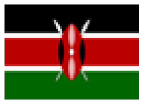
Euler Hermes Economic Research

Country Report

Kenya

Large twin deficits but strong GDP growth trajectory



General Information

GDP	USD60.94bn (World ranking 74, World Bank 2014)
Population	45.55mn (World ranking 30, World Bank 2014)
Form of state	Republic
Head of government	Uhuru Kenyatta
Next elections	2018, presidential and legislative

Strengths

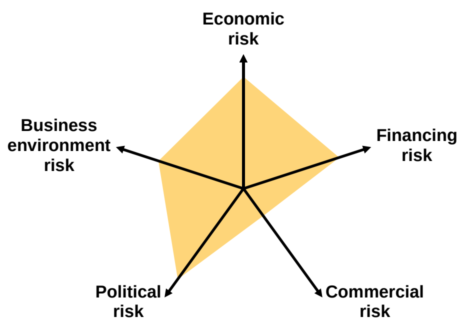
- Large domestic market (population 45mn and member of a regional trading bloc, East African Community, which is expanding and offering good business opportunities.
- Vibrant horticultural and tourism sectors, although the latter is volatile, subject to domestic political stability and regional security concerns.
- Regional energy sector has significant potential (including offshore gas fields), with direct (exploitable reserves within Kenya's territory) and indirect (inputs through Kenyan ports and exports from them) benefits.
- Strategic importance: regional economic hub.

Weaknesses

- Poor record in terms of political party and individual rivalries and ethnic, tribal and religious divides, which spilled over into violence in 2008. Despite a relatively successful election process in March 2013, these fault lines remain in place.
- Regional uncertainties (including Somalia, piracy and terrorist activity).
- Classified as a lower-middle income economy by the World Bank, with associated need to maintain aid and other external assistance flows.
- Chequered relationship with the IFIs and wider donor community, partly reflecting perceptions of corruption.
- Twin deficits in fiscal and current accounts.

Country Rating

C2



Source: Euler Hermes

Trade Structure

By destination/origin (% of total)

Exports		Rank		Imports
Uganda	14%	1	14%	India
United Republic of Tanzania	9%	2	12%	China
United Kingdom	8%	3	11%	United Arab Emirates
Netherlands	6%	4	5%	Saudi Arabia
United Arab Emirates	6%	5	5%	United States

By product (% of total)

Exports		Rank		Imports
Coffee, tea, cocoa, spices, and manufactures thereof	25%	1	26%	Petroleum, petroleum products and related materials
Crude animal and vegetable materials,	10%	2	7%	Road vehicles
Vegetables and fruits	8%	3	6%	Cereals and cereal preparations
Petroleum, petroleum products and related materials	5%	4	4%	Iron and steel
Articles of apparel & clothing accessories	4%	5	4%	Textile yarn and related products

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General Overview

The IMF is broadly supportive of the government's use of policy tools and its reform agenda to stabilise the economy. Indeed, in March 2016, the Fund approved USD1.5bn in fresh financing, with the funds made available through a stand-by arrangement (SBA) of around USD989.8mn and a stand-by credit facility (SCF) of around USD494.9mn. Financing under both arrangements is for a 24-month period. Kenya has immediate access to around USD757.5mn, with the remaining funds to be disbursed in four tranches following semi-annual programme reviews by the IMF. However, the Kenyan authorities will see the facility as essentially a "precautionary" measure, rather than a fund to be drawn down.

Fiscal consolidation plan will not upset the current high GDP growth trajectory

Also in March 2016, the Treasury announced supplementary spending plans that introduce net cuts to the budget of around -USD404.34mn. However, the government claims that fiscal plans will not interrupt the nation's "still strong" economic growth, driven by expansion in the construction and agricultural sectors and by a recovery in tourism. EH expects GDP growth of around +6% in both 2016 and 2017, compared with an annual average +5.4% in the ten-year period to end-2015. Kenya will remain one of the faster growing economies in Sub-Saharan Africa (see chart).

The current account registers high deficits but external debt is comfortable

Euler Hermes expects the East African Community (EAC) will grow in importance for Kenya as regional integration deepens, particularly as Mombassa remains the largest regional port and Uganda and Tanzania already account for a combined 23% of Kenyan exports. However, in addition to large fiscal deficits, a further structural imbalance occurs in the external accounts. Large shortfalls in the current account balance (see chart) reflect the economy's vulnerability to local (climatic and security) and global developments. The latter include commodity demand and internationally-determined commodity prices, which have an impact on both sides of the trade balance as Kenya exports soft commodities but is an importer of crude oil.

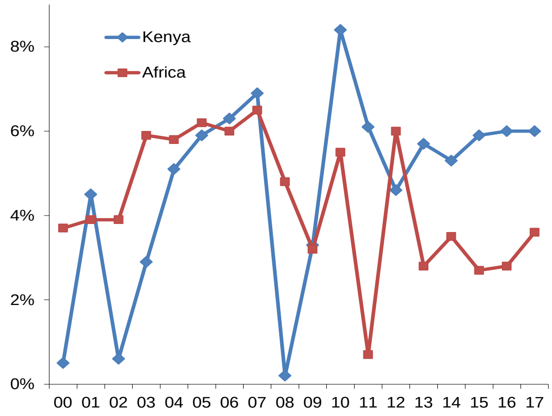
External debt levels (debt/GDP is around 25% and debt/export earnings 119%) also require careful management, although servicing of external debt obligations is low (debt service/export earnings around 4%) and foreign exchange reserves cover between four and five months of imports.

Key Economic Forecasts

	2014	2015	2016f	2017f
GDP growth (% change)	5.3	5.9	6.0	6.0
Inflation (%, end-year)	6.0	7.0	8.5	7.0
Fiscal balance (% of GDP)	-5.3	-6.5	-6.0	-5.5
Public debt (% of GDP)	48.6	50.5	52.0	52.5
Current account (% of GDP)	-10.3	-8.9	-7.0	-7.0
External debt (% of GDP)	24.1	24.2	25.0	23.5

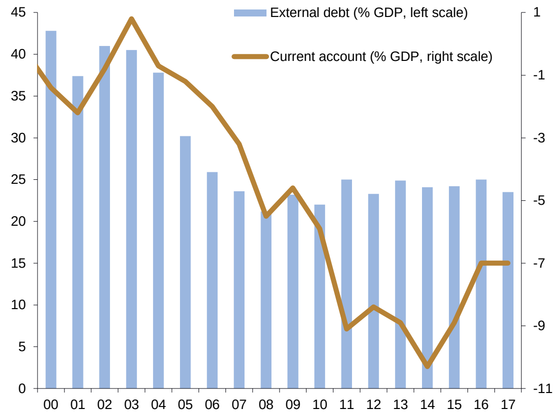
Sources: National Sources, IHS, Euler Hermes

GDP Growth (%)



Sources: National sources, IHS, Euler Hermes

Current Account Balance and External Debt (% of GDP)



Sources: National sources, IHS, Euler Hermes

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