Kenya

Recent macroeconomic and financial developments

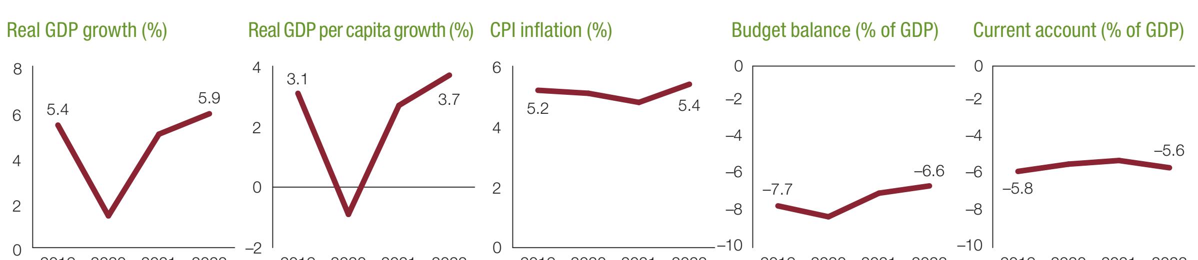
Kenya's economy has been hurt by the COVID–19 pandemic. In 2020, GDP growth is expected to decelerate to 1.4% from 5.4% in 2019. Growth is supported by agriculture, while weaknesses in services and industry have had a dampening effect. Domestic demand is subdued while external demand has neither helped nor hurt growth. Expansionary fiscal, monetary, and financial policy measures were introduced to mitigate the impact of the pandemic on businesses and households. Inflation is expected to ease to 5.1% because of lower aggregate demand. The fiscal deficit is expected to widen to 8.3% of GDP—the result of revenue shortfalls and pandemic-related spending increases to deal with health issues and to mitigate the damage to household income and businesses. The current account deficit is expected to narrow to 5.4% of GDP, supported by a sharp reduction in the oil import bill. Foreign exchange reserves declined to $7.8 billion (4.8 months of import cover) at the end November 2020 from $8.96 billion (5.6 months of import cover) at the end November 2019. The local currency weakened by 8.9% to KSH 110 to the US dollar at the end November 2020 from KSH 101 to the dollar a year earlier. The financial sector was affected by spillover effects from major sectors; the capital market was the hardest hit. The Nairobi Securities Exchange share index fell 20% between 30 September 2019 and September 2020, and market capitalization fell 2% over the same period. The pandemic did serious social damage. Nearly 2 million people are estimated to have fallen into poverty, and nearly 900,000 lost their jobs.

Outlook and risks

The growth outlook is positive. The economy is projected to grow by 5.0% in 2021 and 5.9% in 2022. The rebound assumes that economic activity will normalize due to a full reopening of the economy, the Economic Recovery Strategy being successfully implemented, and Kenya capitalizing on an expected improvement in external liquidity and benefiting from initiatives to meet its external financing needs. The external initiatives could include debt refinancing, restructuring and debt service relief, and additional concessional loans. Inflation is projected to remain within the Central Bank of Kenya's target range of 2.5% to 7.5%, and fiscal and current account deficits are forecast to narrow as a result of improved revenue collection and exports. Downside risks to the outlook could emanate from delays in the full reopening of the economy, failure to secure external financing to execute the budget, a slowdown in global growth, and disruptive social conditions during the run-up to the 2022 elections.

Financing issues and options

Public debt surged to 72% of GDP in 2020 from 61% in 2019, driven mainly by public investment in infrastructure, debt management–related challenges, and the COVID–19 crisis. Kenya is now in high risk of debt distress as determined by the International Monetary Fund. Addressing the emerging fiscal and debt vulnerability risks would require growth friendly reforms, soliciting external financial assistance, concessional credit, and debt refinancing and restructuring. The growth–friendly reforms could entail revenue-related steps to improve tax compliance, widening the tax net by reviewing the list of tax-exempt and zero-rated items, formalizing the informal sector, ensuring that public expenditures reach their intended targets, and deepening the domestic financial market to support private and public sector credit growth.



Source: Data are as of December 2020 and are from domestic authorities; figures for 2020 are estimates and figures for 2021 and 2022 are projections by the African Economic Outlook team. Data on the budget balance correspond to Kenya's fiscal year, which runs from July 1 to June 30.