February 9, 2026

RESEARCH NOTE NO.1 – 2026 (RN/1/26)

A call to sustain the Current Monetary Policy Stance

Highlights

The decision of the Monetary Policy Committee (MPC) of the Central Bank of Kenya at its meeting scheduled for 10th **February 2026** is expected to be underpinned by the following five key developments:

- **First**, headline inflation, though within target range, faces upsurge risks from food supply side;
- **Second**, domestic economic growth depicting resilience and its fragility is easing off on stronger supply of credit;
- **Third**, domestic interest rates continue declining and yet to reflect the full transmission of previous successive cuts in the Central Bank Rate;
- **Fourth**, the private sector credit growth edging upwards, though cautiously, as banks watch the evolution of nonperforming loans in key sectors;
- **Fifth**, exchange rate remains stable supported by a steady current account deficit, strong inflows of diaspora remittances and positive sentiment supported by strong official foreign exchange reserves position.

"Inflation remains low but risks are imminent. ...Banking sector on course to smooth transitioning of its existing portfolios to the new pricing framework..

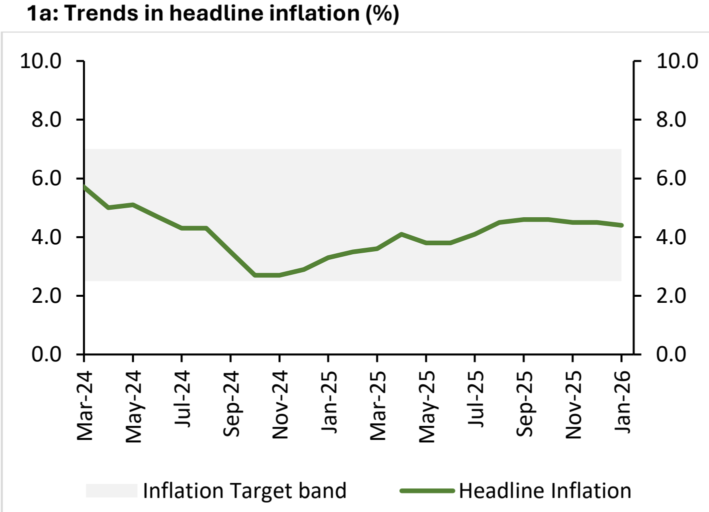
Considering the above developments and the balance of inflation risks in the economy, we view that there is merit to keep the CBR unchanged. This move will allow the full transmission of the previous CBR cuts through the market and ensure a non-disruptive transition of the entire banking sector's Kenya shilling variable rate loan book to the revised risk-based pricing framework scheduled to complete by end February 2026.

Background

At its meeting on **10th February 2026**, the Monetary Policy Committee (MPC) is expected to anchor its policy decision on five key developments:

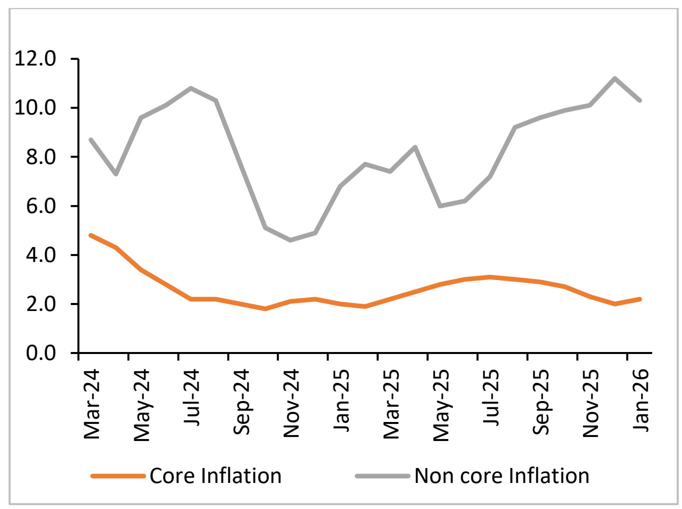
First, headline inflation, though within target range, faces upsurge risks from food supply side. The headline inflation, as reflected in **Figure 1a**, remains largely within the target range of 2.5% to 7.5%. In January 2026, the headline inflation stood at 4.4%, marginally below 4.5% recorded in December 2025. Moreover, the decomposition of inflation drivers (in **Figure 1b)** shows a clear divergence between core and non-core inflation components, with the latter manifesting volatile food prices. The ongoing dry spell across the food basket zones presents upsurge risks on inflation. In addition, the risks of external price pressures pushing up domestic inflation are also evident. These include the potential pass-through effects of tariff adjustments resulting from ongoing trade tensions between many key trading countries and the U.S.A, that are projected to influence global inflation landscape. While commodities and Murban crude oil prices remain steady **(Figure 1c),** Global Supply Chain Pressure Index reflects a potential pressure **(Figure 1d)**. Going forward, Kenya's inflation outlook will largely hinge on the evolution of domestic food prices, with the risk of drought and a prolonged dry spell threatening agricultural output and exerting pressure on prices.

1a: Trends in headline inflation (%)



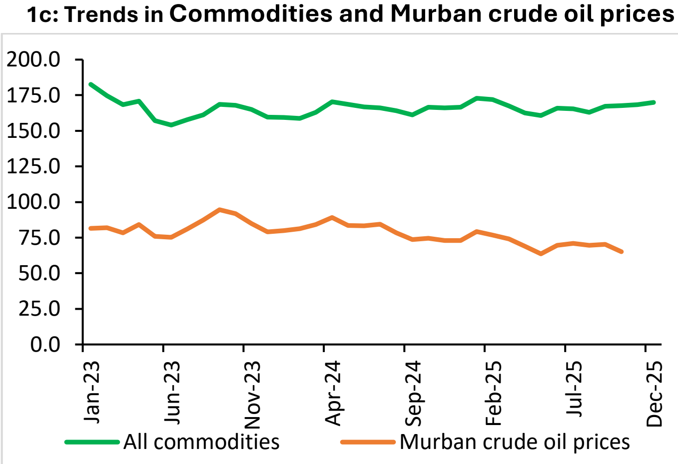
Source: KNBS

1b: Headline inflation drivers



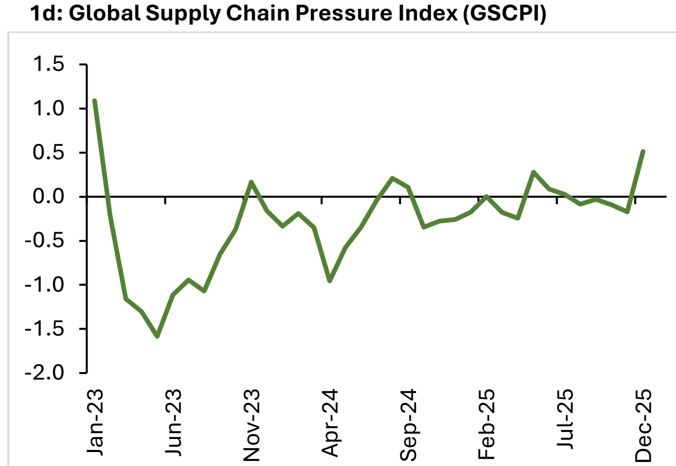
Source: KNBS

1c: Trends in Commodities and Murban crude oil prices



Source: Oil price.com and IMF Commodity prices

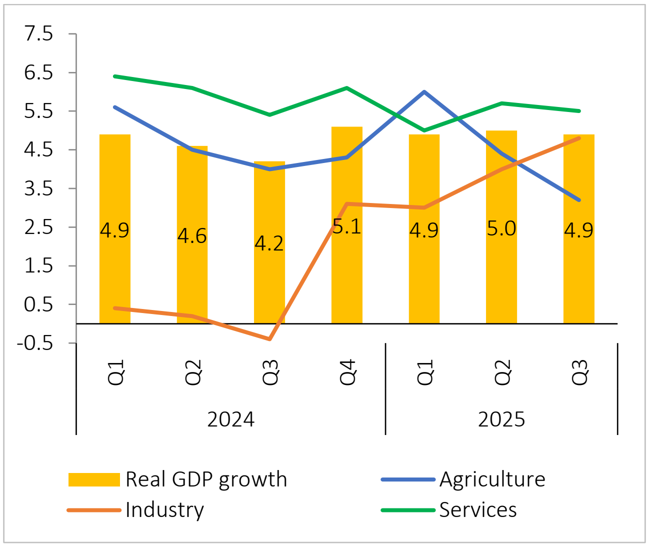
1d: Global Supply Chain Pressure Index (GSCPI)



Source: Federal Reserve Bank of New York

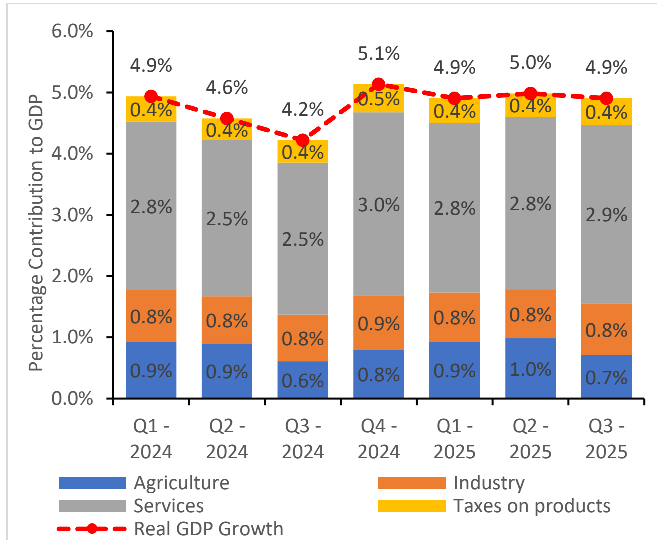
Second, domestic economic growth is depicting resilience and its fragility is easing off on stronger supply of credit. The economy has continued to demonstrate resilience, growing by 4.9% in the third quarter of 2025, compared 4.2% in a similar quarter in 2024 **(Figure 2a)**. While the services sector consistently accounts for the largest share of growth, agriculture's contribution remains volatile mirroring weather patterns and structural productivity challenges, while industry provides a modest but steady contribution **(Figure 2b)**.

2a: Domestic Economy Growth rates (%)



Source: KNBS

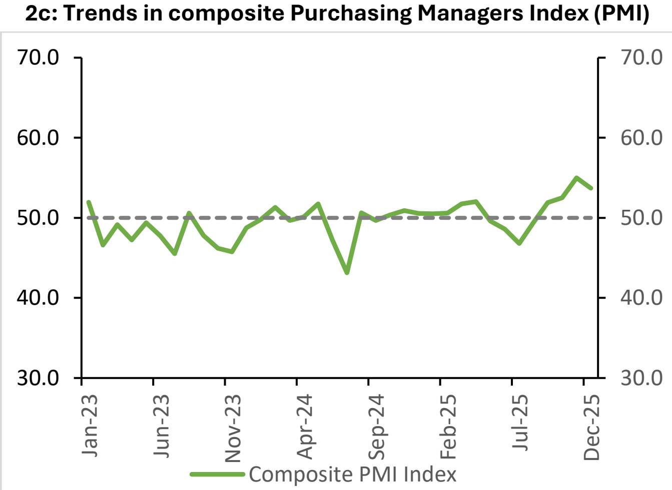
2b: Sectoral contribution to Kenya's GDP growth rates



Source: KBA staff computations

Higher frequency indicators depict a sustained month after month growth in economic activity. The country's Purchasing Managers Index (PMI) posted levels above 50.0 for the fifth consecutive month in January 2026 **(Figure 2c)**, signalling continued expansion by the manufacturing sector. Additionally, global growth is projected to be resilient at 3.3% in 2026 **(Table 2d)**, though downside risks to this outlook remain on abrupt market corrections, geopolitical tensions, elevated public debt and trade disruptions threatening to potentially weaken investment and growth. Conversely, rapid AI-driven productivity gains and eased trade frictions could bolster global growth, boosting efficiency, business dynamism and policy predictability.

2c: Trends in composite Purchasing Managers Index (PMI)



Source: IHS Markit

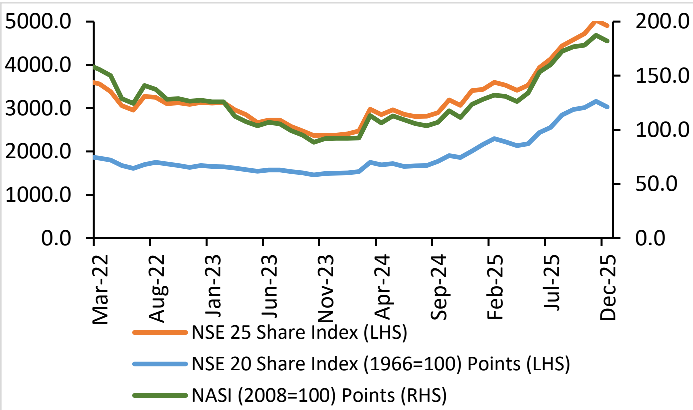
2d: Global Economic Growth rates (%)

		January 2026 Projections	
	2024	**2025**	**2026**
World Output	**3.3**	**3.3**	**3.3**
Advanced Economies	**1.8**	**1.7**	**1.8**
United States	2.8	2.1	2.4
Euro Area	0.9	1.4	1.3
Japan	-0.2	1.1	0.7
Emerging and Developing Economies	**4.3**	**4.4**	**4.2**
China	5.0	5.0	4.5
India	6.5	7.3	6.4
Sub-Saharan Africa			
Nigeria	4.1	4.2	4.4
Kenya	4.7	4.8	4.9
South Africa	0.5	1.3	1.4

Source: IMF WEO (January 2026)

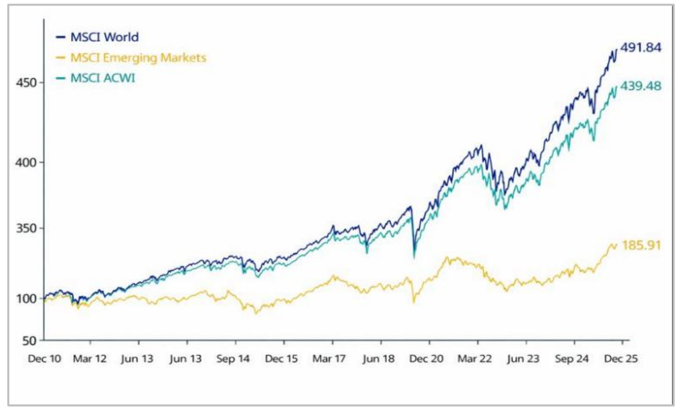
In the equities market, investor sentiment remains largely positive **(Figure 3a)**. All the NSE benchmark indices have remained bullish, reflecting a pass-through of the performance of the global equities markets (**Figure 3b)** and eased monetary policy stance internally and in advanced economies. Going forward, Kenya's equity market performance is expected to be driven by the pace of adjustments in interest rates in the local and global markets, moderated by the evolution of domestic fundamentals such as fiscal credibility, corporate profitability and exchange rate stability.

3a: Performance of the domestic equity market



Source: NSE

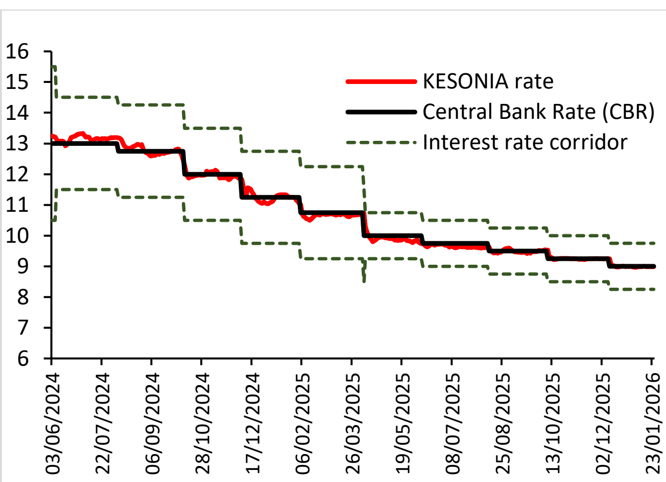
3b: Performance of global equity market



Source: MSCI

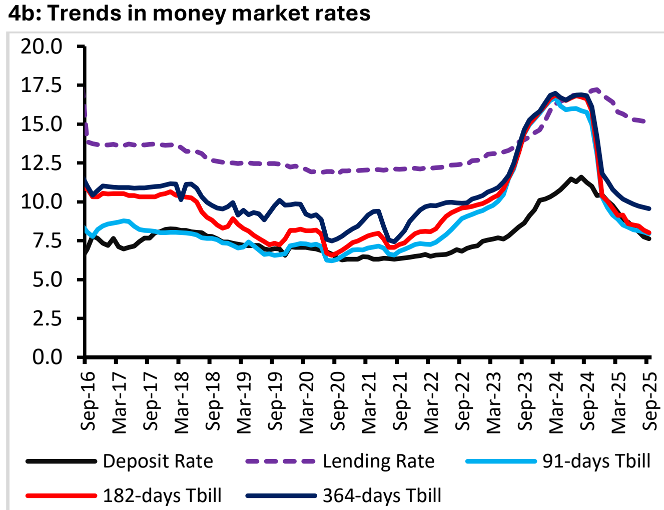
Third, domestic interest rates continue declining but yet to reflect the full transmission of previous successive cuts in the Central Bank Rate. The CBK monetary operations continue to ensure the KESONIA rate tracks the Central Bank Rate (CBR) within the interest rate corridor **(Figure 4a).** Both short term and longer-term interest rates have also declined **(Figure 4b & 4d)**, but at differentiated paces reflecting market and structural rigidities. Some global economies, such the U.S.A have paused policy rate cuts **(Figure 4c).** For instance, in January 2026, the U.S. Federal Reserve maintained the federal funds target range at 3.5% - 3.75%, following three rate cuts in 2025. Similarly, in December 2025, the ECB kept its key rates unchanged: the deposit facility at 2.00%, main refinancing at 2.15% and marginal lending at 2.40%. Going forward, these policy rates are expected to impact Kenyan economy through capital flows and exchange rate pressures, if not matched by a corresponding decision on the local policy rate.

4a: Trends in KESONIA rate and the Central Bank Rate



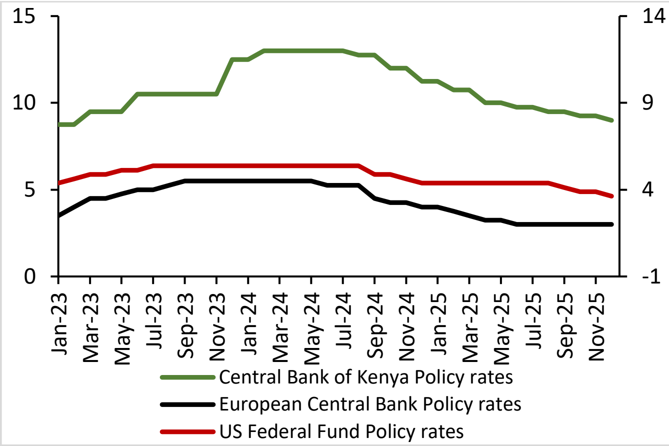
Source: CBK

4b: Trends in money market rates



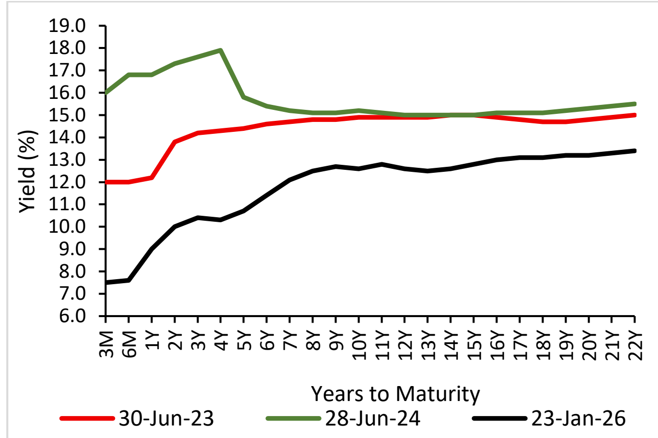
Source: CBK

4c: Trends in selected policy rates



Source: Central banks' websites

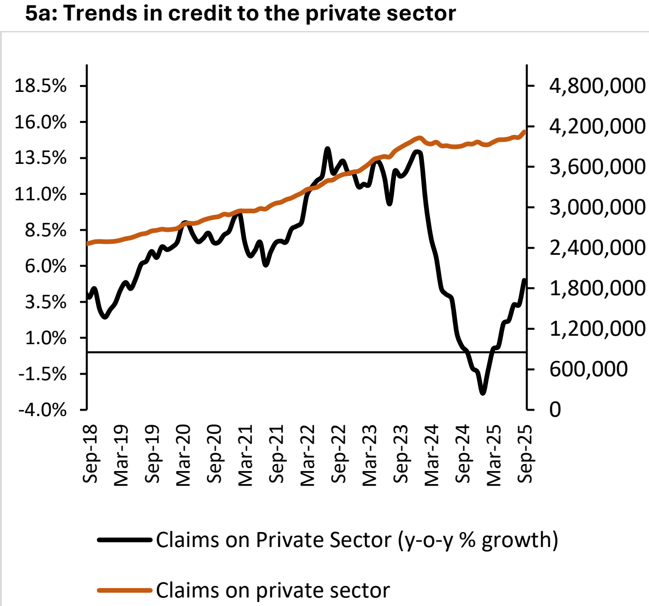
4d: Trends in the domestic yield curves



Source: NSE

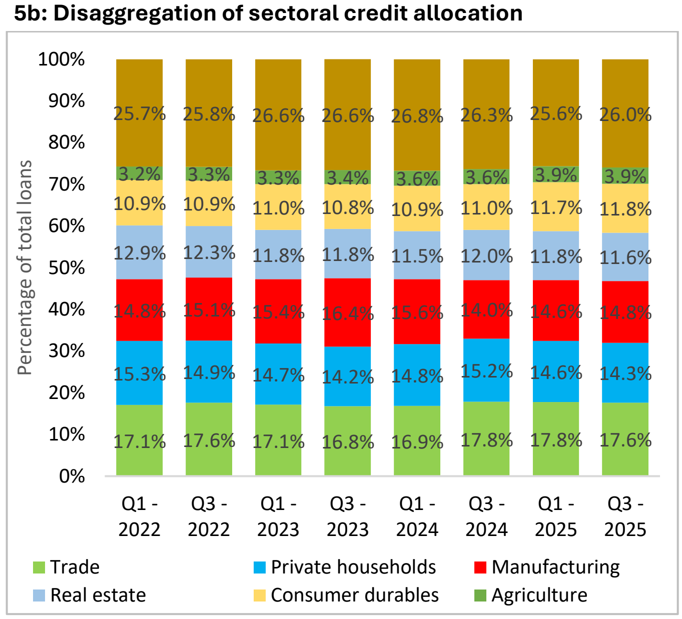
Fourth, the private sector credit growth is edging upwards, though cautiously, as banks watch the evolution of nonperforming loans in key sectors. Credit to the private sector remains on a strong recovery path, growing by 6.3% in November 2025 up from 5.9% in October 2025 and -2.85% in January 2025 **(Figure 5a)**. Strongest recovery in November 2025 was observed in manufacturing (7.9%), building and construction (43.8%), trade (6.2%) and consumer durables (8.3%). The disaggregation of sectoral credit allocation in **Figure 5b** indicates a tilt toward sectors perceived to be safer while segments that account for a large portion of non-performing loans such as real estate face tighter lending standards. Credit growth has also been supported, though mildly, by easing non-performing loans (NPLs) as economic activity picks up **(Figure 5c)**. Bank lending is expected to grow faster, but cautiously, as banks monitor sectoral evolution of NPLs particularly in key sectors.

5a: Trends in credit to the private sector



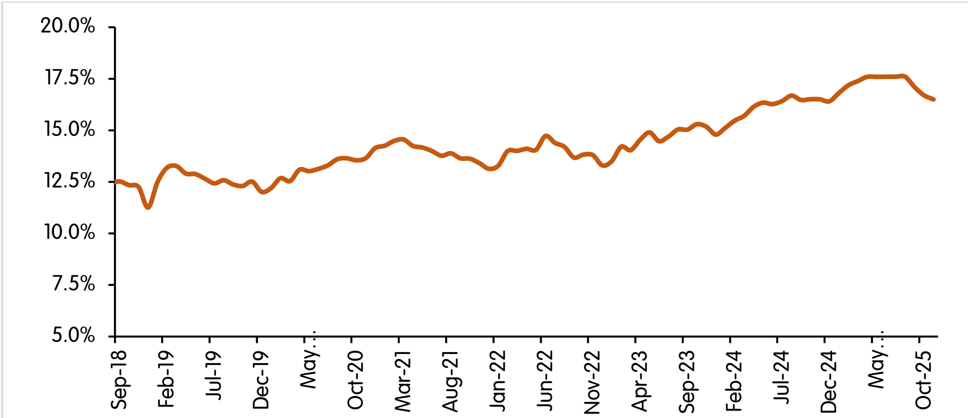
Source: CBK

5b: Disaggregation of sectoral credit allocation



Source: CBK

5c: Trends in Industry NPLs ratio (Asset Quality)

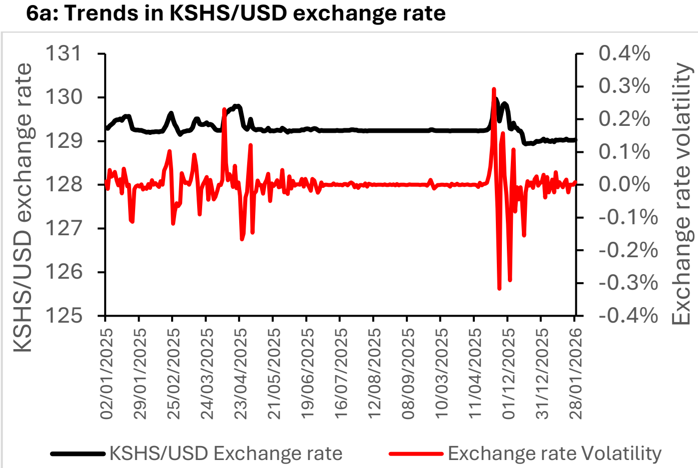


Source: CBK

Reforms effected in 2025 in credit pricing are expected to affect credit growth dynamics. The sector is transitioning to the new risk-based credit pricing environment, shifting from each respective bank's base rate to either KESONIA or the CBR. All Kenya shilling-denominated variable rate facilities issued from December 1 are priced based on the new benchmark plus a margin that accounts primarily of the customer's risk. The portfolios pre-existing December 1 are expected to be transitioned to the new benchmark by 1st of March 2026. Banks in January 2026 issued 30-day notices to customers about the transition and are currently recalibrating their systems to reflect these changes. Holding all factors unchanged, a smooth transition is expected as the industry has provided certainty to customers with adequate 30-day notice period. Once full transition of portfolios has been undertaken and disclosures of lending rates are made, the industry will be able to reflect comparable prices across lenders and enable customers to appreciate the role of their risk profile in loan rates.

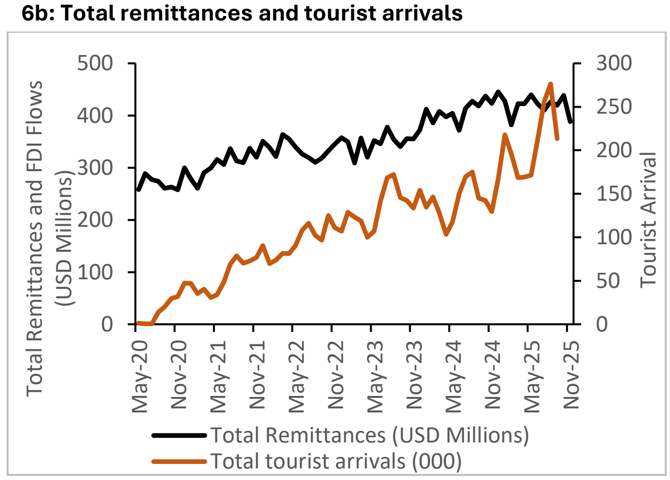
Fifth, exchange rate remains stable supported by a steady current account deficit, strong inflows of diaspora remittances and positive sentiment supported by strong official foreign exchange reserves position. The stability of the KSHS/USD exchange rate **(Figure 6a)** has been supported by strong remittance inflows and recovering tourist arrivals **(Figure 6b)**, alongside resilient export earnings from key crops such as tea, horticulture, and coffee **(Figure 6c)**. In addition, confidence in the ability of the economy to manage short term foreign exchange market shocks has been enhanced, with elevated CBK's usable foreign exchange reserves at USD 12,334 million, equivalent to 5.3 months of import cover as of 29 January 2026 (higher than the statutory minimum of 4 months) **(Figure 6e)**. Nonetheless, risks to the foreign exchange outlook remain moderate; but actors continue to focus on the new external debt contracting in 2026 and service obligations (**Figure 4b**).

6a: Trends in KSHS/USD exchange rate



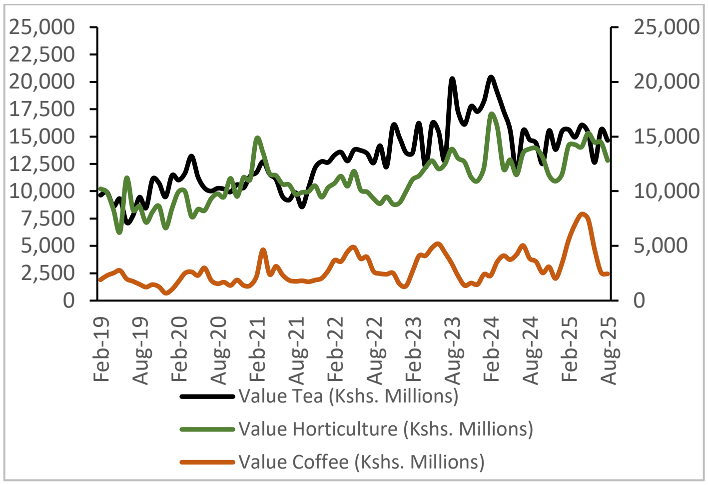
Source: CBK

6b: Total remittances and tourist arrivals



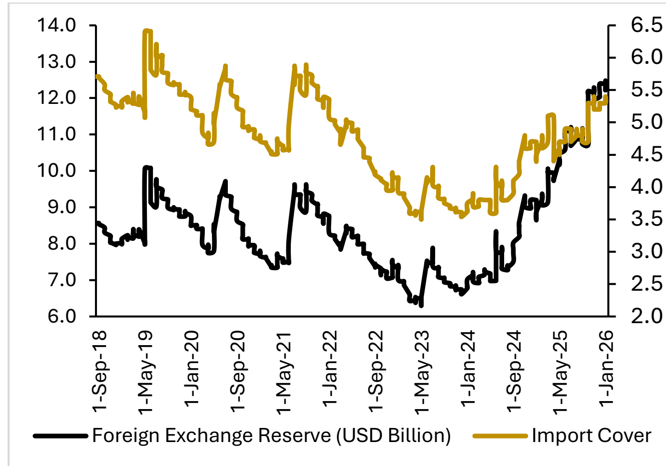
Source: CBK

6c: Export Trends of Key crops



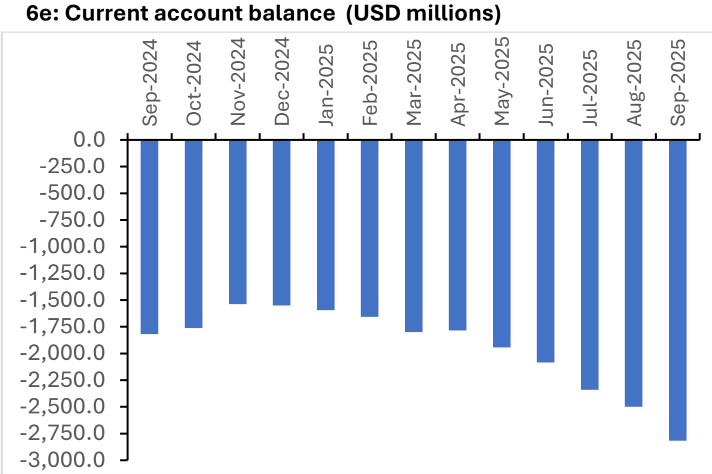
Source: CBK

6d: Foreign exchange reserves and import cover



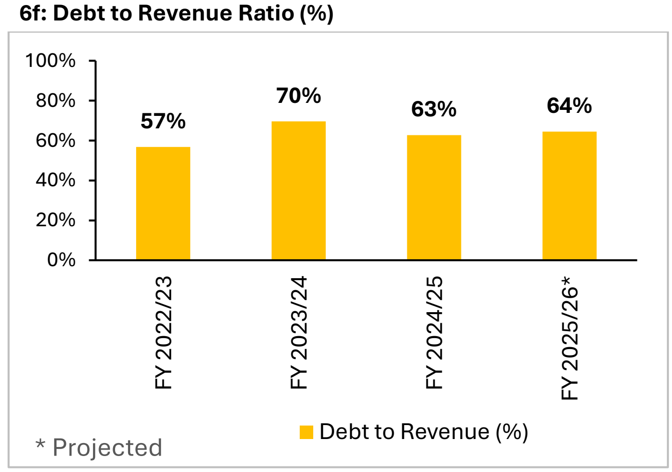
Source: CBK

6e: Current account balance (USD millions)



Source: CBK

6f: Debt to Revenue Ratio (%)



Source: CBK

Conclusion

Considering the above developments and the balance of inflation risks in the economy, we view that there is merit to keep the CBR unchanged. This move will allow the full transmission of the previous CBR cuts through the market and ensure a non-disruptive transition of the entire banking sector's Kenya shilling variable rate loan book to the revised risk-based pricing framework scheduled to complete by end February 2026.

Comments on this *Research Note* can be forwarded to research@kba.co.ke