

# Research Note



1 October 2026

RESEARCH NOTE NO.5 – 2026 (RN/5/26)

## A Call to hold the Central Bank Rate to Anchor Private Sector Credit Growth and Sustain Economic Activity

### Highlights

The decision of the Monetary Policy Committee (MPC) of the Central Bank of Kenya in its meeting scheduled for **7<sup>th</sup> October 2026** is expected to be underpinned by the following developments:

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*“With inflation within the target range, and exchange rate stability sustained, sustaining the current stance of monetary policy, to anchor the recovery in private sector credit and economic activity is appropriate..”*

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- **First**, headline inflation remains within target range, though edging up towards the upper limit, driven primarily by supply-side factors and moderated by minimal demand pressures;
- **Second**, economic growth remains resilient, though vulnerable to headwinds from external developments and projected domestic wide-spread El Niño rains;
- **Third**, the monetary policy stance, favourable interest differentials and responsive yields are strengthening credit expansion and supporting economic growth; and
- **Fourth**, exchange rate stability continues to provide an important buffer, but protracted oil price pressure increases external-sector risks.

With inflation currently anchored within the target range and minimal threats to its escalation in the near term, we view that maintaining the current stance of monetary policy in keeping the CBR unchanged at 8.75% would be appropriate to support the ongoing private sector credit growth and sustain economic activity.

## Background

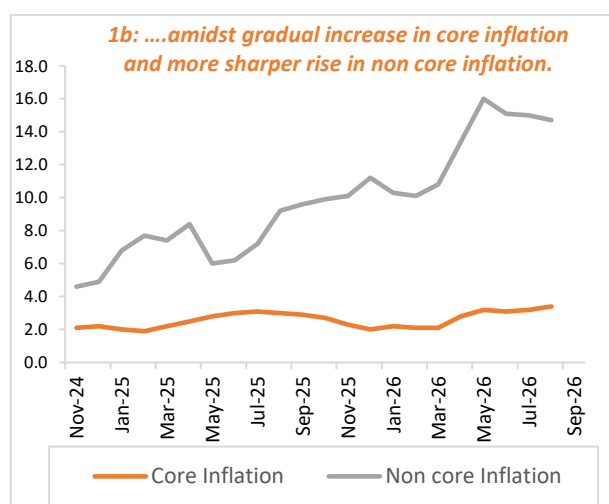
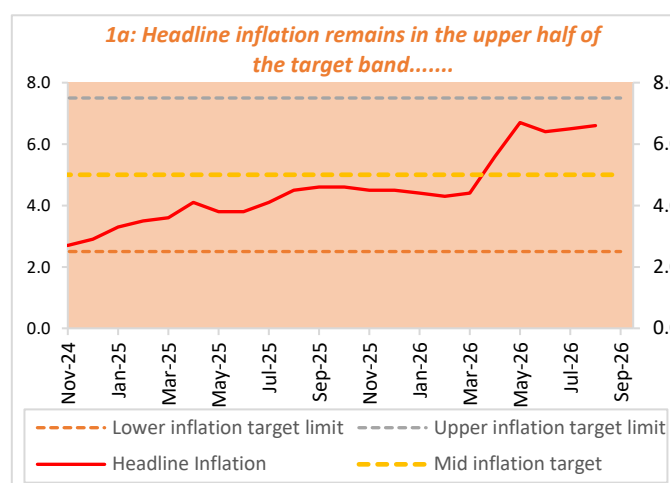
The **October 7, 2026** Monetary Policy Committee (MPC) meeting is expected to set the stance of monetary policy, with the decisions informed primarily by four key developments.

**First, headline inflation remains within target range, though edging up towards the upper limit, driven primarily by supply-side factors, and moderated by minimal demand pressures.** As shown in **Figure 1a**, headline inflation rose progressively from 4.3% in February 2026 to 6.6% in August and 6.8% in September 2026, moving closer to the upper limit of 7.5%. September inflation was driven mainly by an increase in food inflation to 9.5% and elevated transport inflation at 15.6%.

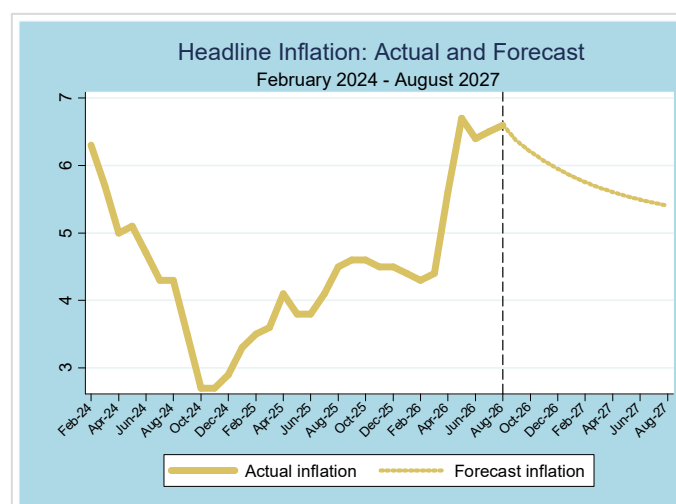
Changes in core and non-core inflation trends remained differentiated (**Figure 1b**), with core inflation rising minimally from 2.1% in March 2026 to 4.0% in September 2026, whereas non-core inflation moderated, reaching 14.0% in September 2026 from 14.7% in August, but reflecting a sharper elevation from 10.8% in March 2026.

Nevertheless, our inflation forecast shows inflation dissipating moderately as food supply shocks ease with the onset of harvest in major bread-basket zones (**Figure 1c**). This outlook, however, remains conditional on global energy prices stabilizing and the Government sustaining its measures to contain oil price increases, food supply conditions improving, and the exchange rate stability sustained.

**Figure 1: Inflation trends, drivers and Forecast**



Source: KNBS (data) & KBA (forecasts)

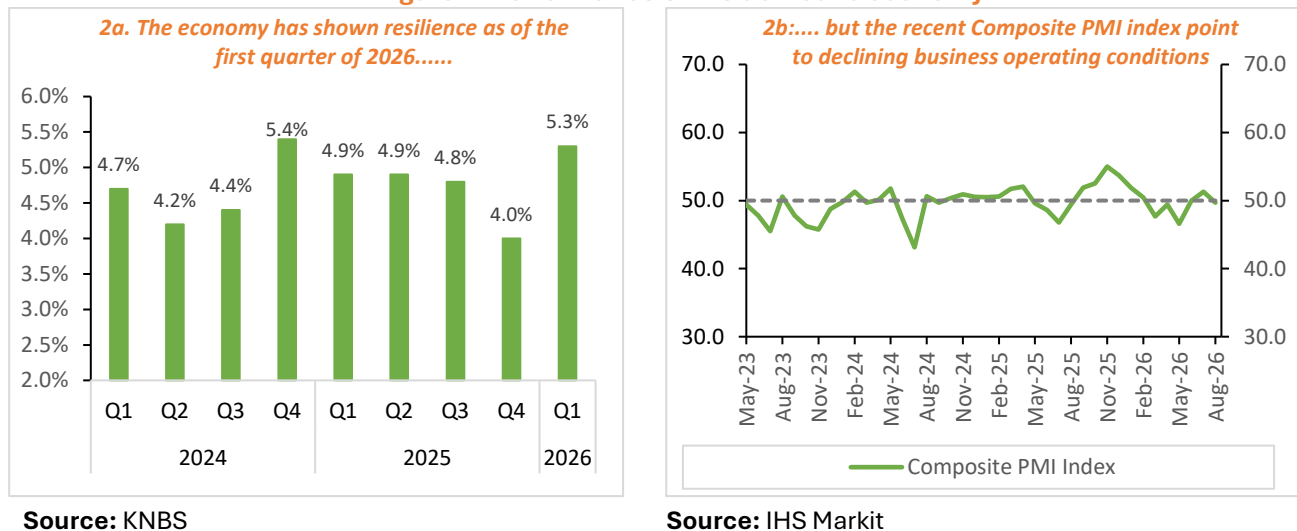


**Second, economic growth remains resilient, though vulnerable to headwinds from external developments and projected domestic wide-spread Elnino rains.** As shown in **Figure 2a**, real GDP that expanded by 5.3% in the first quarter of 2026, compared with 4.9% in the corresponding quarter of 2025, faces several headwinds. The Purchasing Managers' Index (PMI) fell to 49.7 in August 2026 (**Figure 2b**), indicating a

deterioration in operating conditions with a drop in demand for production inputs leading to reductions in output and purchase of stocks, as firms continue to face elevated fuel and other input costs.

Going forward, additional headwinds to the recovery path include rising possibilities of higher fuel and food prices that would constrain household consumption, and elevated production and transportation costs that may depress business margins and investment. Additionally, the impending El Niño rains expected from October 2026 through the first quarter of 2027 across 43 out of the 47 counties, risks adversely impacting agricultural production with implications on food prices. Externally, weaker global growth, which is projected by OECD at 2.9% in 2026 and 3.0% in 2027<sup>1</sup>, could reduce external demand for Kenyan exports and services. On the fiscal front, elevated government financing requirements can increase competition for domestic funding and put upward pressure on market interest rates, potentially moderating private investment.

**Figure 2: Performance of the domestic economy**



**Third, the monetary policy stance, favourable interest differentials and responsive yields are strengthening credit expansion and supporting economic growth.** The movements in the Central Bank Rate (CBR) that respond to inflationary pressures and threats have helped moderate demand pressures and contain second round oil price related supply side effects (**Figure 3a**). Moreover, relative to selected advanced economy policy rates, Kenya's CBR remains well elevated (**Figure 3b**) providing a cushion against any adverse interest rate differential that would threaten capital flows and exchange rate stability. More recently, the Federal Reserve, European Central Bank and Bank of England have moved into tightening cycles; potentially indicating the path of monetary policy in the near to medium term.

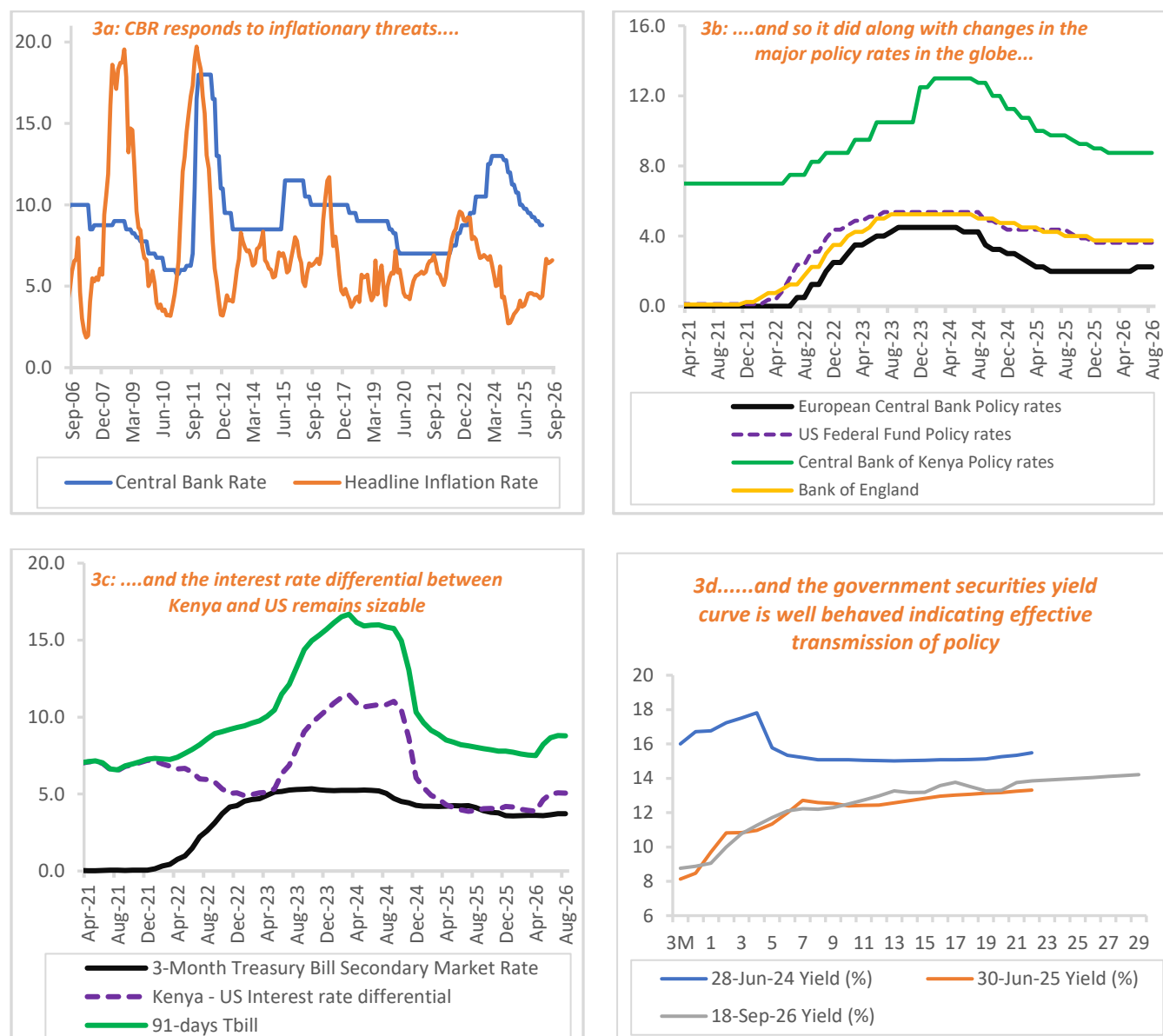
Accordingly, the US Federal Reserve hiked the policy rate to 3.75% – 4.00% in September 2026, and the European Central Bank raised its three key ECB interest rates by 25 basis points to 2.50% for the deposit facility, 2.65% for main refinancing operations and 2.90% for the marginal lending facility, effective September 16, 2026. The rate hikes in advanced economies are mitigative responses to supply-side inflationary pressures. For the near to medium term, the Kenya - US interest rate differential remains sizable

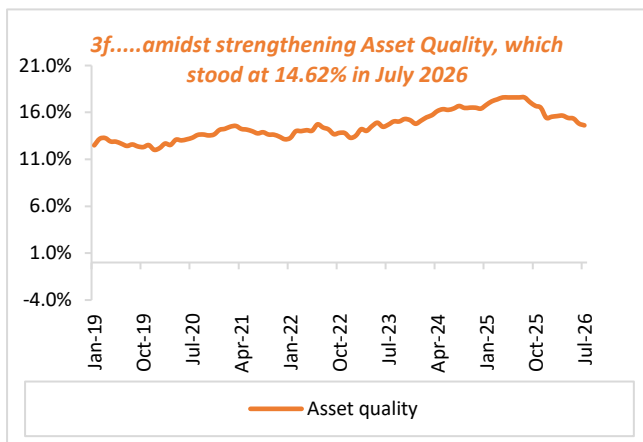
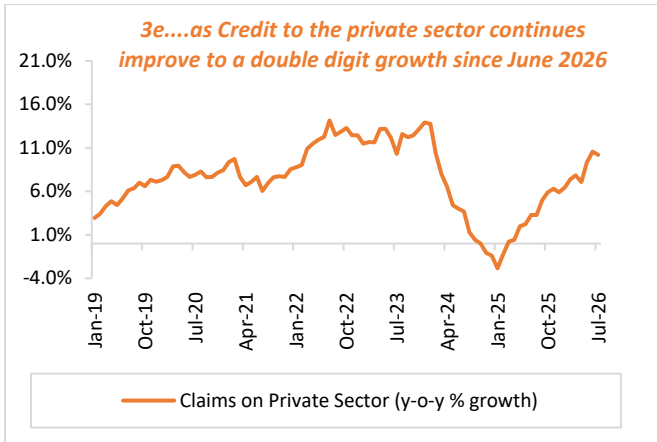
<sup>1</sup> [OECD Economic Outlook report](#), September 2026

(Figure 3c) and expected to support the relative attractiveness of Shilling-denominated assets with the exchange rate remaining stable.

Domestically, Treasury bill yields have declined alongside monetary easing, while the government securities yield curve is well-behaved pointing to lower funding costs and expectations of a less restrictive interest rate environment (Figure 3d). These developments are expected to lower expectations of an increase in funding and benchmark pricing costs, thereby creating scope for lending rates to continue declining in the near term. Consequently, improved affordability of credit should reinforce the recovery in credit growth (Figure 3e), although the pace of transmission will depend on the evolution of credit risk (Figure 3f).

Figure 3: Developments in the Credit Market





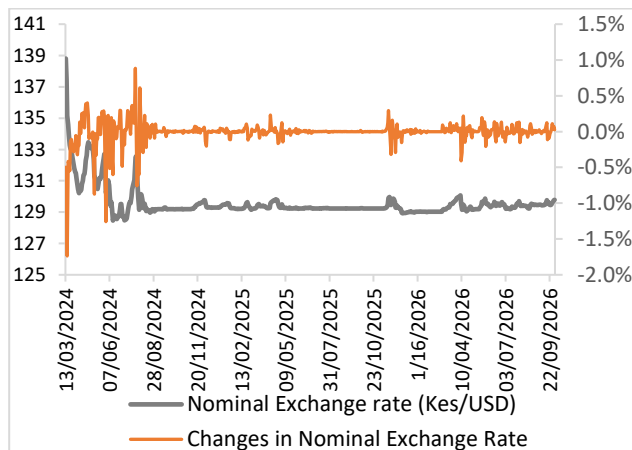
Source: KNBS, Fed Reserve, European Central Bank, Bank of England, NSE and CBK

**Fourth, exchange rate stability continues to provide an important buffer, but protracted oil price pressure increases external-sector risks.** The stability of the Kenya shilling remains an important anchor for the inflation outlook. **Figure 4a** shows that the Kes/USD exchange rate has traded within a relatively narrow range during much of 2025 and 2026. This stability is significant in limiting the extent to which higher international commodity prices are compounded by currency depreciation. This is particularly important for a net oil importing economy such as Kenya, where simultaneous increases in dollar denominated energy prices and depreciation of the shilling would generate considerably stronger imported inflationary pressures.

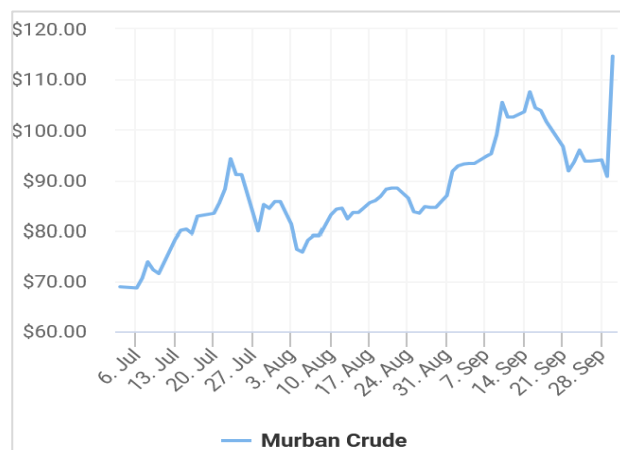
Going forward, while the emerging current account deficit bulge - from USD2.81 billion in August 2025 to USD 4.64 billion in July 2026 on account of the higher import bill - continues to build up fundamental pressure to the exchange rate, the accumulated official foreign exchange reserves sustain the confidence in the economy to manage any volatility in the exchange rate. As of 24<sup>th</sup> September 2026, the country's official foreign exchange reserves had risen to approximately USD15.042 billion, equivalent to 6.1 months of import cover – well above the statutory minimum of 4 months. Additionally, crude oil price movements remain a key risk to the external sector, with Murban crude prices rising sharply in the recent week with considerable volatility (**Figure 4b**) associated with geopolitical developments. Going forward, sustained oil price volatilities will continue to drive the current account deficit given the large share of oil imports in total imports, determine changes in the domestic pump prices and local transport costs, affect firms' production costs and exchange rate stability.

**Figure 4: The external sector developments**

**4a The Kes/USD exchange rate has been stable....**



**4b....and yet the Murban oil prices has risen sharply.**



Source: CBK and Oilprice.com

## Conclusion

Inflation remains well anchored within the target range and faces minimal threats to its escalation in the near term. In this regard, we view that maintaining the current stance of monetary policy in keeping the CBR unchanged at 8.75% would be appropriate to support the ongoing private sector credit growth and sustain economic activity.

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