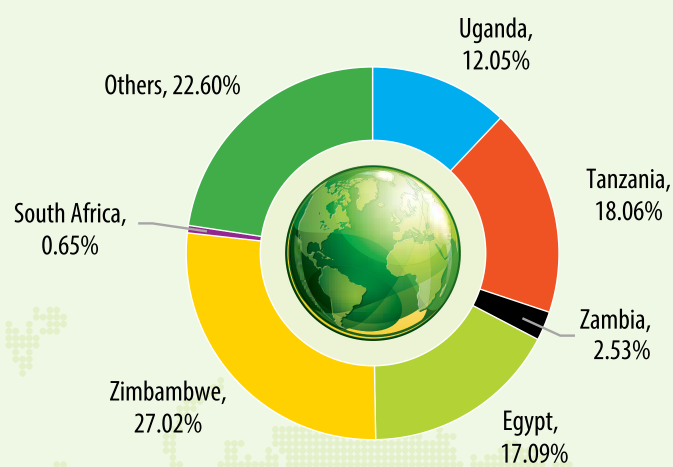
b) Intra-African Trade - Kenya's Major Trading Partners



c) Share of imports of goods by trading partners

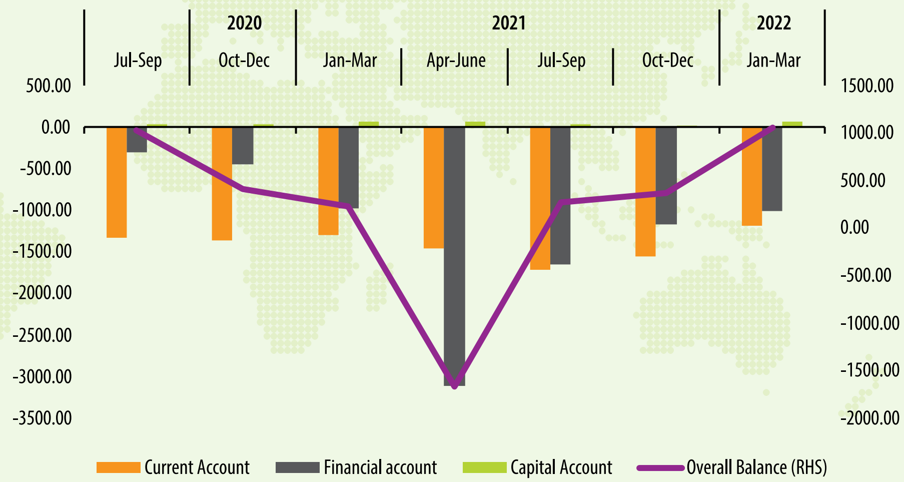


d) Intra-African Share of Imports of goods by trading partners

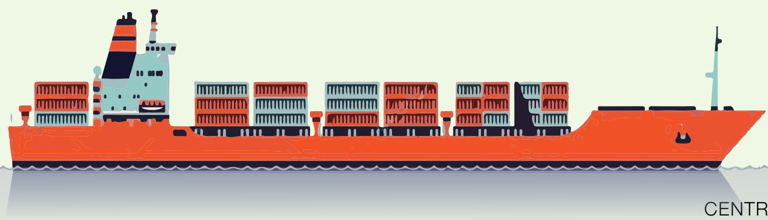


The balance of payment accounts strengthened on account of heighted cross-border activities. The current account deficit narrowed to USD 1,179 million because of a 21 percent increase in remittances and earnings from transport and travel services exports which grew by 89 percent and 38 percent, respectively. The net financial account inflows were higher at USD 1,005 million in the first quarter of 2022, compared to USD 983 million in the first quarter of 2021. Even so, it was lower than USD 1,177 million in the last quarter of 2021. The net capital account inflows in the period under review stood at USD 72 million. Consequently, the overall balance of payment strengthened to a surplus of US$ 1,059 million during the period under review (**Figure 6**).

Figure 6: Balance of the Payments Performance



Source: CBK Quarterly Economic Review



Sectoral Performance

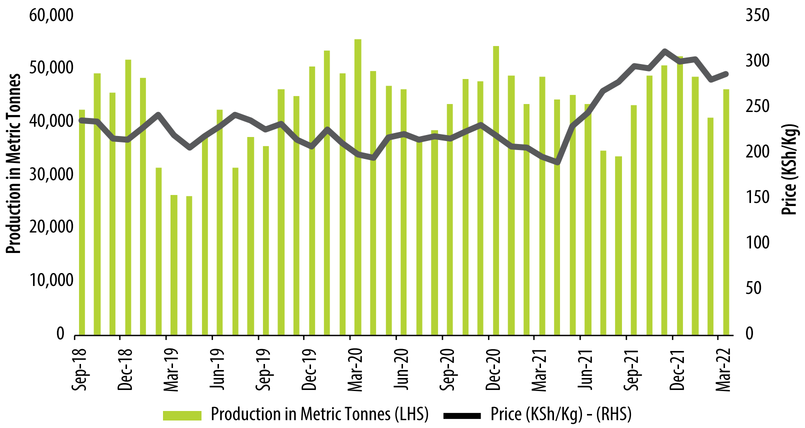
Agriculture

The agricultural sector is not only the driver of Kenya's economy but also the means of livelihood for the majority of Kenyan population. However, of key concern is the over-reliance on three marketed agricultural products: tea, coffee and horticulture. Consequently, improved productivity and an increased agricultural production base of these three crops is critical in enhancing the competitiveness of the agricultural sector.

In fact, tea has been ranked among the leading foreign exchange earners in the country. As depicted in **Figure 7**, tea production declined from 140,987 metric tonnes in the first quarter of 2021 to 135,830 metric tonnes in the first quarter of 2022 on account of extended sunny and dry weather conditions that were recorded over most parts of the country and across the tea growing regions. Additionally, the average monthly tea auction price was 34.74 percent higher in the period under review compared to the first quarter in 2021, mainly on account of minimum reserve price of 2.43 USD per kilogram that was instituted by the Ministry of Agriculture in July 2021.

Both tea and coffee earnings benefitted from the strengthening US dollar, as indicated by export value in local currency created amidst declining export volume. In comparison to the first quarter of 2021, tea export

Figure 7: Tea production and Prices



Source: KNBS

> **"Both tea and coffee earnings benefitted from the strengthening US dollar, as indicated by export value in local currency created amidst declining export volume.**

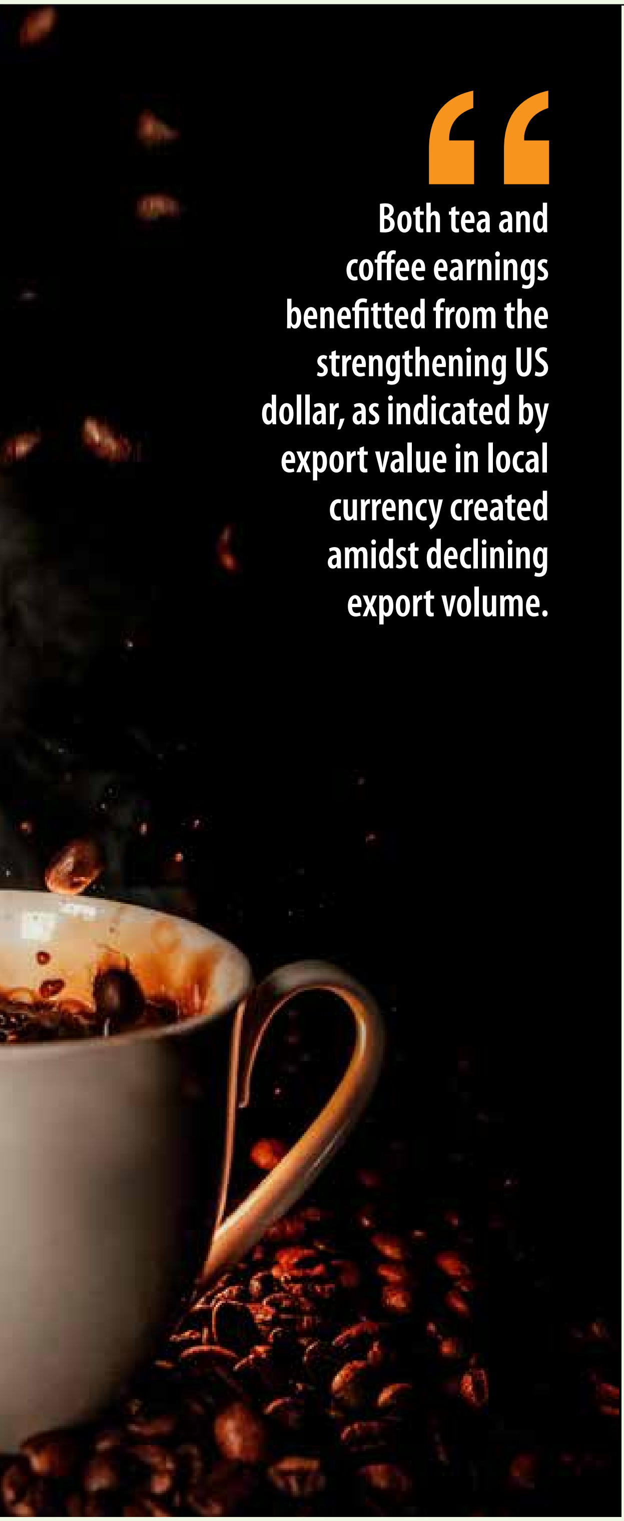
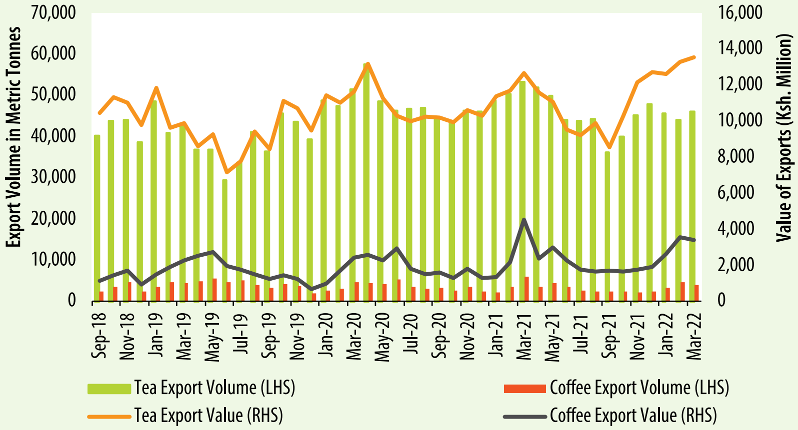


Figure 8: Value of Tea and Coffee Exports

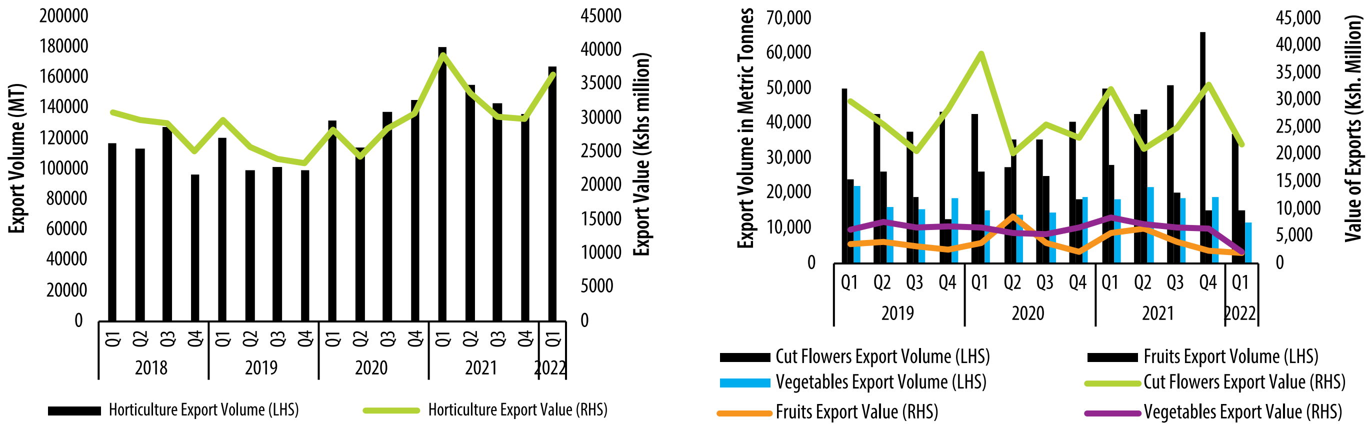


volume declined by 11.08 percent, but the export value was higher by 10.38 percent during the first quarter of 2022. A similar trend was evident with coffee; with its export volume in the first quarter of 2022 growing by 2.12 percent in comparison to a similar period in 2021, as its export value rose by 19.04 percent (**Figure 8**).

The volume and value of horticultural exports in the first quarter of 2022 declined by 6.89 percent and 7.31 percent, respectively, relative to a similar period in 2021, mainly driven by a slump in all the three major horticultural exports. However, it is no surprise as these horticultural export products have often been less competitive in the global market because they are exported in their raw form with little or no value added. As the quantity of cut flower exports declined by 26.3 percent in the current period, relative to a similar period in 2021, the quantity of fruits and vegetables exported were also significantly low compared to a similar period in the previous year. Similarly, the quantity of fruits exports decreased by 64.3 percent, from 28,222.6 metric tonnes in the first quarter of 2021 to 15,210.81 metric tonnes in the current period (**Figure 9**). Notably, there was a boost in fruit farming with the Chinese government lifting the ban on imports effected in 2019 on non-frozen produce. As a result, Kenyan farmers could access the Chinese markets with their avocado exports, particularly those that could comply with all applicable Chinese phytosanitary (plant health) laws and regulations, health and safety standards and be free from any quarantine pests of concern to China.

Figure 9: Export trends in horticultural sub-sector

a) Horticultural Exports **b) Cut Flowers, Vegetables and Fruits**

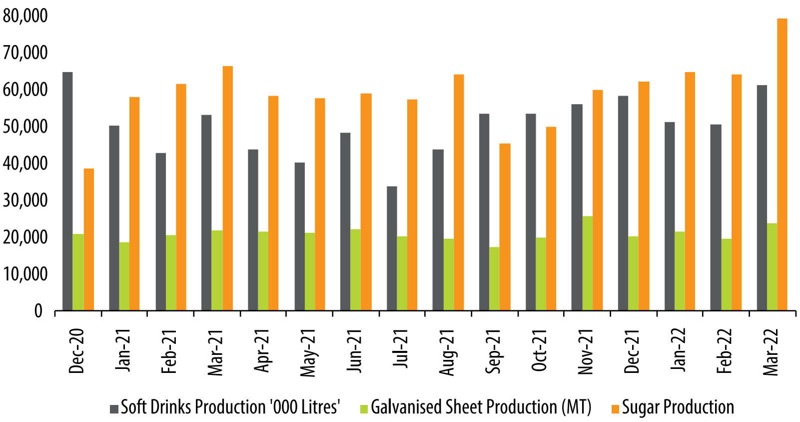


Source: KNBS

Manufacturing

The manufacturing sector has been acknowledged for driving economic development in many countries across the globe by stimulating and sustaining high productive growth. However, Kenya, akin to many other developing countries, has not managed to develop a robust manufacturing sector since production in the later is predominantly geared towards consumer goods. Consequently, economic growth in Kenya has been primarily driven by the agriculture and services sectors. During the quarter, the Gross Domestic Product of the manufacturing sector expanded by 3.7 percent and it accounted for 8.34 percent of the Gross Domestic Product. The production of soft drinks increased by 11.7 percent to about 208.7 million litres in the current period, up from 186.0 million litres produced during a similar period in 2021. Similarly, total galvanized sheet produced during the quarter edged upwards by 6.59 percent, rising 65,206 metric tonnes. On its part, sugar production grew by 11.67 percent during the first quarter of 2022.

Figure 10: Production in manufacturing sub-sectors

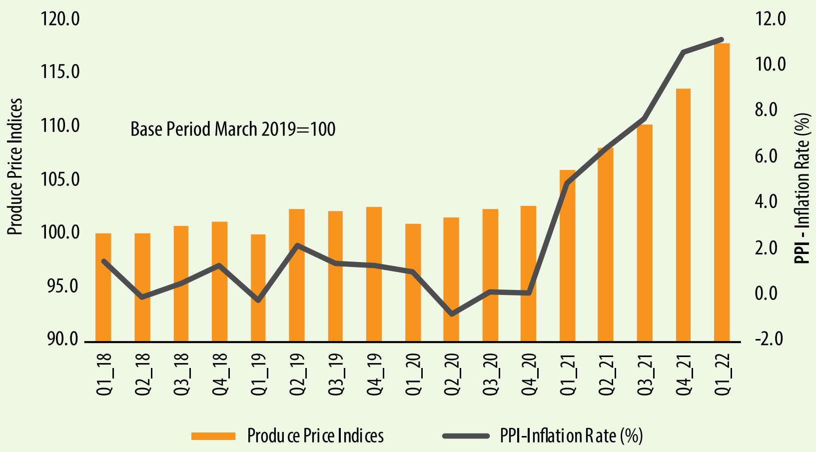


Source: KNBS

Producer Price Index

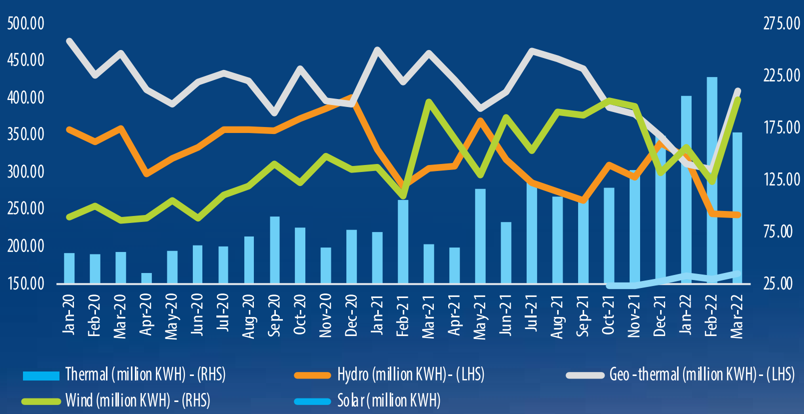
In the first quarter of 2022, the producer prices index increased by 11.2 percent in comparison to a similar period in 2021 to settle at 117.9 (**Figure 11**). The recent marked acceleration in PPI inflation is partly attributable to the low base created in 2020 at the onset of Covid-19 pandemic. Even so, there are fundamental drivers which have compounded the effect. For instance, various production inputs, particularly commodities, have experienced sharp price increases since the onset of the pandemic and the increase was further catalysed during the quarter by the Russia-Ukraine geo-political tensions, reflecting large shifts in demand for goods, and supply chain bottlenecks. The staggered re-opening of economies and supply chains' inability to recover quickly enough to meet the surge in demand led to mismatches in demand and supply. Thus, the shift in consumer demand towards goods, supported by the fiscal stimulus packages in advanced economies coupled with economic sanctions imposed on Russia piled additional pressure on supply chains and boosted demand for commodities and other inputs.

Figure 11: Producer Price Index



Source: KNBS

Figure 10: Production in manufacturing sub-sectors



Energy

The trends in the energy sector reveals continued efforts to align to the global shift to renewable energy, particularly solar and wind energy, since the production of the duo has gradually grown. During the quarter, the production of solar energy production rose to 97.64 million kilowatts from 22.18 million kilowatts produced in a similar period in 2021, thereby representing 340.2 percent increase on solar energy generation. Wind energy generation equally increased, albeit marginally (7.58 percent increase). Despite the strides made in the production of renewable energy, energy production is dominated by hydropower and geothermal energy. The two sources have continued to account for slightly over 70 percent of energy production in the country (**Figure 12**).

Crude oil prices in the global market remained elevated during the quarter, in part, on account of the Ukraine-Russian geopolitical tension. The Murban crude oil prices surged upwards, from USD 74.4 per barrel at the end of the fourth quarter of 2021 to USD 113.5 per barrel at the end of the first quarter of 2022. Consequently, the average domestic petrol pump prices and LPG gas prices which had remained unchanged for five consecutive months were revised upwards in March 2022, as shown in **Table 1**.

Table 1: Average Monthly Crude Oil and Retail Fuel Prices

	Apr-21	May-21	Jun-21	Jul-21	Aug-21	Sep-21	Oct-21	Nov-21	Dec-21	Jan-22	Feb-22	Mar-22
Murban crude oil (US$/Barrel)	63.2	66.9	71.9	73.5	70.3	73.9	82.1	80.4	74.4	85.4	94.0	113.5
Super petrol (KES/Litre)	123.7	127.2	128.0	128.0	128.0	135.5	130.5	130.5	130.5	130.5	130.5	135.5
Diesel (KES/Litre)	108.6	108.6	108.6	108.6	108.6	116.5	111.5	111.5	111.5	111.5	111.5	116.5
Kerosene (KES/Litre)	98.8	98.8	98.8	98.8	98.8	111.7	104.5	105.5	106.5	106.5	106.5	104.5
LPG (13Kgs)	2074.2	2074.2	2074.2	2394.2	2420.7	2445.2	2513.7	2611.2	2638.8	2659.2	2659.7	2866.2

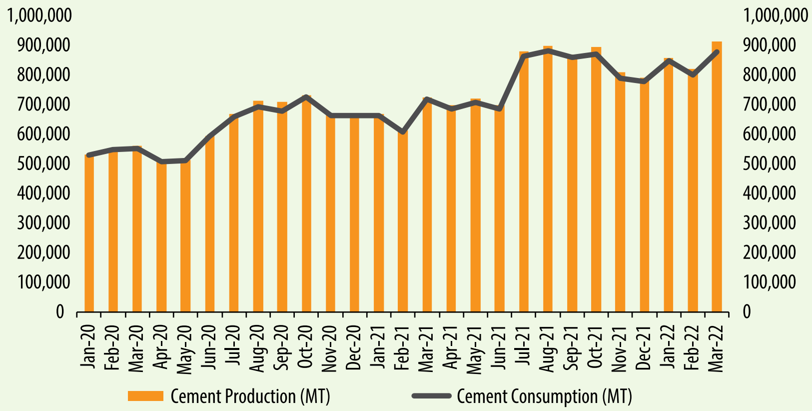
Source: ADNOC oil prices and KNBS

“ Cement consumption rose from 1,985,967 metric tonnes the first quarter of 2021 to 2,520,968 metric tonnes in the current period under review

Building and Construction

Activities in the building and construction sector sustained the upward trajectory. Cement production was 29 percent higher in the quarter under review relative to a similar period in 2021. In tandem with this growth, the latter's consumption was equally higher, rising from 1,985,967 metric tonnes the first quarter of 2021 to 2,520,968 metric tonnes in the current period under review; representing a 26.9 percent growth (**Figure 13**).

Figure 13: Cement Production and Consumption

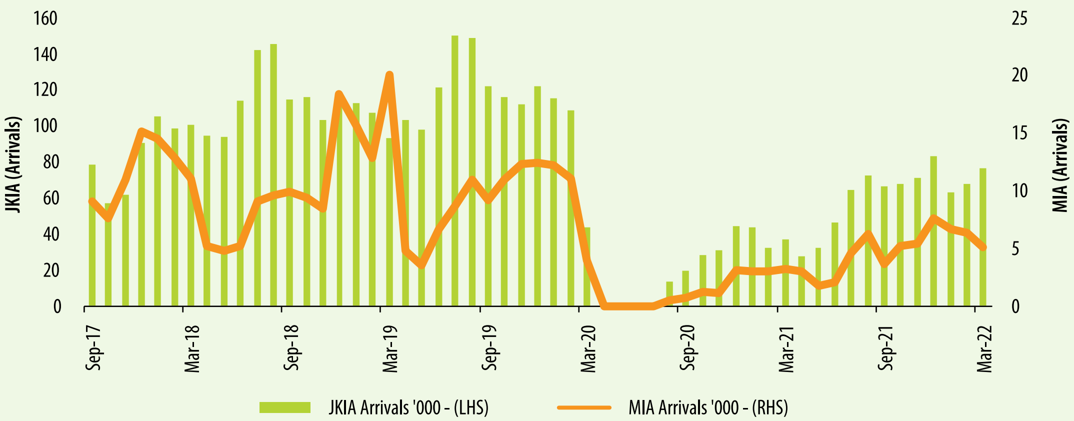


Source: KNBS

Tourism

Significant improvements in the number of tourists' arrivals continue to be registered, signifying a recovery of a sector that had been depressed by to the impact of the pandemic containment measures. The total inbound tourist arrivals during the quarter stood at 225,321; which was 83.9 percent higher than the total inbound tourists over a similar period in 2021. The inbound arrivals through JKIA terminal stood at 207,203 in the quarter compared to 18,118 arrivals through Mombasa international airport (MIA) terminal (**Figure 14**).

Figure 14: Monthly Inbound Tourist Arrivals



Government Revenue and Expenditure

Analyses of the Government's budgetary operations for the third quarter of FY 2021/2022 show that total revenue and grants grew by 18.3 percent to Ksh. 525.9 billion from Ksh 444.6 billion over a similar period in FY 2020/21. Total expenditures over the period also grew, but by a higher margin of 26.1 percent, to Ksh 7/63.7 billion in FY 2021/2022.

However, since the growth in the total revenue & grants was more than the growth in total expenditures, the overall impact was a contraction in the revenue – expenditure gap (**Figure 15**).

Figure 15: **Quarterly Revenue-Expenditure Gap**

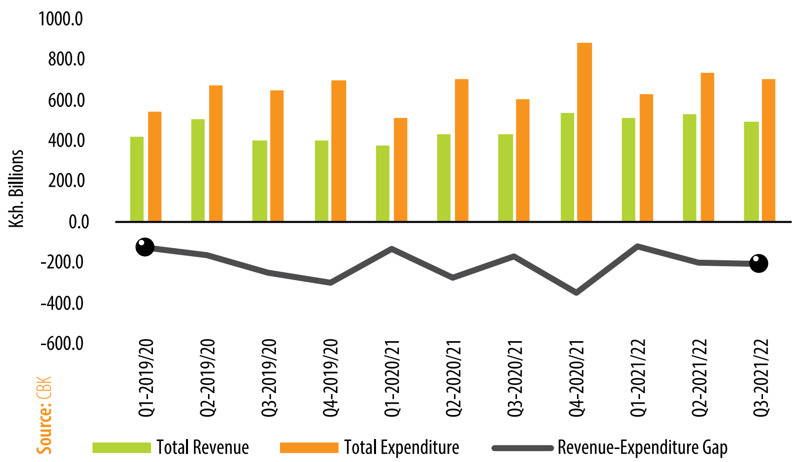
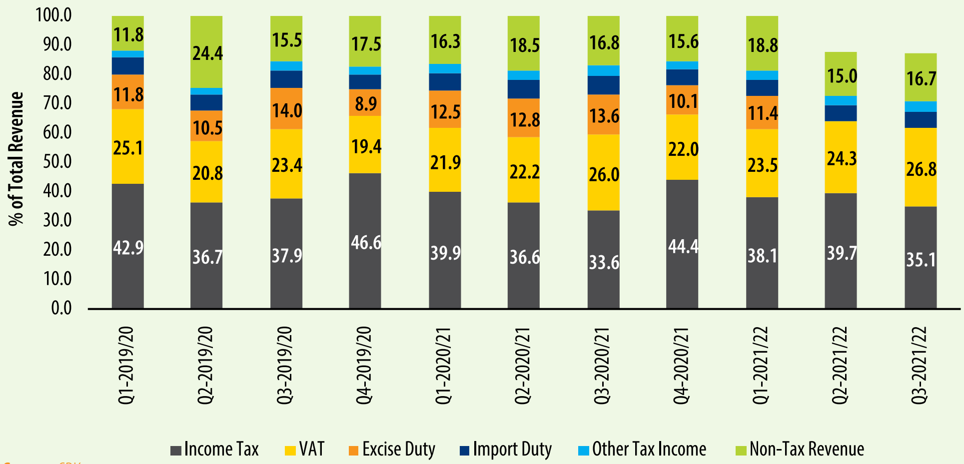


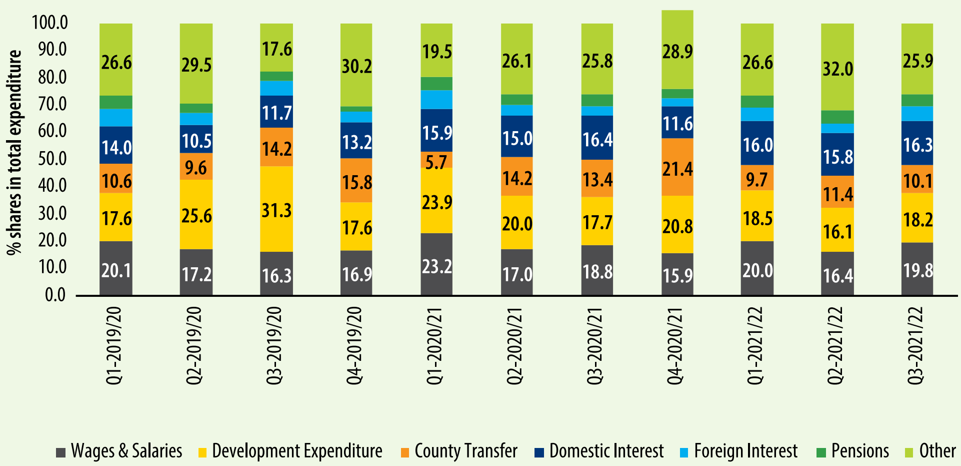
Figure 16: Quarterly Revenue Structure



Source: CBK

As shown in **Figure 16**, there was a shift in in the contribution of various sources of government revenue; the proportion of revenue raised through income tax declined during the quarter, while non-tax revenue increased relative to the previous quarter. Government expenditure grew by 26.1 percent, with wages and salaries weighing heavily on the same as they accounted for 19.8 percent of the total expenditure. Other significant expenditure components were development expenditure (18.2 percent) and domestic interest rate (16.3 percent). The share of county transfers was lower in comparison to a similar period in FY 2020/2021 (**Figure 17**).

Figure 17: Quarterly Expenditure Structure



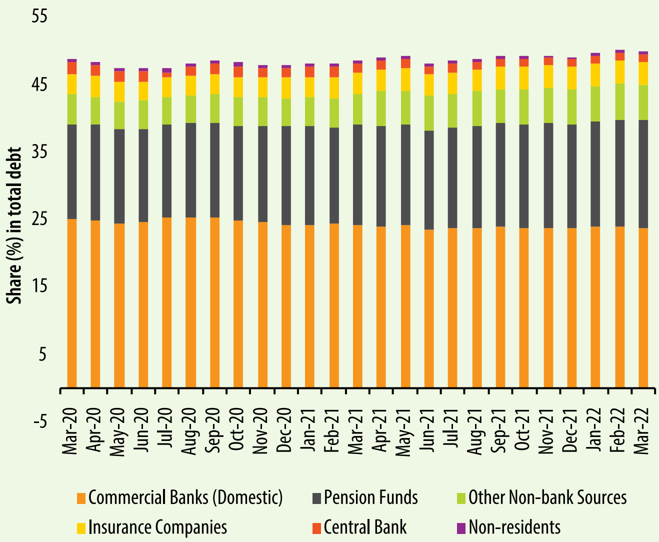
Source: CBK

Government Deficit Financing and Public Debt

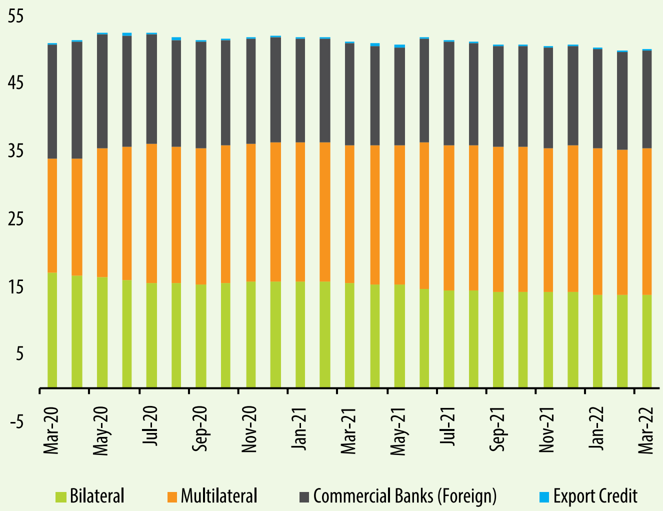
Total public debt as at end March 2022 stood at Ksh. 8.4 trillion (estimated at 67.8% of GDP) having grown from Ksh. 7.3 trillion in March 2021 (or 66.2% of GDP). Domestic debt accounted for 33.8 percent of GDP while the external debt was 34.0% of GDP. Public and publicly guaranteed external debt increased by 0.8 percent during the third quarter of the FY 2021/22. This increase was mainly driven by loan disbursements from multilateral lenders. The composition of external debt continued to improve with increased flow of Multilateral loans. The share of outstanding debt from official multilateral lenders (who provide concessional loans) increased by 0.5 percentage points, while the proportion of commercial debt decreased by 0.2 percentage points.

Figure 18: External and Domestic Debt and its Composition

a) Domestic Debt



b) External Debt



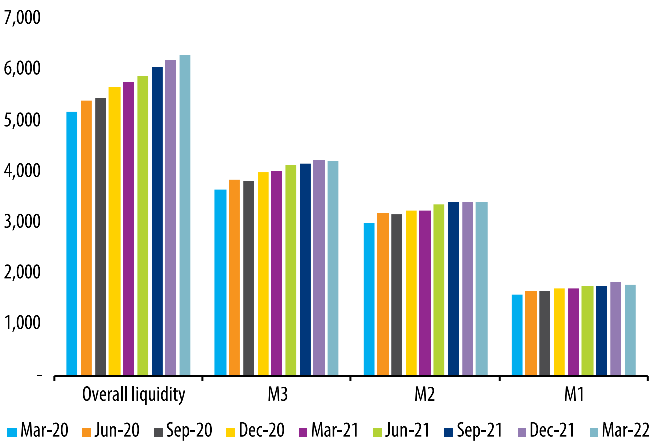
Source: CBK

Money Supply

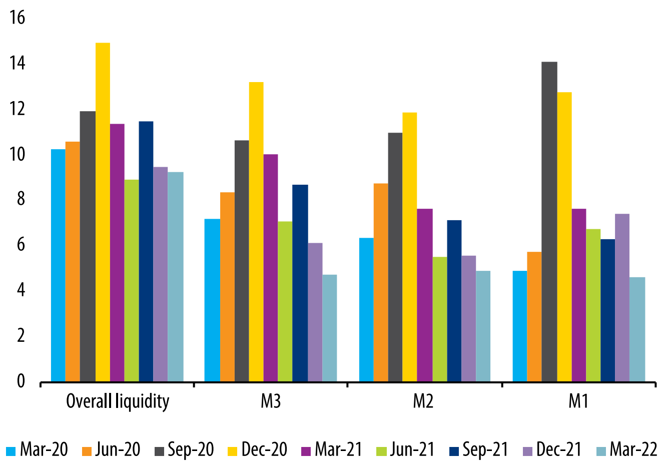
Overall liquidity in the economy grew by 1.6 percent on a quarter-on quarter basis by the end of March 2022 to close at Ksh. 6,303.4 billion. The largest component of liquidity , that is, broad money supply (M3), registered a slower growth in the first quarter of 2022 by 0.3 percent compared to a growth of 1.4 percent in the previous quarter (**Figure 19**).

Figure 19: Trends in Monetary Aggregates

a) Volumes, Ksh Billions



b) Year-on-Year growth rates, %



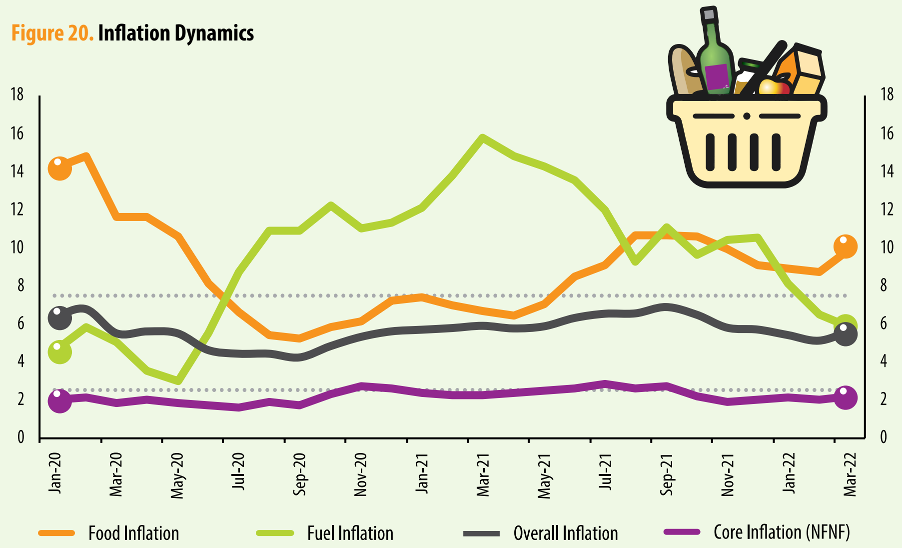
Source: Central Bank of Kenya

Inflation

Overall inflation for the first part of the quarter, dropping from 5.7 percent in December to 5.4 percent in January and 5.1 percent in February. However, following the onset of the war in Ukraine, inflationary pressure was induced to the domestic economy as a result of global supply disruptions and the resulting shocks on key commodity prices.

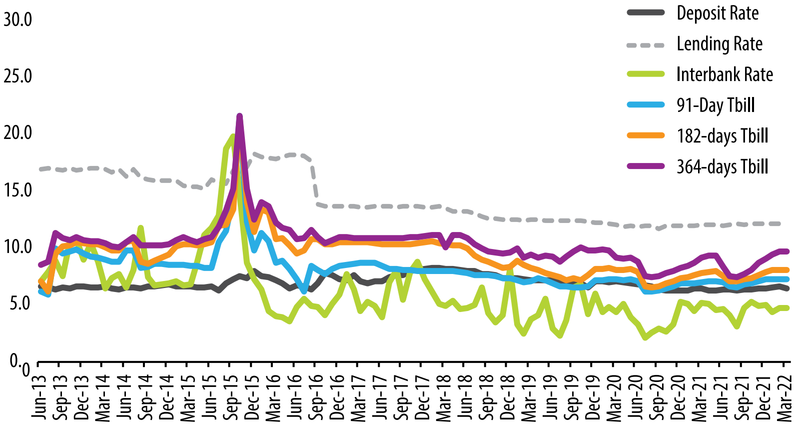
Consequently, the overall inflation surged in March to 5.6 percent; though remaining within the 5±2.5 percent government target range (Figure 20). At the end of the quarter, the food and fuel inflation stood at 9.9 percent and 5.8 percent. Core inflation, however, rose marginally to end the quarter at 2.2 percent.

Figure 20. Inflation Dynamics



Source: Central Bank of Kenya

Figure 21: Interest Rates Dynamics



Source: Central Bank of Kenya

The banking sector average cost of funds remained relatively unchanged - with the average deposit rate in March 2022 rising marginally to 6.5 percent from 6.4 percent in March 2021. The short-term interest rates, however, depicted some volatility overtime in response to temporary market liquidity changes. In March 2022, the average overnight interbank rate stood at 4.7 percent compared to 5.2 percent registered in a similar period in 2021.

Yields on government securities in March also edged up, to 7.3 percent, 8.1 percent and 9.8 percent for the 91-day, 182-day and 364-day treasury bills, respectively (**Figure 21**).

Interest Rates

As the Central Bank Rate (CBR) was kept unchanged at 7.0 percent during the first quarter of 2022, market interest rates were largely stable during the period. The average banking industry lending interest rate in March 2022 stood at 12.2 percent, thus reflecting some stickiness that was partly an outcome of the slow rollout of risk-based pricing frameworks in the banking sector.

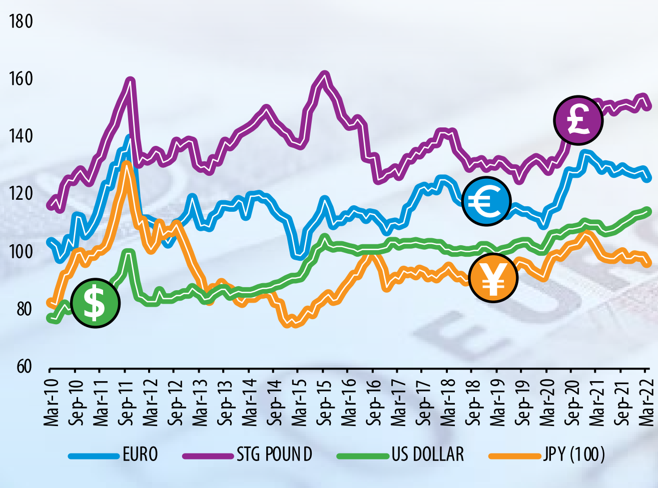
Exchange Rates

The Kenya Shilling during the quarter weakened by 3.7 percent against the dollar mainly on account of the Russia-Ukraine geopolitical tensions that created uncertainties in global foreign exchange and stock markets.

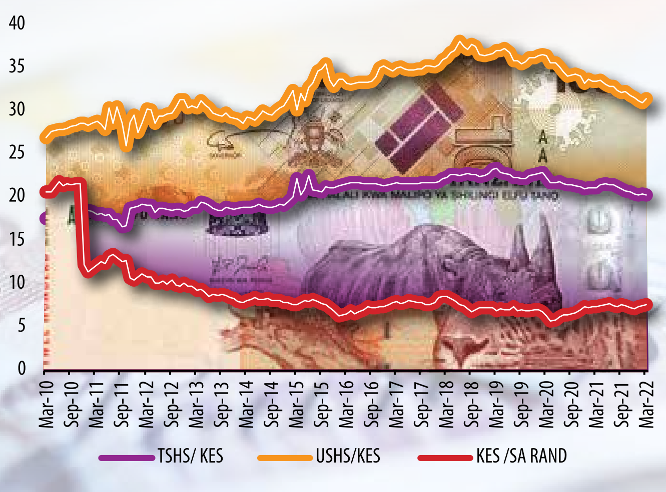
The Shilling also weakened against the Sterling Pound but strengthened against the Euro and the Japanese Yen. In the region, it weakened against the Uganda and Tanzania Shilling, but remained steady against the South African Rand during the review period (**Figure 22**).

Figure 22: Exchange Rate Developments

a) Major currencies



b) EAC region currencie



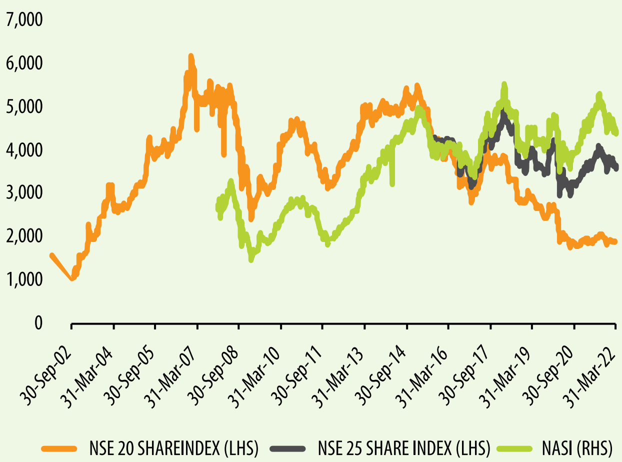
Source: Central Bank of Kenya

Capital Markets

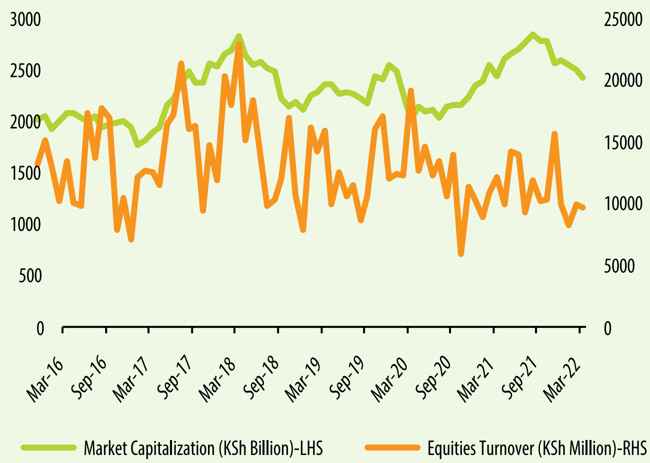
Mixed performance characterised the capital market during the quarter (Figure 24). In particular, the benchmark indices recorded mixed trends with the NASI down 1.82 percent, while the NSE 20 and NSE 25 up by 0.02 percent and 0.95 percent to close the first quarter of 2022 at 1,846.74 and 3,565.06, respectively. Equities market turnover at the NSE decreased by 13.9 percent to Ksh. 27,860.72 from Ksh. 31,735.29 recorded over a similar period in 2021. Market capitalization was also down, declining to Ksh. 2,425.53 billion at the end of the first quarter of 2022, from Ksh. 2,437.0 billion in a similar period in 2021. The volume of contracts traded in the derivative markets stood at 1,188.

Figure 24: Trends in Nairobi Securities Exchange Leading Indicators

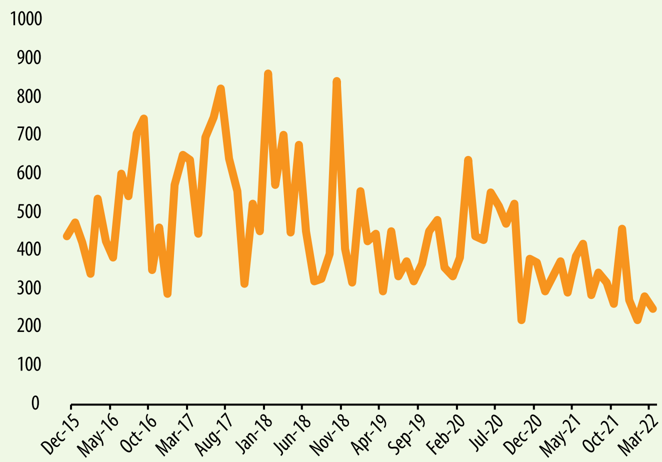
a) NASI is tilted down, while the NSE 20 and NSE 25 edge upwards



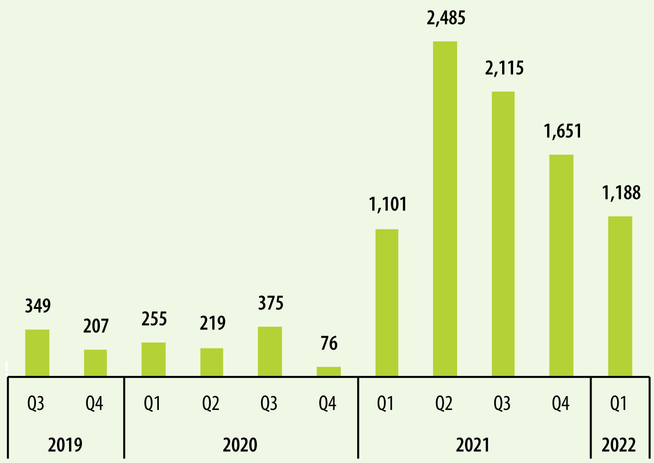
b) Market capitalization and equity turnover are both declining



c) Number of Shares Traded continue to decline



d) Number of derivatives contracts decline on a quarter-on-quarter basis



Source: Nairobi Securities Exchange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Banking Sector Performance

The banking sector performance indicator point to a strong but growing industry with all the regulatory indicators remaining above the minimum threshold (Figure 25). The quarter registered growth in the total net assets rising to Ksh 6,103.0 billion in March 2022, from Ksh 6,008.0 billion in December 2021, thereby representing 1.6 percent increase.

Similarly, the total shareholders' fund was on an upward trajectory, closing the quarter at Ksh 912.50 billion, up from Ksh 903.4 billion at the end of the previous quarter. Despite the industry gross loans growing from ksh. 3,248.70 billion in December 2021 to ksh. 3,382.40 billion in March 2022, credit risk remained a major concern as the Gross Non-performing Loans (NPLs) to Gross Loans Ratio rose to 14.0 percent over the period – from 13.1 percent in the fourth quarter of 2021 - occasioned by 11.0 percent increase in gross Non-performing Loans (NPLS) as compared to a 4.1 percent increase in gross loans. Capital adequacy ratio remaining strong, at 18.9 percent, above the minimum capital regulatory requirement of 14.5 percent. Core capital to total risk-weighted assets ratio and total capital to total risk-weighted assets ratio though above regulatory minimum limits of 10.5 percent and 14.5 percent, however, decreased to 16.2 percent and 18.9 percent, respectively in the first quarter of 2022, down from 16.7 percent and 19.6 percent in the fourth quarter of 2021. The banking sector's overall liquidity was strong during the quarter, at 55.0 percent against a regulatory minimum limit of 20 percent (Figure 25).

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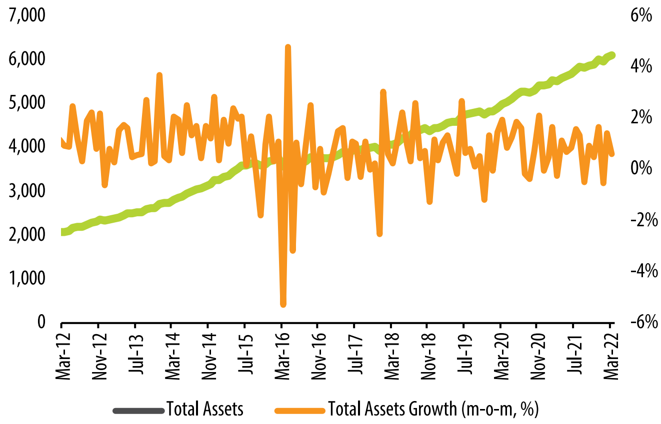
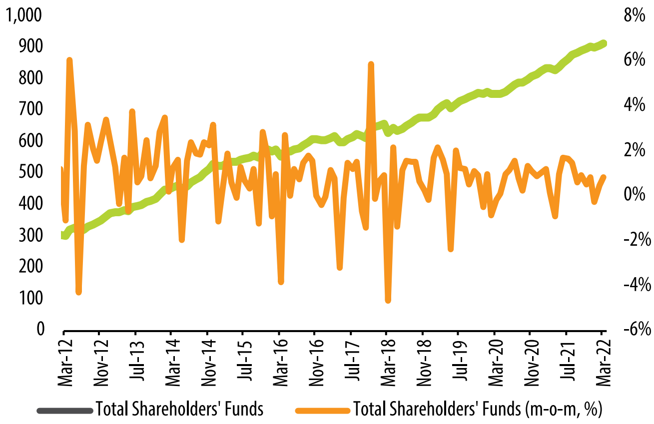
Figure 25: The performance of the banking sector

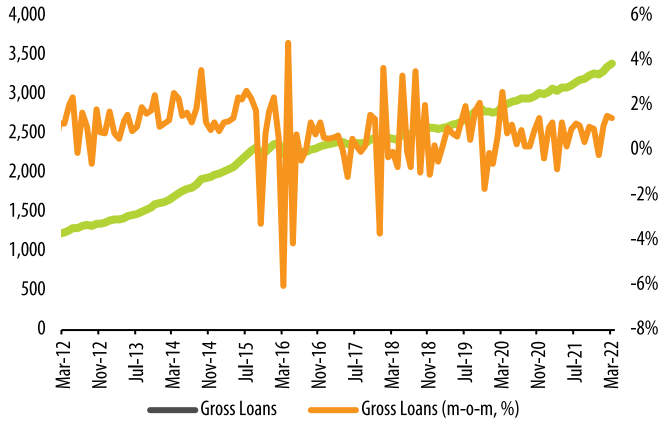
Total net assets grew by 1.6 percent from the previous quarter....



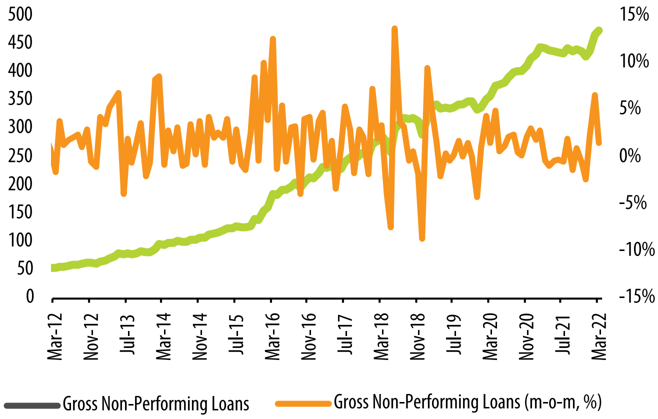
Total shareholders funds remained on an upward trend...



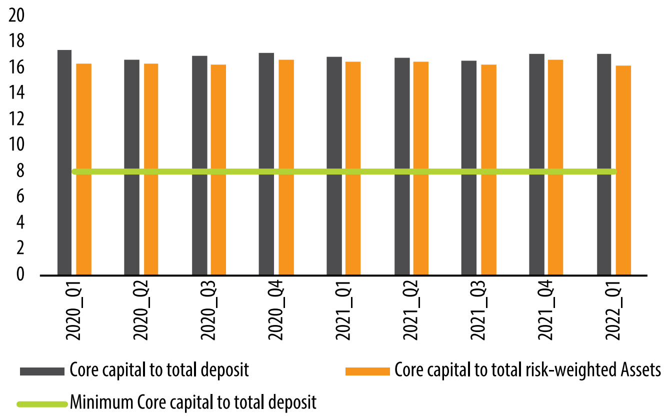
The gross loans grew from ksh. 3,248.70 billion in December 2021 to ksh. 3,382.40 billion in March 2022...



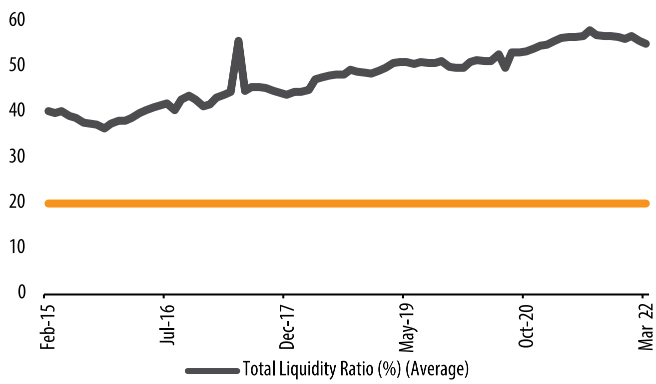
The gross non-performing loans (NPLs) increased to Ksh 473.7 billion at the end of the first quarter of 2022.......



The sectors capital indicators were above regulatory thresholds.....



The banking sector liquidity ratio remained above the minimum statutory level of 20 percent.....



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