RECENT ECONOMIC DEVELOPMENTS AND MACROECONOMIC OUTLOOK: FY 2021/22-FY 2023/24 MEDIUM TERM BUDGET

Presentation During the Launch of Sector Working Groups

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PRESENTATION OUTLINE

1. Background and Global and Domestic Economic Outlook
2. Fiscal Performance and Outlook
3. Policy Priorities - “The Big Four” Agenda
4. Macroeconomic Outlook
5. Support Measures against adverse effects of COVID-19 Pandemic
6. Potential Risks to the Macroeconomic Outlook

1a. Background

- FY 2021/22 - FY 2023/24 medium term budget is set against outbreak and the rapid spread of the COVID-19 Pandemic
- The Pandemic and the attendant containment measures has led to contraction of the global economy and disrupting businesses including international trade
- On the domestic scene, the Pandemic and the containment measures have not only disrupted our livelihoods, but to a greater extent business and reduction in government revenue
- To stimulate economic recovery, the Government has implemented a range of fiscal measures, introduced an 8-Point Economic Stimulus Programme (ESP) and is also finalizing the development of a Post COVID-19 Economic Recovery Strategy
- Growth outlook will also be supported by the stable macroeconomic environment, investments in the strategic areas under the “Big Four” agenda, the ongoing public investments in infrastructure projects

1a. Background Cont…

- Leading economic indicators for the second quarter point to continued strong performance in agriculture, mainly due to favorable weather conditions and lifting of restrictions in the key export markets.

- The performance of the manufacturing sector shows a recovery in June 2020 from a contraction in the previous months. This is reflected by improved performance in cement production, total electricity generation and agro-processing.

- The Information and communication Sector has supported all other sectors of the economy during this pandemic period. The sector is expected to perform better on account of increased digital communication to hold meetings, enhanced minutes of talk time and increased digital transfers on Account of COVID-19 pandemic.

- The construction sector has generally declined in the second quarter of 2020, but improvement has been observed in cement consumption in May 2020 and June 2020 compared to April 2020

- The transport and storage, accommodation and restaurant sectors were more affected by the lockdown and curfew in the second quarter of 2020, but the sectors are expected to improve in the third quarter as a result of removal of border restrictions and commencement of local and international flights

1a. Background Cont…

- **Roll out of the Post Covid-19 Economic Recovery Strategy initiatives**

i. Macroeconomic policy framework;

ii. Resource mobilization.

iii. Enhancing the role of private sector in funding development;

iv. Supporting micro, small and medium enterprises;

v. Implementation of the economic stimulus programme (ESP);

vi. Investing in ICT and digital infrastructure development;

vii. Development of local production and value chains;

viii. Enhanced disaster and risk management;

ix. Social protection; and

x. Monitoring and evaluation (M&E) systems.

1b. Global growth is projected to contract by 4.9% in 2020 from an estimated growth of 2.9% in 2019 due to the COVID-19 pandemic and the attendant containment measures

Economy	2019	2020*	2021**
World	2.9	(4.9)	5.4
Advanced Economies	1.7	(8.0)	4.8
Of which: USA	2.3	(8.0)	4.5
Emerging and Developing Economies	3.7	(3.0)	5.9
Of which: China	6.1	1.0	8.2
India	4.2	(4.5)	6.0
Sub-Saharan Africa	3.1	(3.2)	3.4
Of which: South Africa	0.2	(8.0)	3.5
Nigeria	2.2	(5.4)	2.6
EAC-5	5.7	1.0	3.7
Of which: Kenya	5.4	2.6	5.3

** Estimate   ** Projected*

EAC-5: Burundi, Kenya, Rwanda, Tanzania and Uganda

1c. Global Growth is projected to rebound strongly in 2021 to grow at 5.4% supported by recovery of activities in all the economies

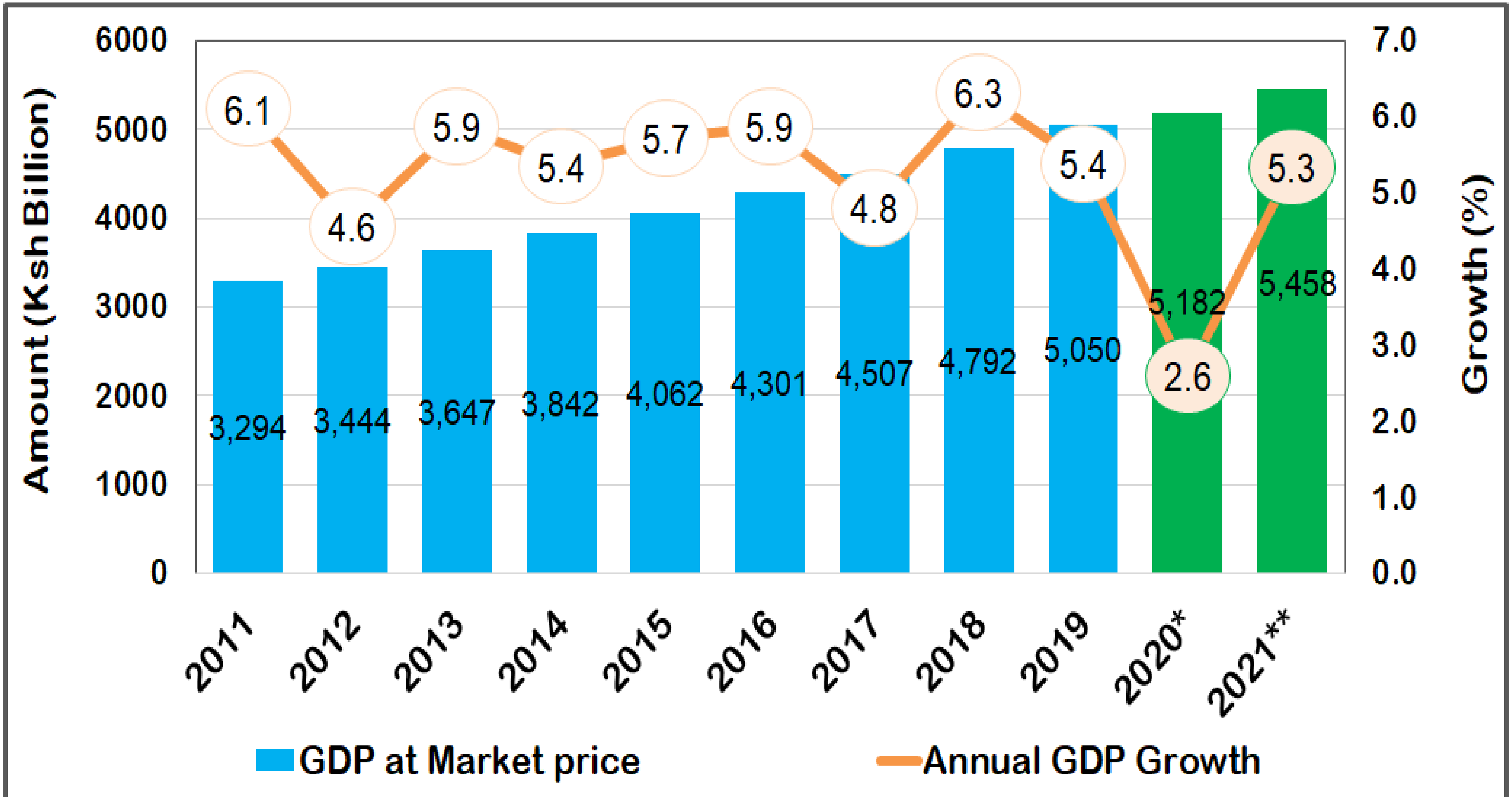
- ❑ **Advanced economies'** growth expected to slow down to -8.0% in 2020 and recover to 4.8% in 2021.

- ❑ **Emerging economies** are estimated to contract by 3.0% in 2020, occasioned by the COVID-19 pandemic, severe external demand shocks, tightening conditions in the global financial markets and significant decline in commodity prices. These economies are expected to bounce back in 2021 to grow by 5.9%.

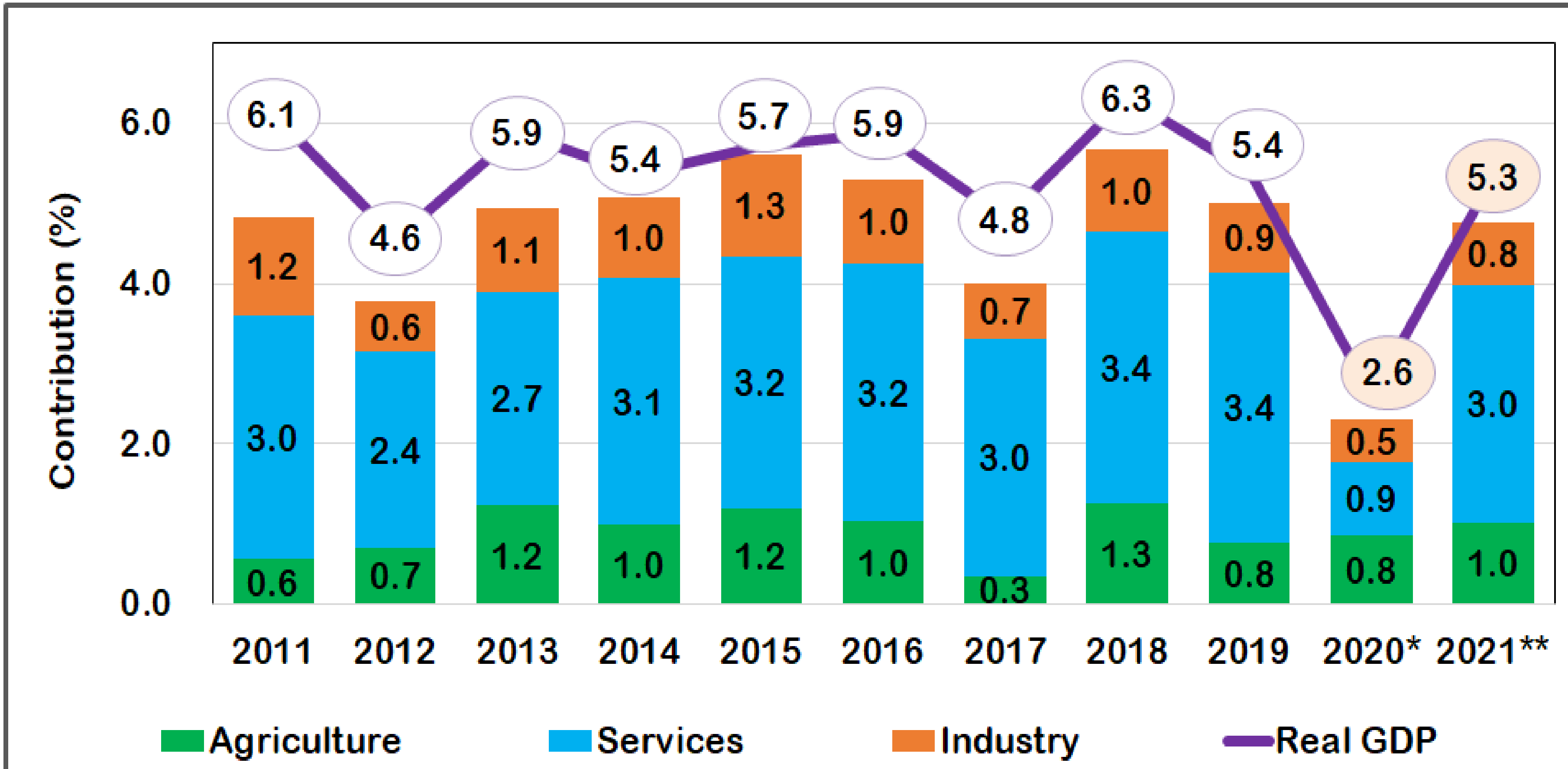
- ❑ Like the rest of the world, COVID-19 poses a new blow to Africa's economies. **Sub-Saharan Africa** is projected to contract by 3.2% in 2020 and recover in 2021 to grow at 3.4%.

- ❑ The rebound in 2021 depends critically on the pandemic fading in the second half of 2020, allowing containment efforts to be gradually scaled back and restoring consumer and investor confidence.

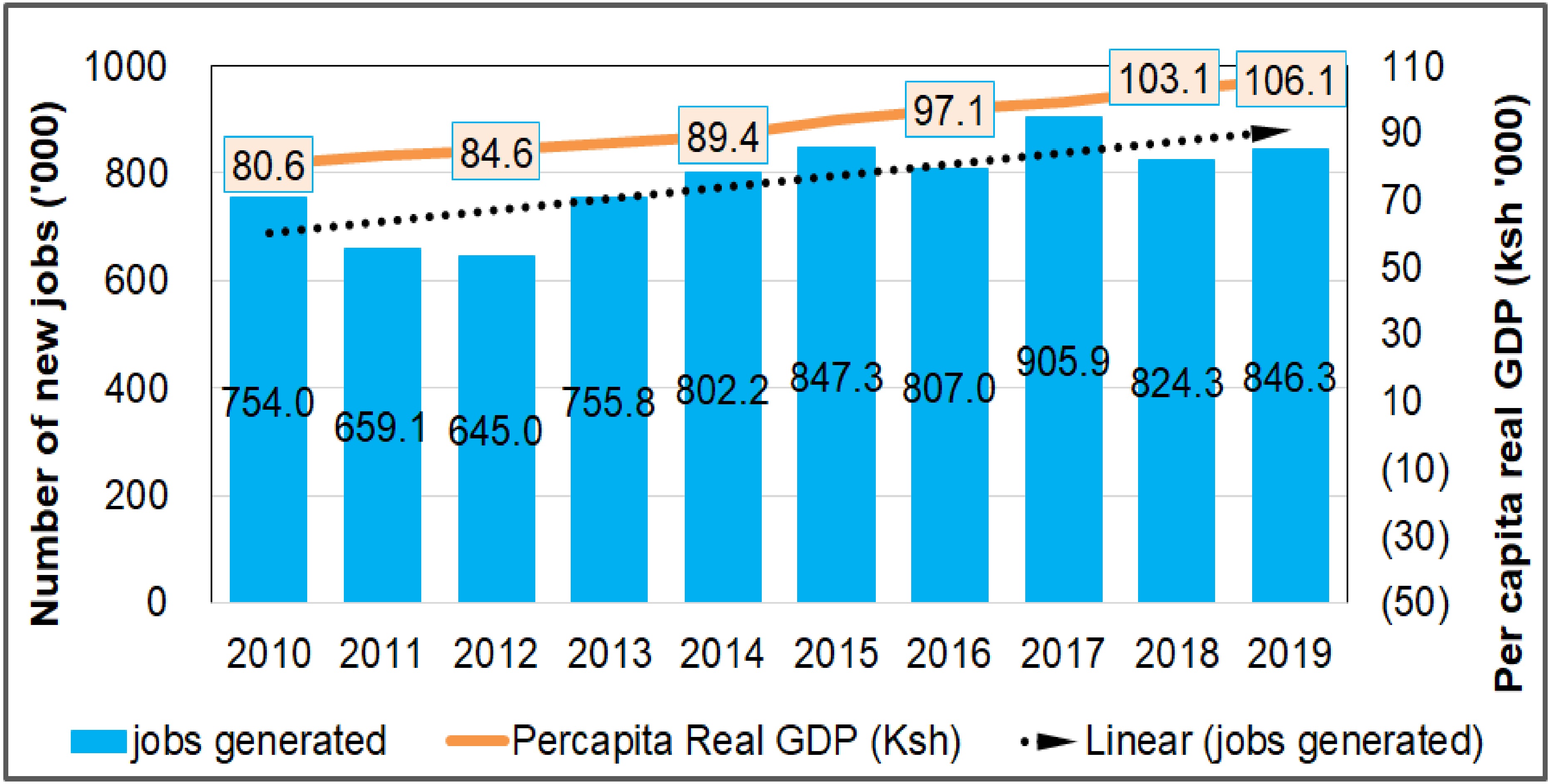
1d. Prior to the outbreak of COVID-19 Pandemic, Kenya's economy was strong expanding by 5.4% in 2019. Growth is projected to decline to 2.6% in 2020 due to the adverse impact of COVID-19 but rebound to 5.3% of GDP in 2021



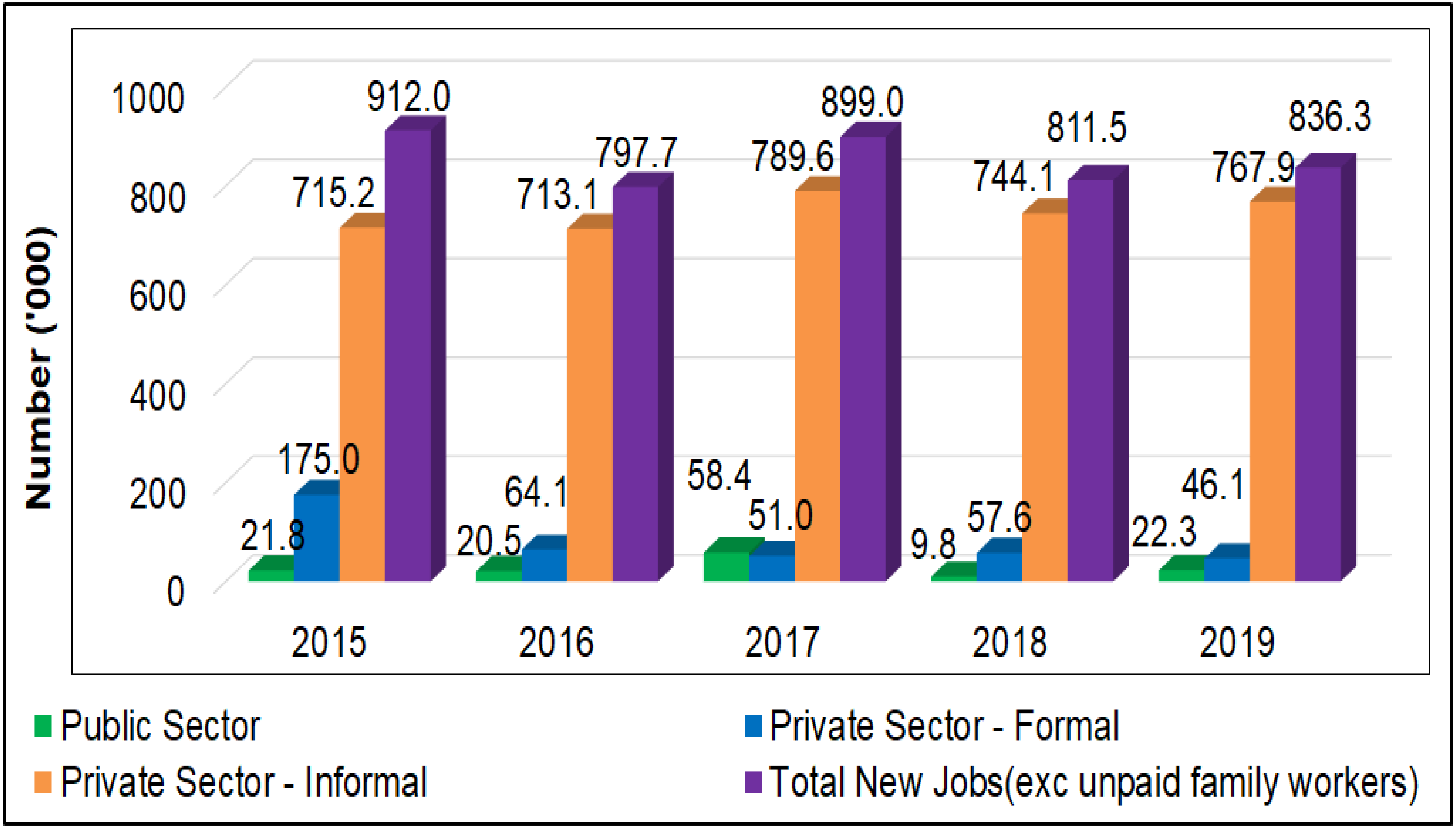
1e. Agricultural sector is expected to support growth in 2020 and 2021 as a result of the prevailing favorable weather conditions. The Services and Industry sectors contribution to Real GDP growth is estimated to decline in 2020 on account of the negative effects of COVID-19 pandemic and increase in 2020



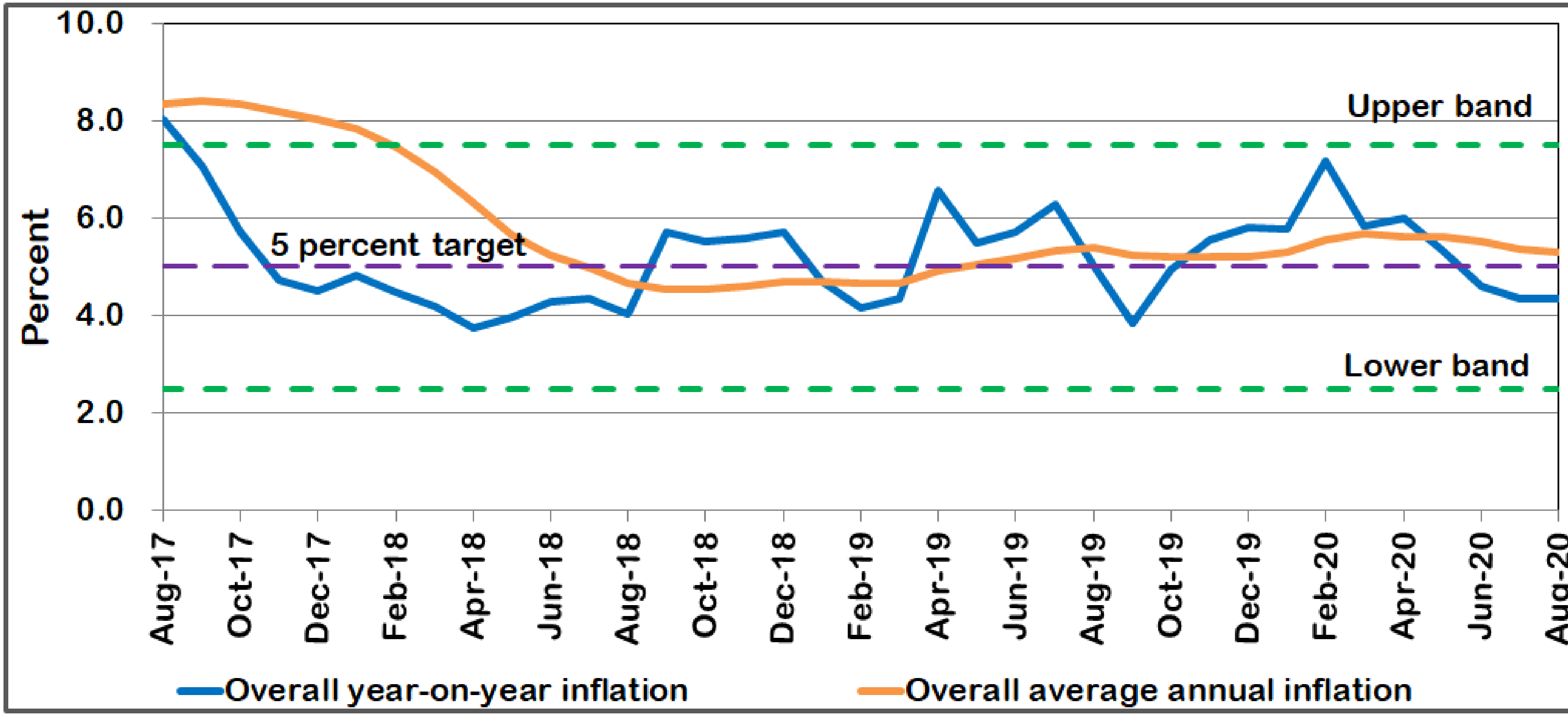
1f(i). In 2019, Per capita income improved from Ksh 103,057 in 2018 to Ksh 106,096 which stimulated job creation by 846,300. Job creation expected to decline in 2020 due to disruption in economic activities especially in the service sector by COVID-19 pandemic



1f(ii). Informal private sector contributes the lion's share of the jobs (at 767,900 in 2019). New Jobs which are created in both formal private and public sector are generally low

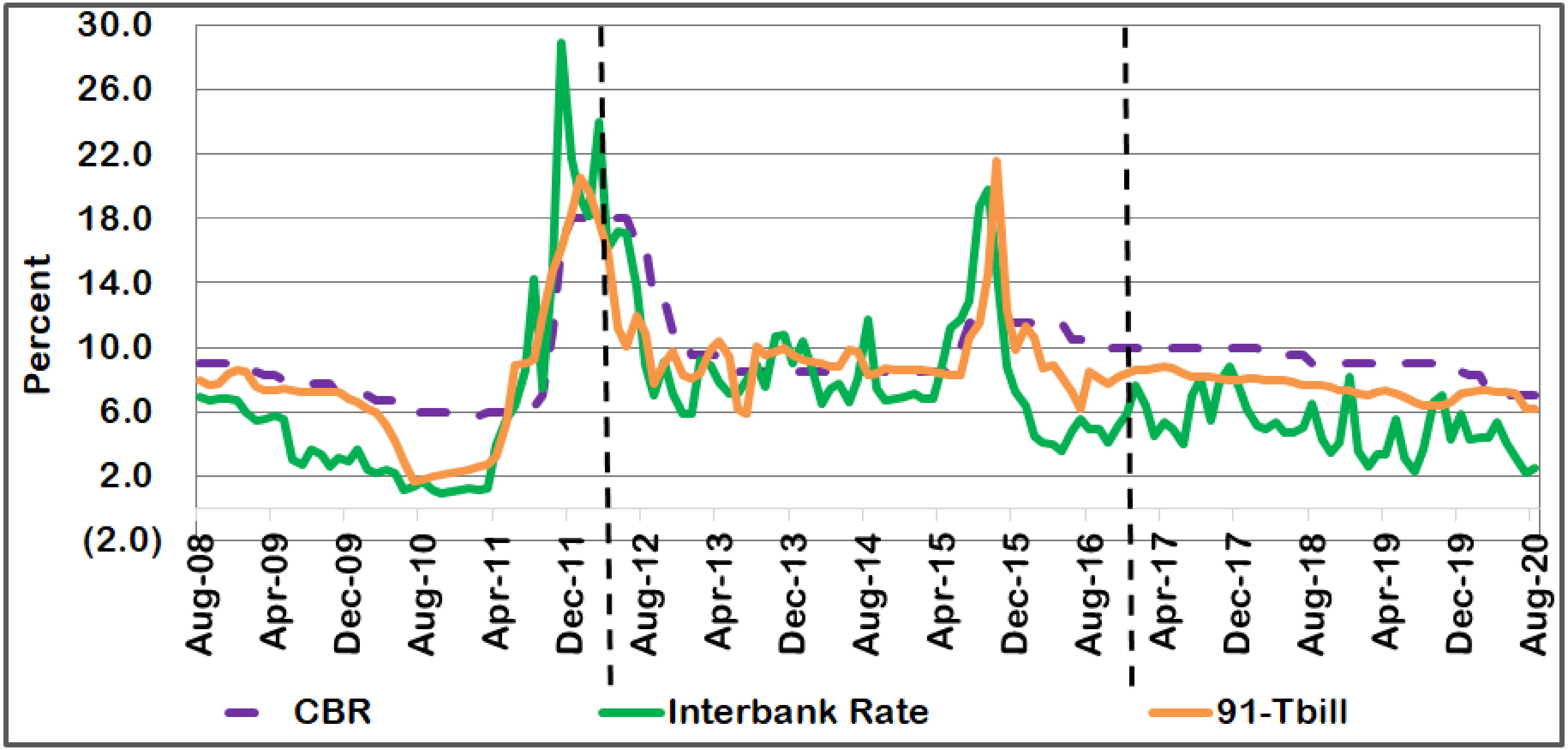


1g. Inflation has largely been within the government target range of 5+/-2.5% since February 2018. Year on year inflation was 4.36% in August 2020 down from 5.0% in August 2019.



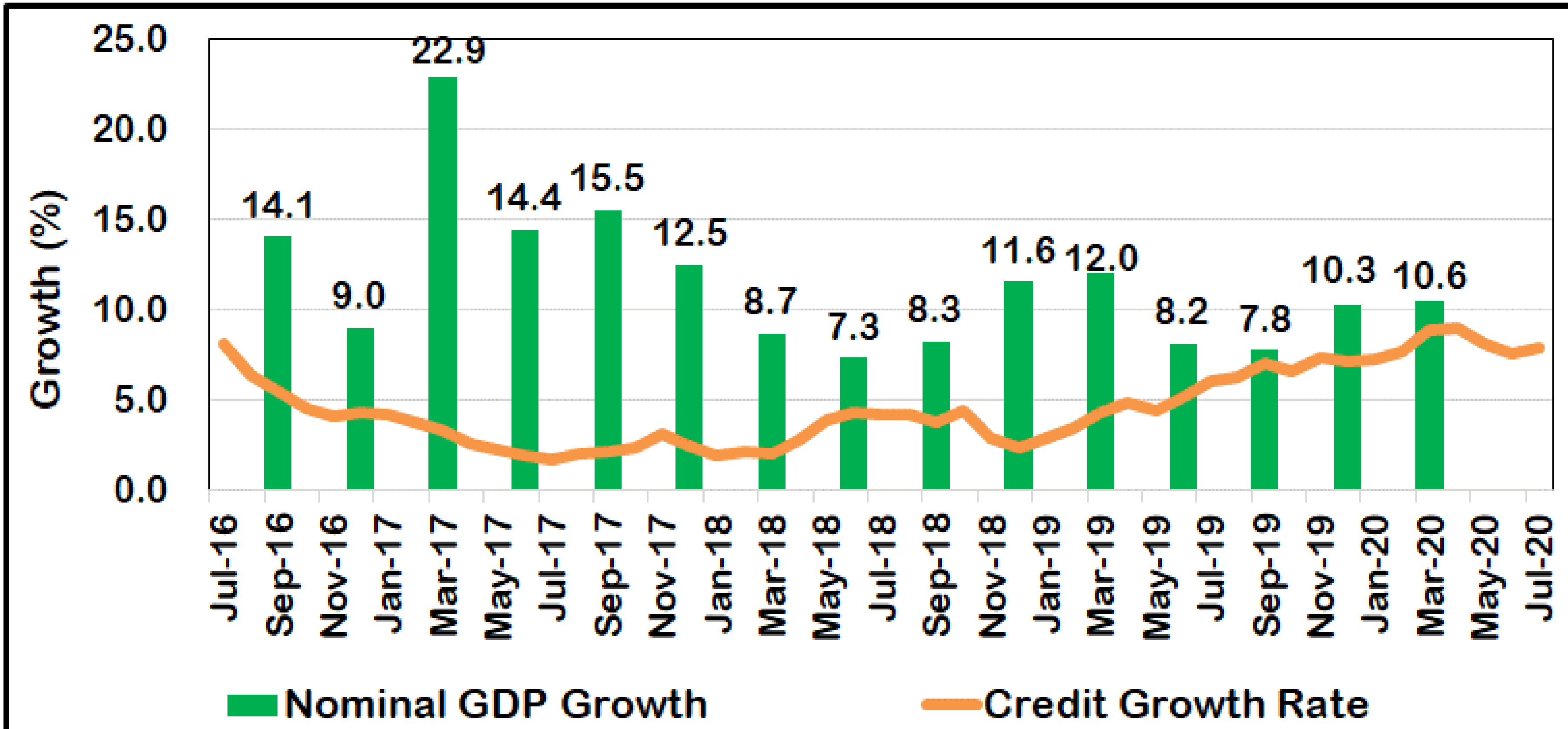
- The decline was mainly supported by increased food supply due to favorable weather condition, impact of reduction in VAT and muted demand pressure in the economy arising from prudent monetary policies.

1h. Interest rates have been fairly low and stable (below 10% from 2016), due to prudent monetary and fiscal stance



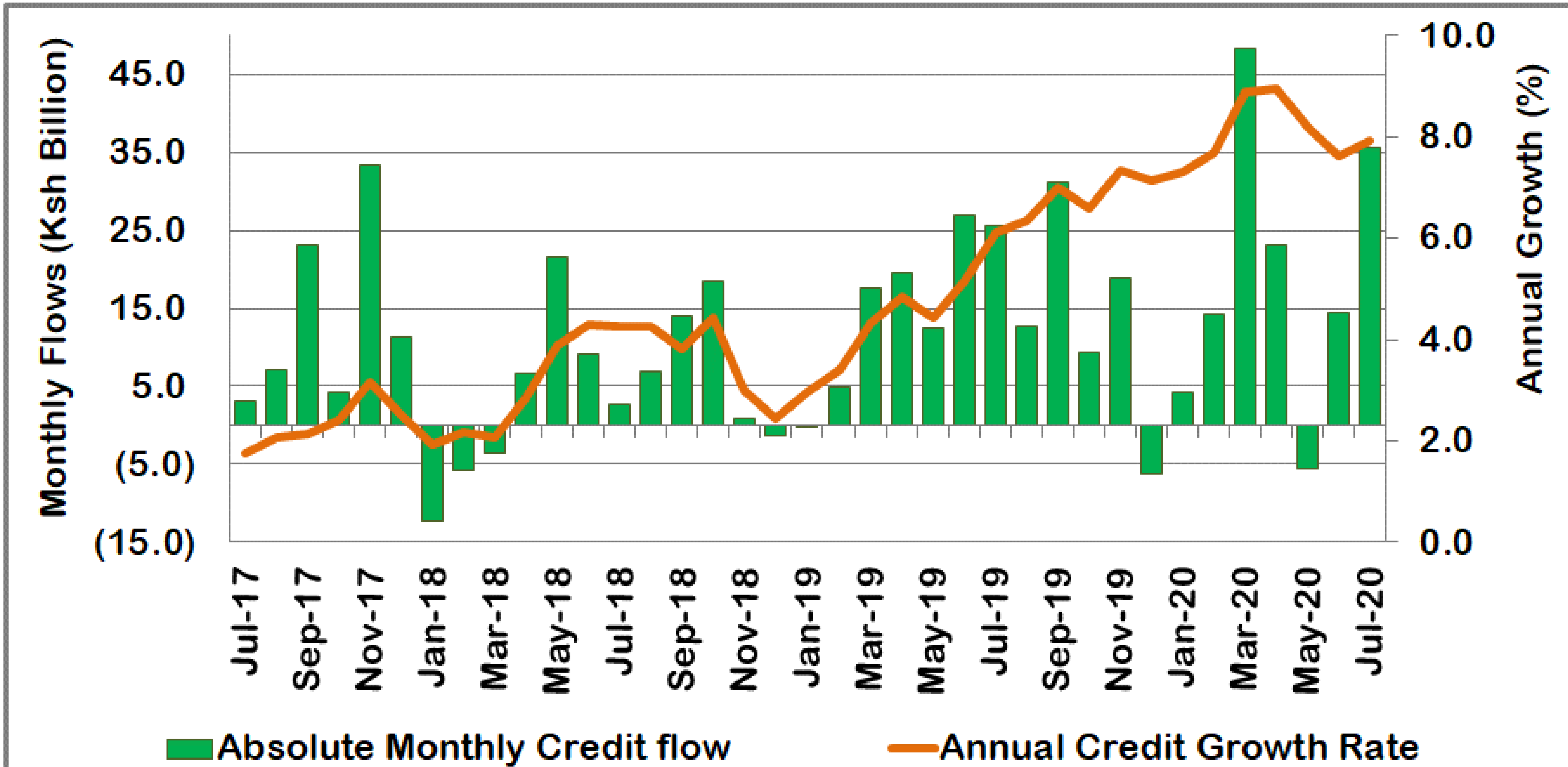
- ❑ **The CBR was retained at 7.0%** in July 2020 to maintain lower lending rates that will support credit access by borrowers especially the SMEs distressed by COVID-19 pandemic
- ❑ **Interbank rate has generally been low at 2.5% in August 2020** from 3.6% in August 2019 due to enhanced liquidity in money market

1i. Credit to private sector has generally been slower than Quarterly growth in nominal GDP since 2016. Since the repeal of interest rate caps, the gap has been closing despite challenges related to COVID-19

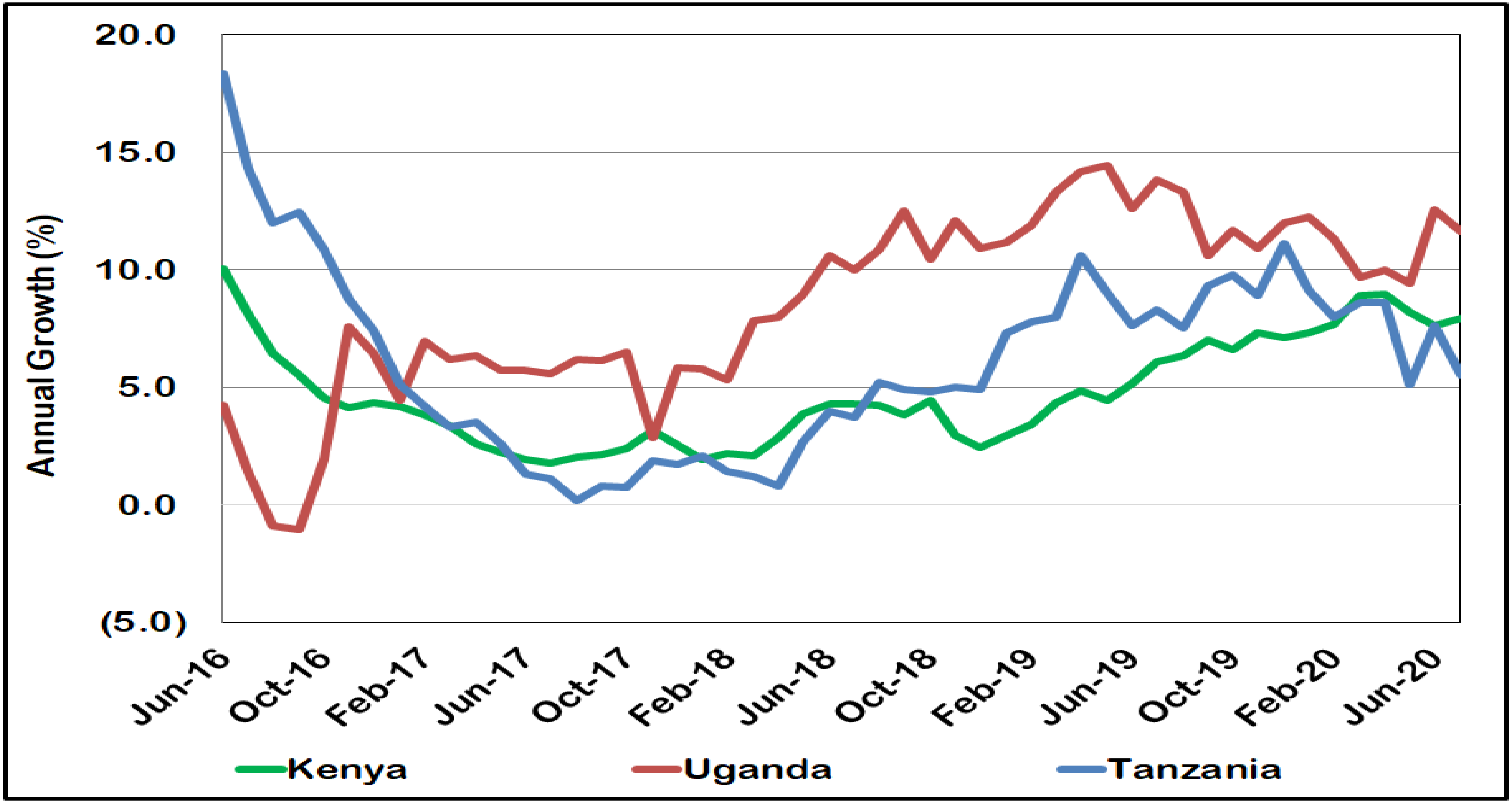


- ❑ Credit stock to private sector grew by 7.9% in June 2019 and expected to improve further by the end of the year.

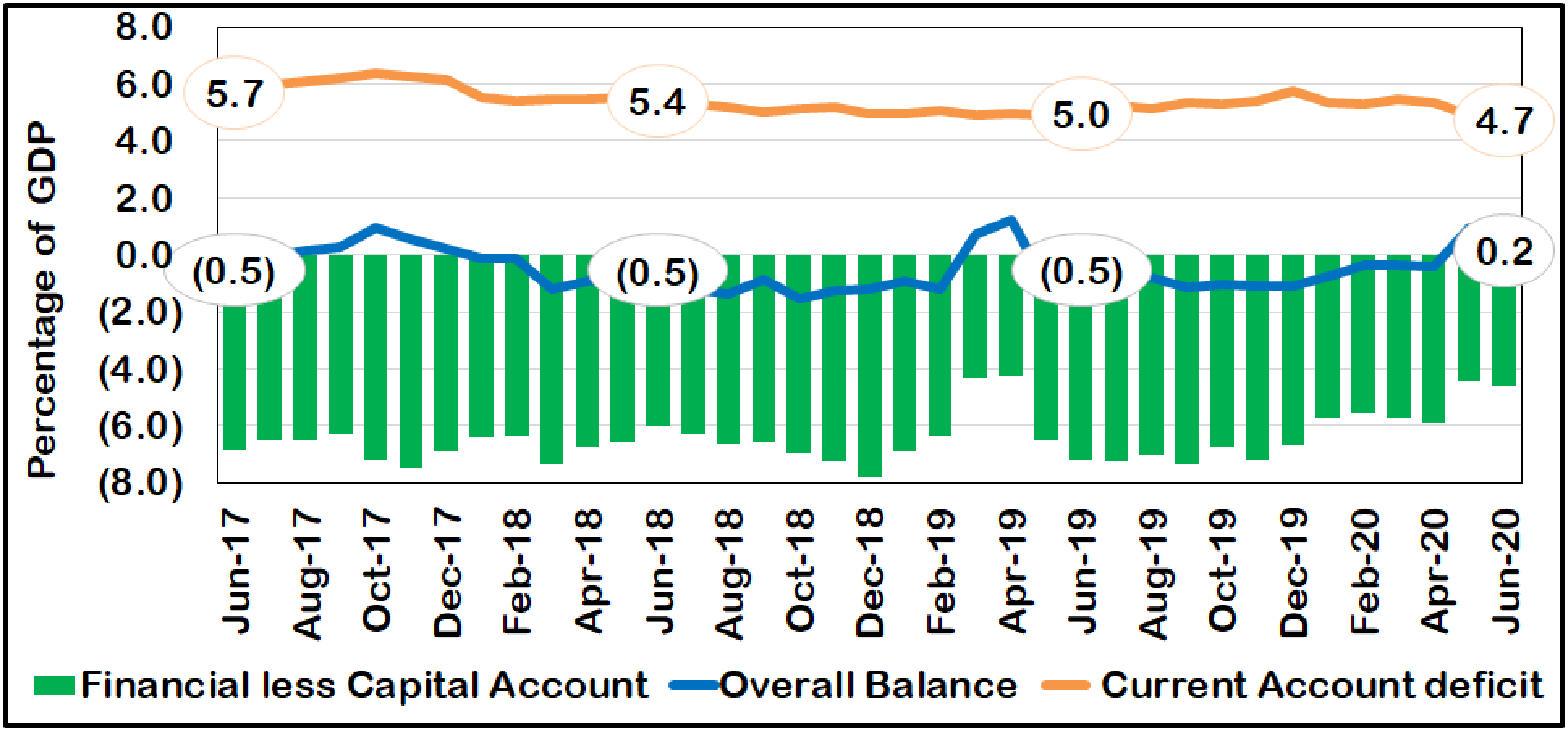
1j. Growth in credit advanced to private sector has been on an upward trend since December 2018. Net credit flow for July 2020 was Ksh 35.7 billion. Net credit flow in the 7 months to July 2020 amounted to Ksh19.2 billion compared Ksh 15.2 billion over same period in 2019



1k Similar trend in credit growth also observed in Tanzania and Uganda. Private sector credit in Kenya has been growing faster compared to Tanzania since November 2019.

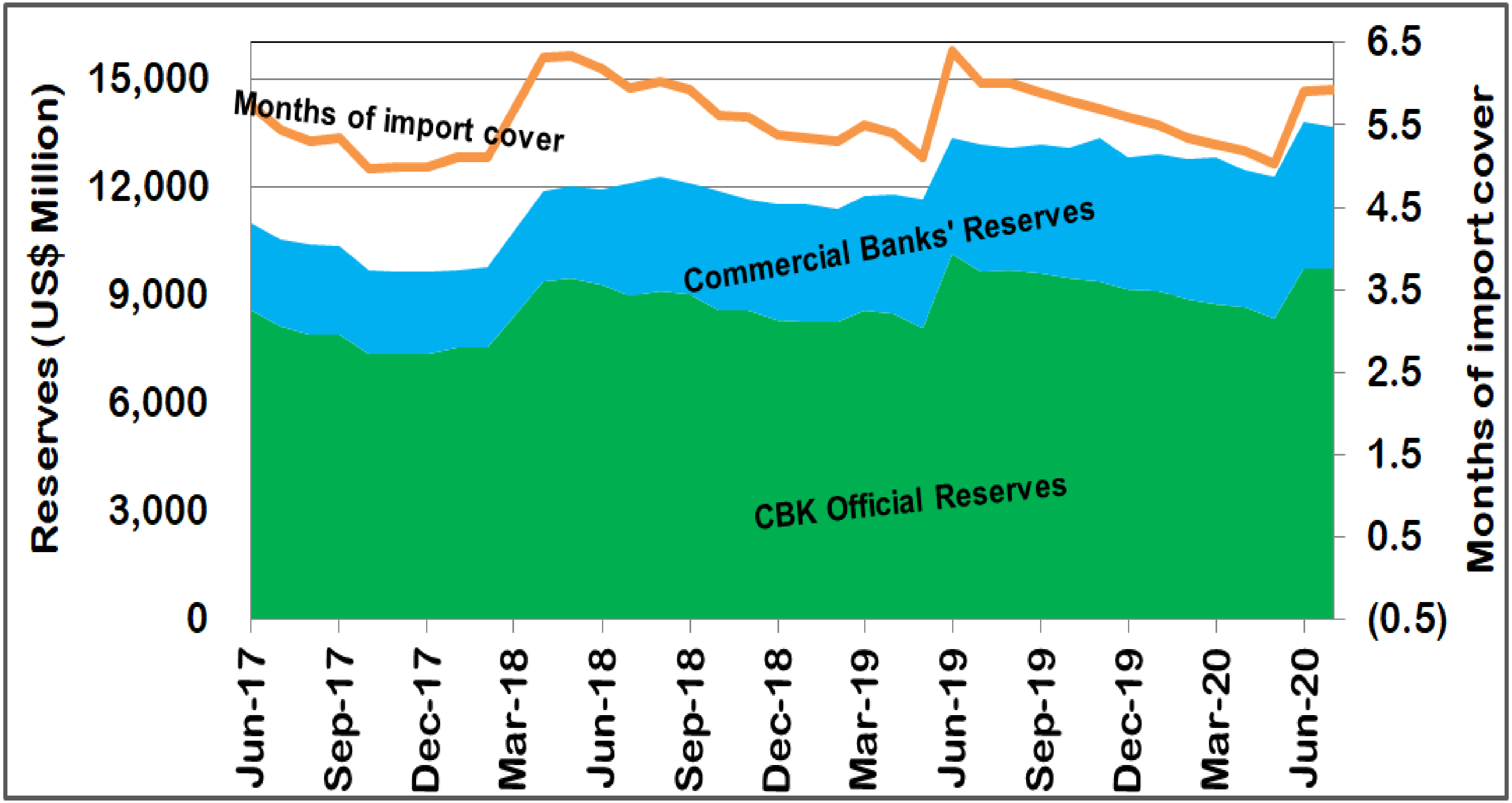


1I. Overall Balance of Payments has improved from a deficit of 0.5% of GDP in June 2019 to a surplus of 0.2% of GDP in June 2020 mainly due to an improvement in the current account



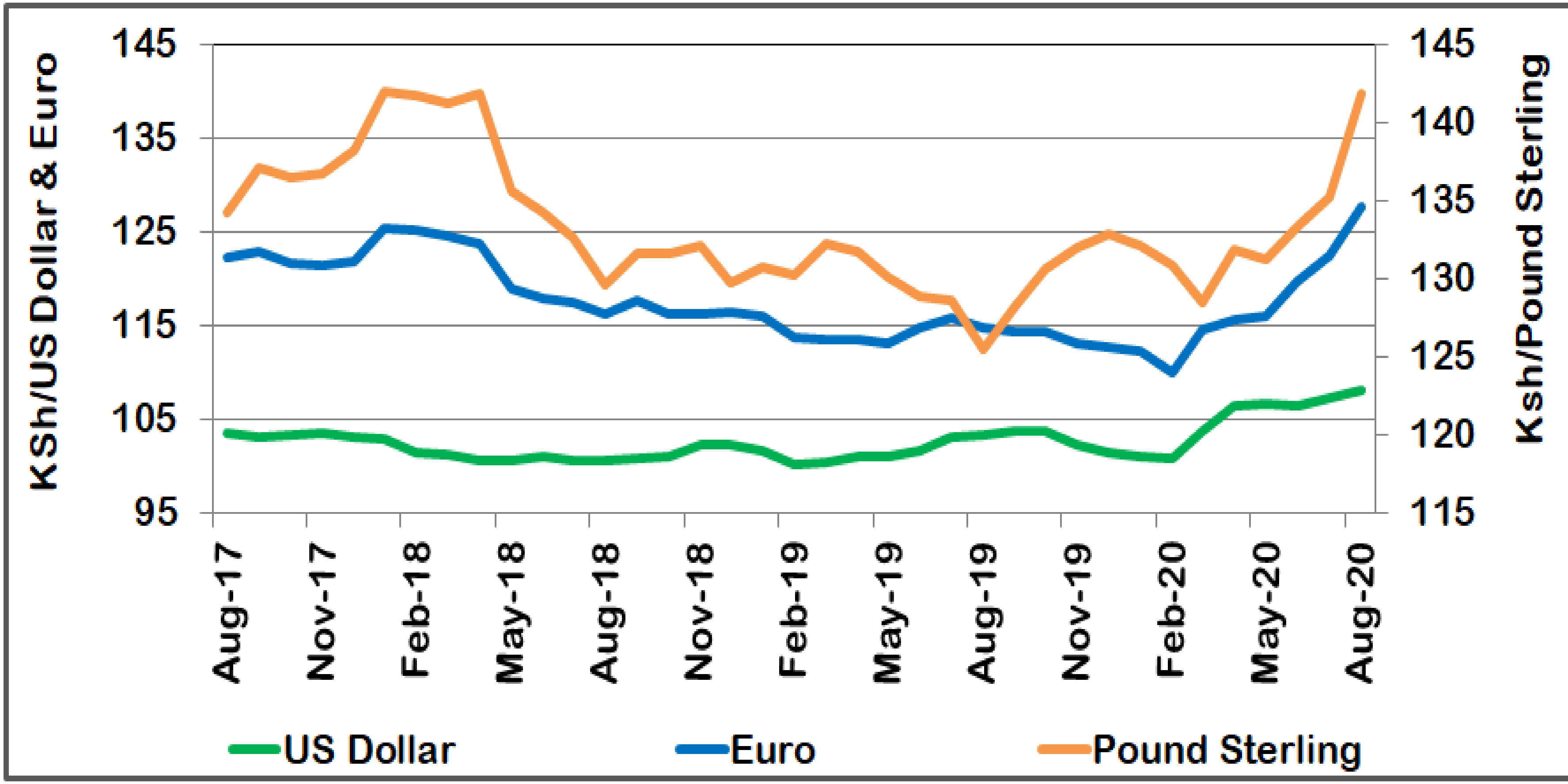
- The current account improved to a deficit of **4.7% of GDP in June 2020** from a deficit 5.0% of GDP in June 2019

1m. Official foreign exchange reserves held by CBK remained strong at 5.9 months of import cover in June 2020 compared to 6.0 months of import cover in June 2019



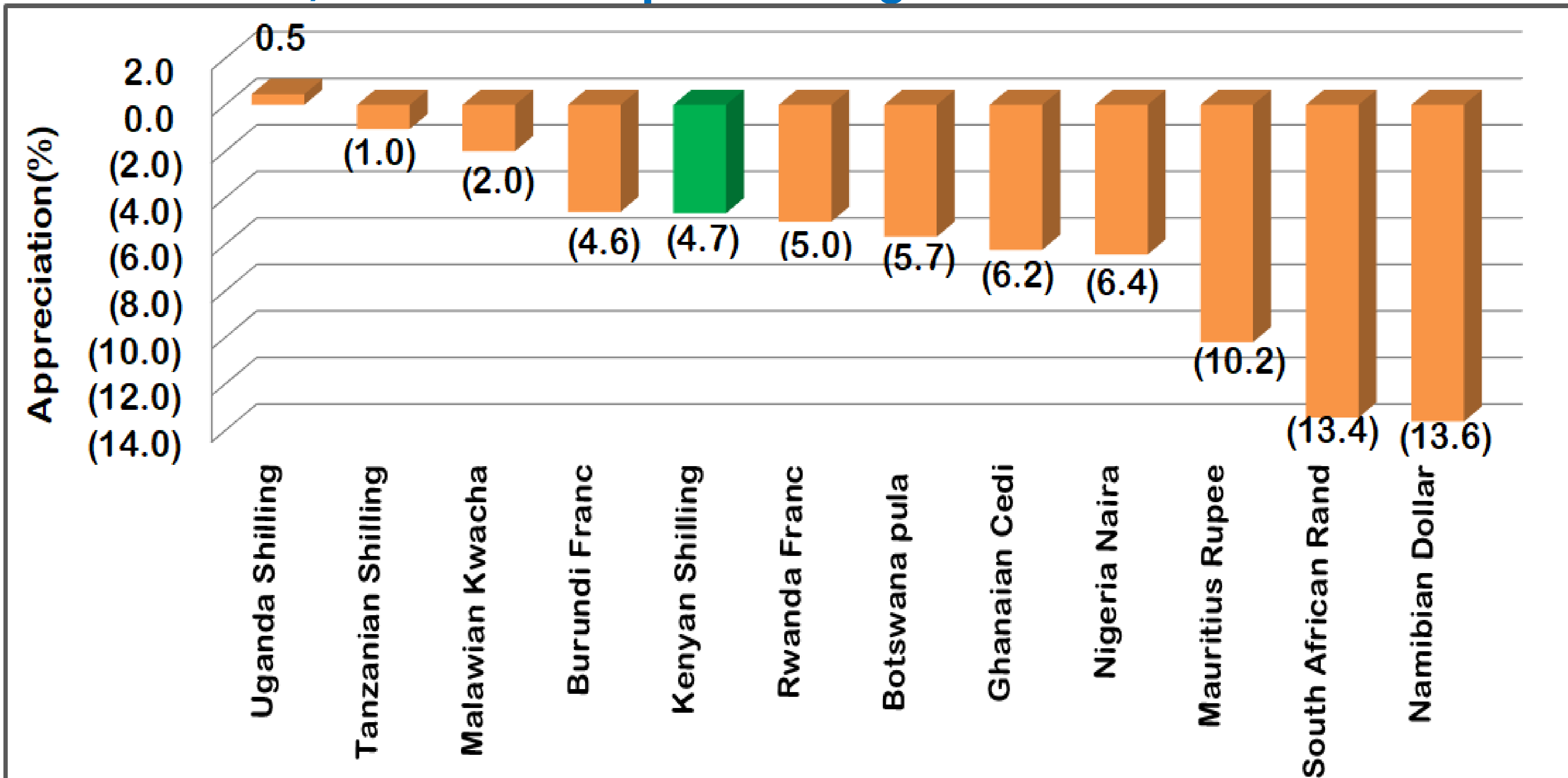
- By June 2020, the usable official reserves stood at **US$ 9,739.9 million** compared to **US$ 9655.9 million** in June 2019.

1n.The foreign exchange market has experienced some volatility in 2020 largely due to uncertainties caused by COVID-19 pandemic and a significant strengthening of the US Dollar in the global markets



- ❑ The Shilling depreciated against the US Dollar, the Euro and the Sterling Pound in august 2020

1o. Kenya Shilling continues to record less volatility compared to majority of other currencies such as the Ghanaian Cedi, South African rand, Mauritius Rupee among others



- The shilling weakened by 4.7% in August 2020 on account of a decline in exports as a result of closure of borders by world economies due to the COVID-19 pandemic

1p. Kenya continues to be ranked favorably in the ease of doing business and as a top investment destination.

Kenya Steps up in Ease of Doing Business

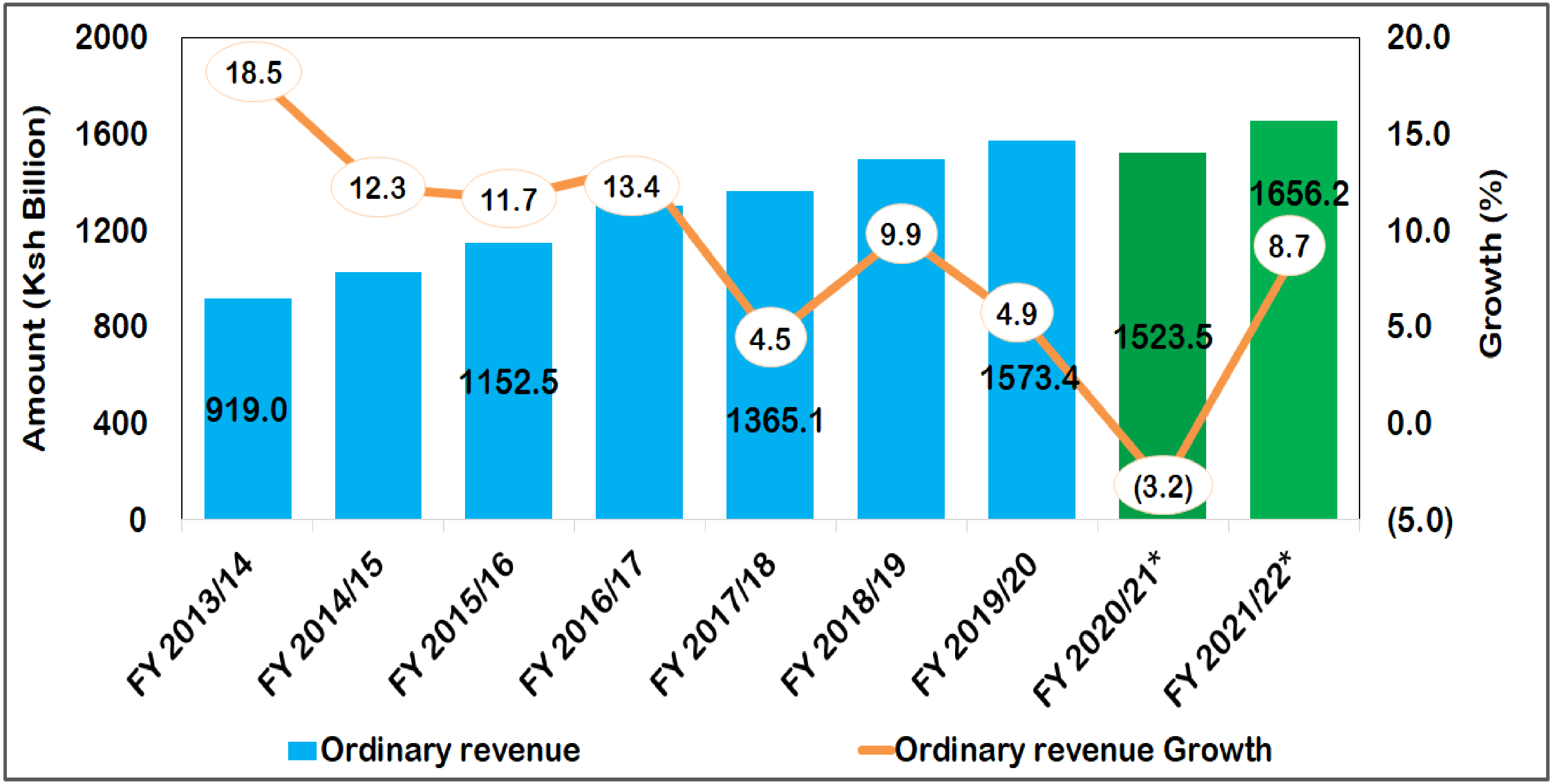
Out of 190 countries (Rank 1 is the highest)

Year	Rank
2019	56
2017	80
2015	129

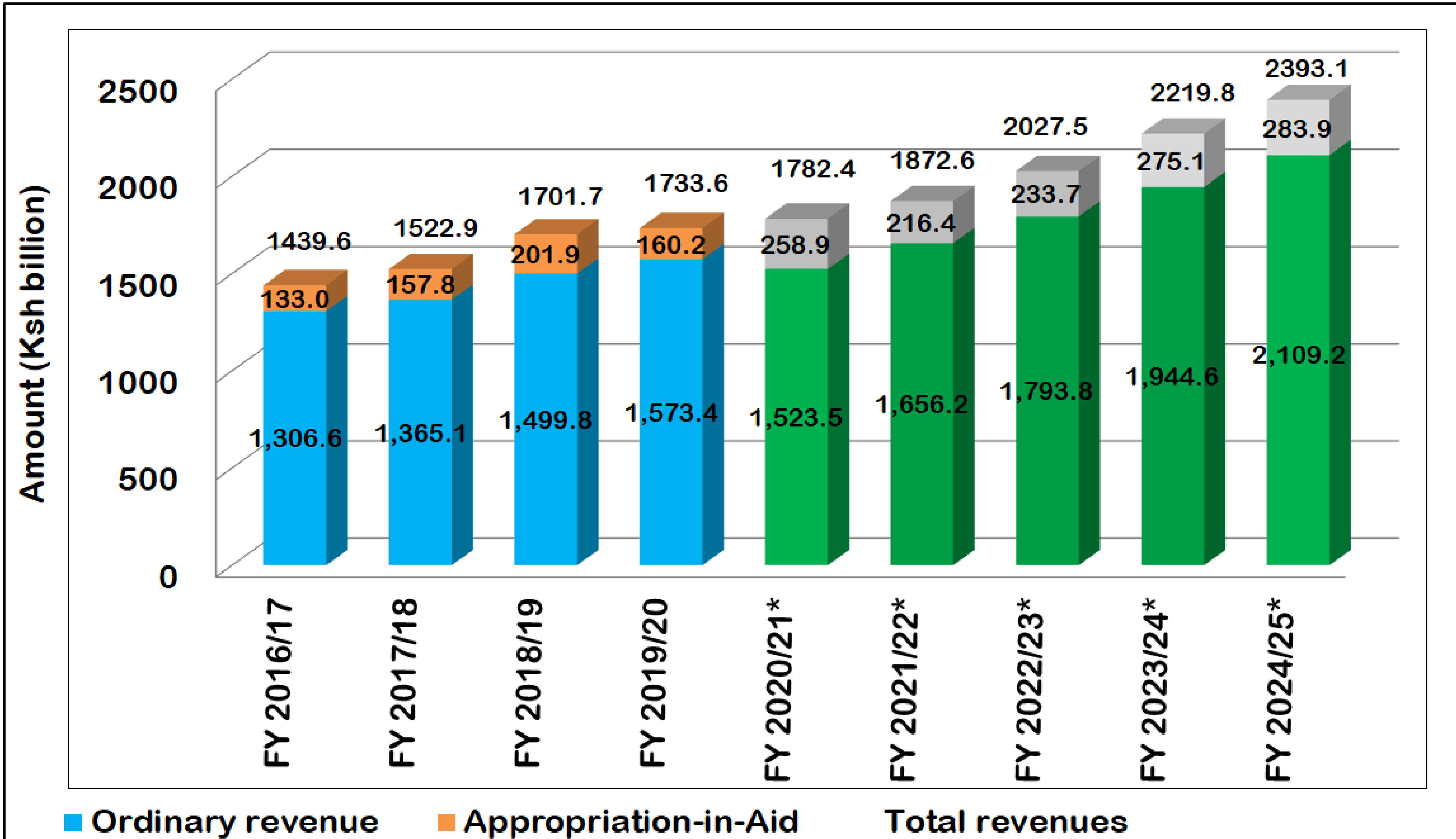
Sub-Saharan Africa Rank
3

- ❑ For four consecutive years (2016, 2017, 2018 and 2019), Kenya emerged at position three in the ease of doing business in sub-Saharan Africa
- ❑ Improving business environment continues to attract investors into the country.

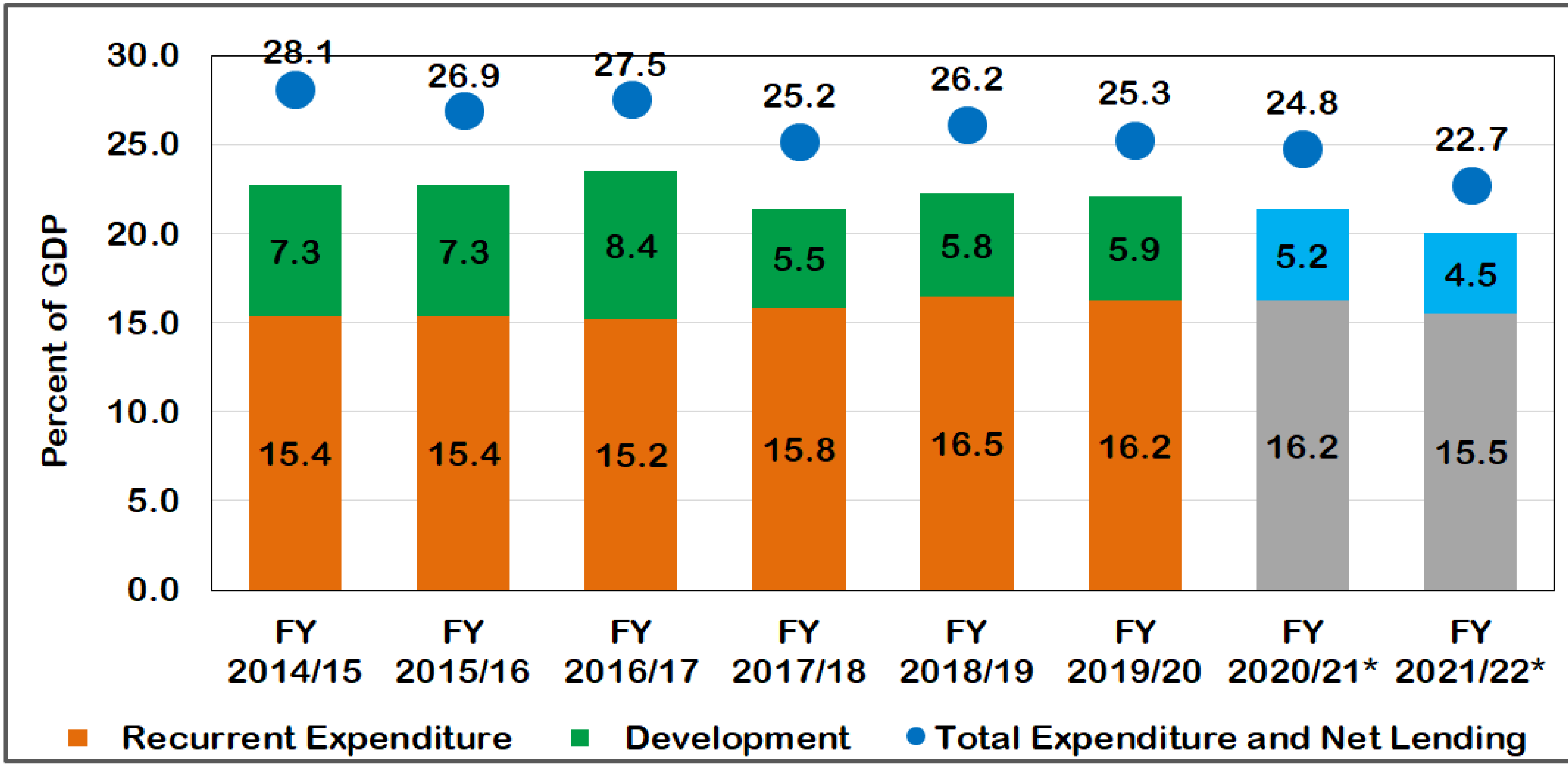
2a. Ordinary revenue growth is projected to contract by 3.2% in FY 2020/21 largely due to the negative effects of the COVID-19 Pandemic on businesses and the tax incentives introduced to cushion Kenyans and businesses from the economic impact of the Pandemic. This growth is expected to rebound to 8.7% in FY 2021/22.



2b. Total revenues for FY 2021/22 are projected at Ksh 1872.6 billion (15.0% of GDP) from Ksh1782.4 billion (15.8% of GDP) in FY 2020/21

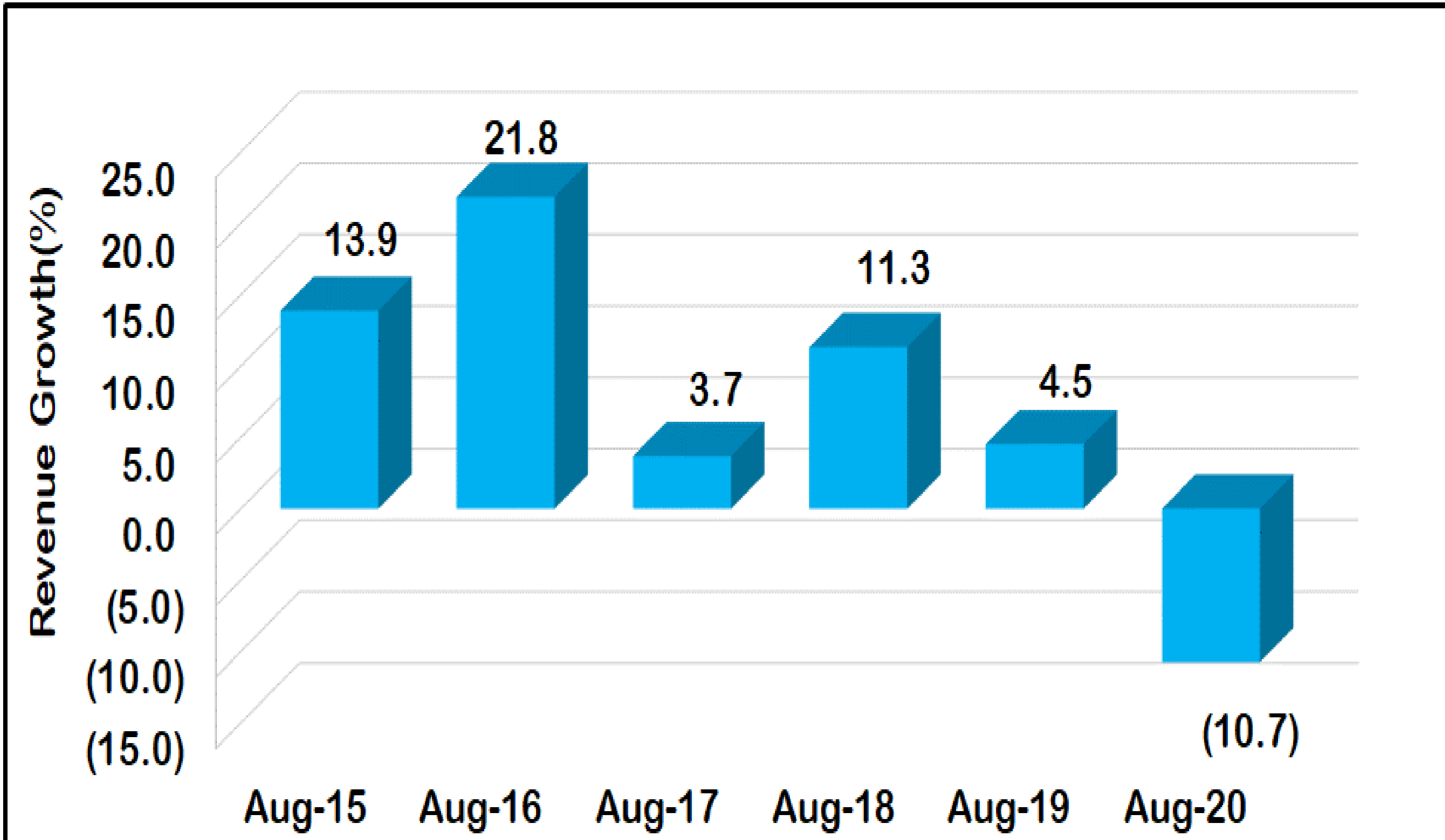


2c. Total expenditure as a share of GDP has fairly been stable since FY 2017/18 and projected at 22.7% of GDP in FY 2021/22. Total expenditure have been rationalized to ease funding pressures and create fiscal space

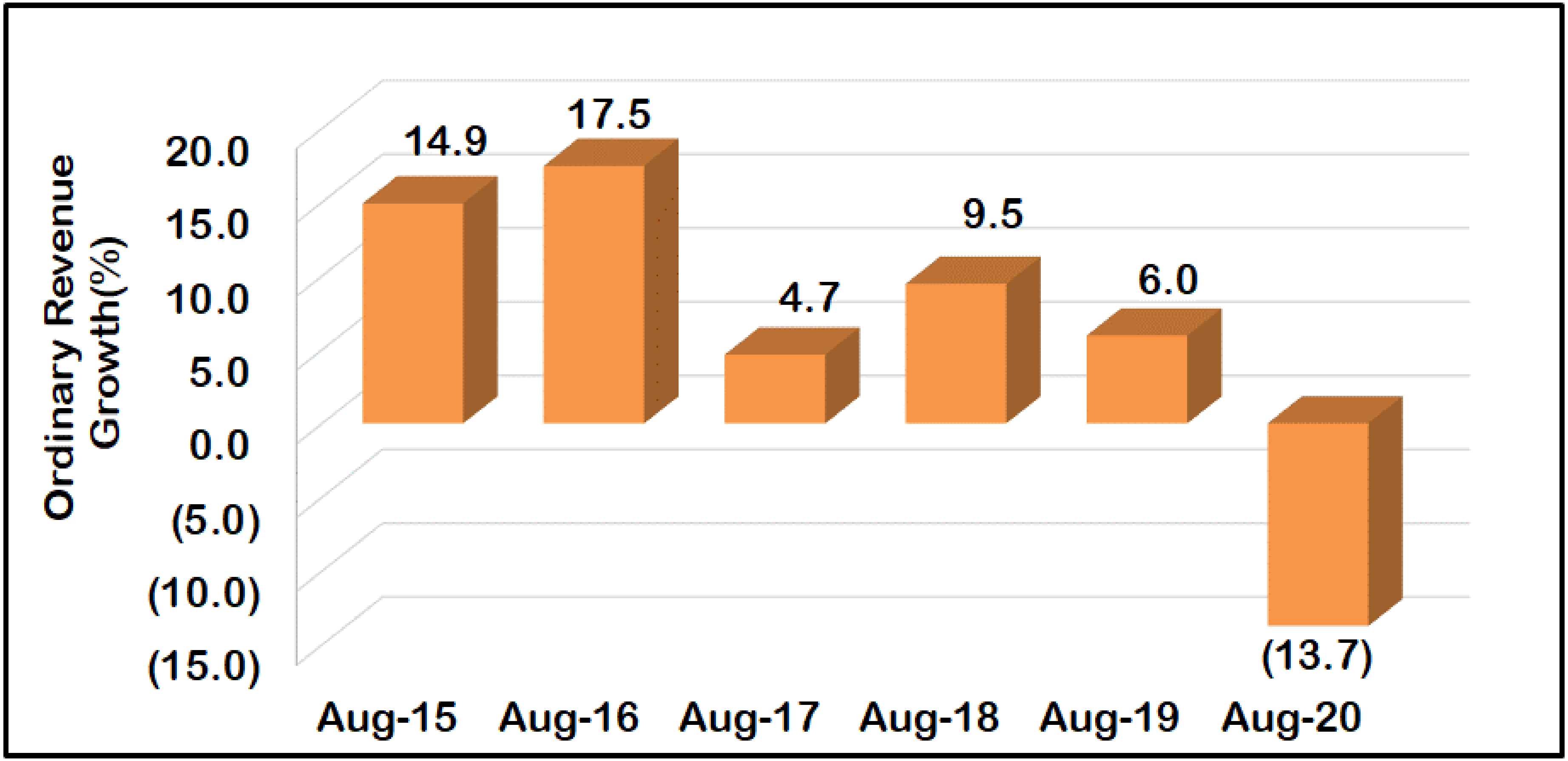


- ❑ Both development and recurrent expenditures are also projected to increase in FY 2020/21

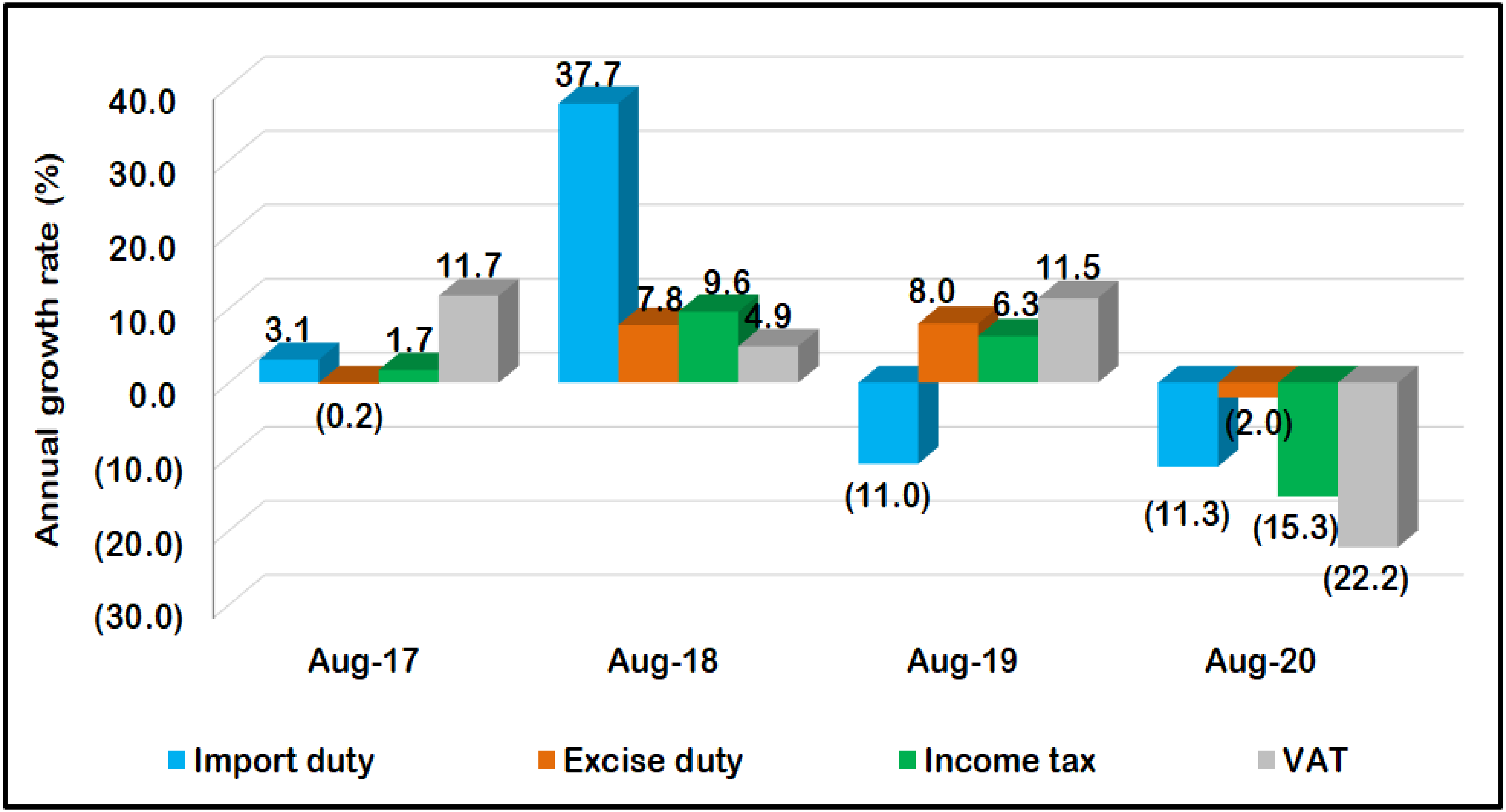
2d. Budget Implementation: Total revenue contracted by 10.7% in August 2020 down from a growth of 4.3% in August 2019…Impact of COVID 19



2e. Budget Implementation: The decline in total revenue was partly due to the decline in ordinary revenue at 13.7% in August 2020…Impact of COVID 19



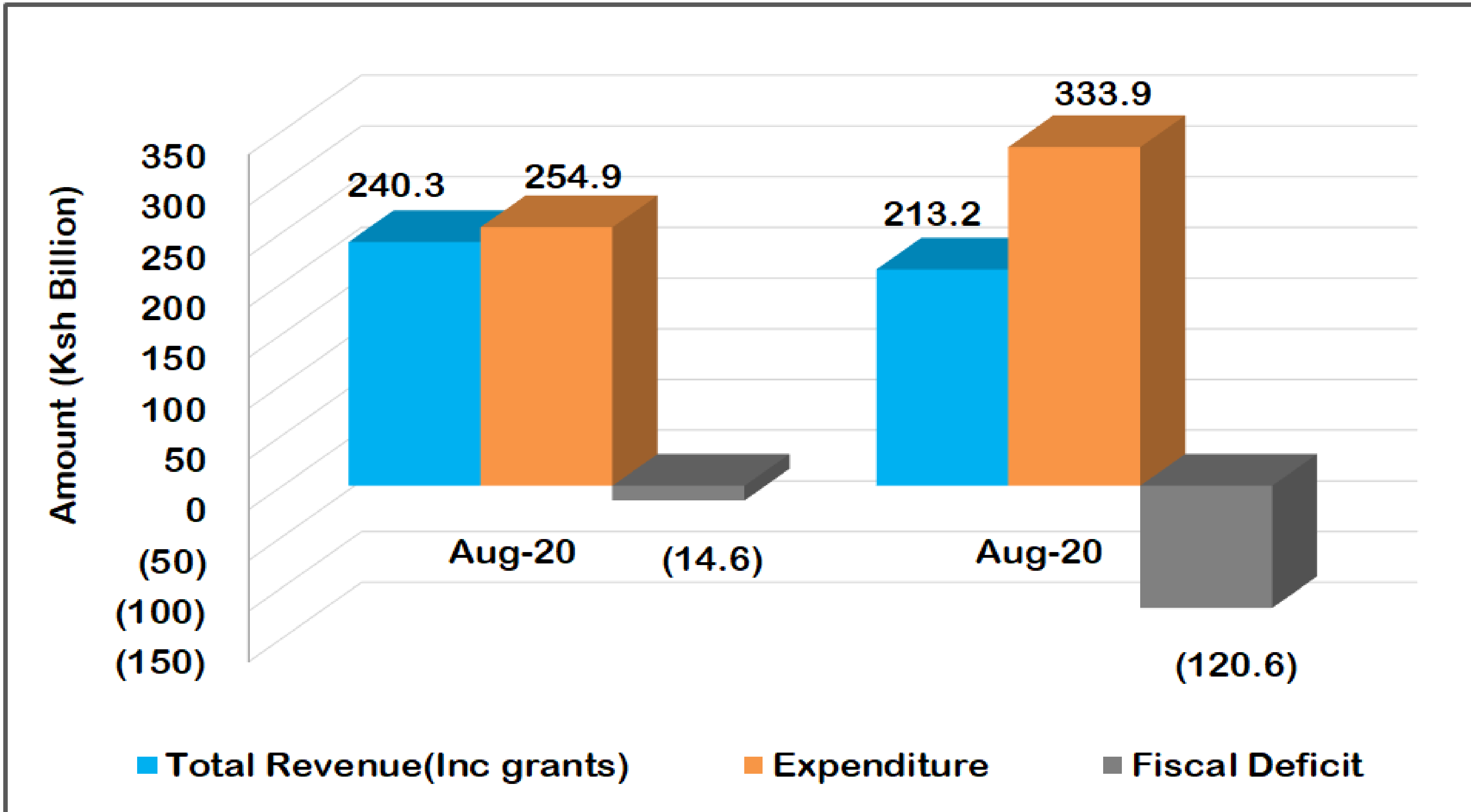
2f. Budget Implementation: All major tax categories recorded a negative growth for the period ending August 2020; income tax declined by 15.3%, excise taxes (2.0%), import duty (11.3%) and VAT by (22.2%)



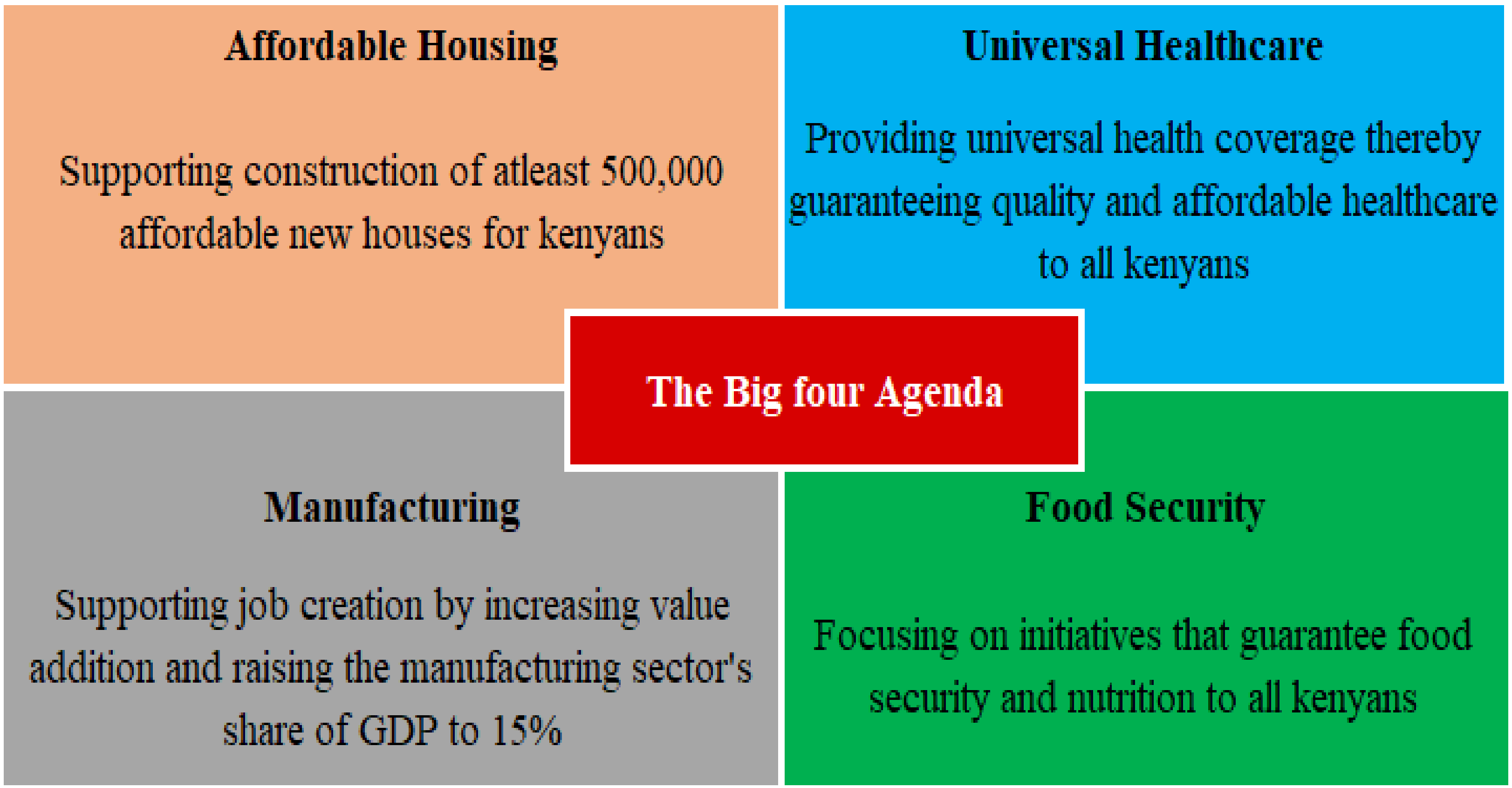
2g. Total Expenditure and Net lending grew by 31.0% in August 2020 compared to August 2019. The increase was observed in both the recurrent and development expenditures

	Aug-19	Aug-20			%
	Actual	Target	Actual	Deviation	Growth
TOTAL EXPENDITURE AND NET LENDING	254.9	293.5	333.9	40.4	31.0
1. Recurrent Expenditure	237.8	249.6	251.6	2.1	5.8
Domestic Interest	50.4	49.2	56.8	7.6	12.7
Foreign Interest due	25.5	33.3	30.3	(3.0)	18.8
Pensions and Othe CFS	6.5	19.0	13.6	(5.4)	107.8
Operation and maintainance	0.2	0.7	0.4	(0.3)	91.4
Wages & Salaries	76.7	75.2	75.2	0.0	(1.9)
Ministerial Recurrent AIA	10.6	9.3	10.4	1.2	(1.4)
2. Development	17.0	38.8	54.2	15.4	218.3
Domestically Financed (Gross)	7.9	15.6	41.9	26.3	430.8
Foreign Financed	9.1	23.2	12.3	(10.9)	34.4
Net Lending				0.0	
Equalization Fund				0.0	
3. County Transfer		5.1	28.0	22.9	

2h. Fiscal deficit including grants by August 2020 was Ksh 120.6 billion compared with Ksh14.6 billion by August 2019



3. Government Policy Priorities - "The Big Four" Agenda are embedded in the FY 2020/21 Budget. Drivers and Enablers of the four priorities are expected to fund sufficiently activities related to the Big Four Agenda



4a Assumptions in the Macroeconomic Framework for the FY 2020/21-2024/25 MTEF Period

	Calender Years	2018	2019	2020	2021	2022	2023	2024	2025
				Projections					
1	**Nominal Gross Domestic Product (GDP) Deflator**	**2.4%**	**4.0%**	**6.8%**	**5.7%**	**5.3%**	**5.3%**	**5.6%**	**5.6%**
2	Consumer Price Index (CPI (average) (%)	4.7%	5.2%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%
	Consumer Price Index (CPI) (end of period) (%)	5.7%	5.8%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%
3	**Real Gross Domestic Product (GDP) growth (%)**	**6.3%**	**5.4%**	**2.6%**	**5.3%**	**5.0%**	**5.8%**	**5.9%**	**5.9%**
4	**Nominal Gross Domestic Product, Ksh Billion**	**8,892.1**	**9,740.4**	**10,677.8**	**11,886.2**	**13,148.0**	**14,649.5**	**16,386.5**	**18,326.6**
5	**Nominal Gross Domestic Product, Growth (%)**	**8.9%**	**9.6%**	**9.6%**	**11.3%**	**10.6%**	**11.4%**	**11.9%**	**11.8%**

4b. Assumptions in the Macroeconomic Framework for the FY 2020/21-2024/25 MTEF Period

	Fiscal Years	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24	2024/25
1	**Nominal Gross Domestic Product (GDP) Deflator**	**3.2%**	**5.4%**	**6.2%**	**5.5%**	**5.3%**	**5.4%**	**5.3%**
2	Consumer Price Index (CPI (average) (%)	4.9%	5.1%	5.0%	5.0%	5.0%	5.0%	5.0%
	Consumer Price Index (CPI) (end of period) (%)	5.7%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%
3	**Real Gross Domestic Product (GDP) growth (%)**	**5.9%**	**4.0%**	**4.0%**	**5.2%**	**5.4%**	**5.9%**	**5.9%**
4	**Nominal Gross Domestic Product, Ksh Billion**	**9,303.1**	**10,199.9**	**11,266.6**	**12,501.6**	**13,879.0**	**15,494.8**	**17,286.2**
5	**Nominal Gross Domestic Product, Growth (%)**	**5.9%**	**4.0%**	**4.0%**	**5.2%**	**5.4%**	**5.9%**	**5.9%**

4c: Sectoral GDP Growth Projections

Growth is projected at 2.6 percent in 2020 and 5.3 percent in 2021

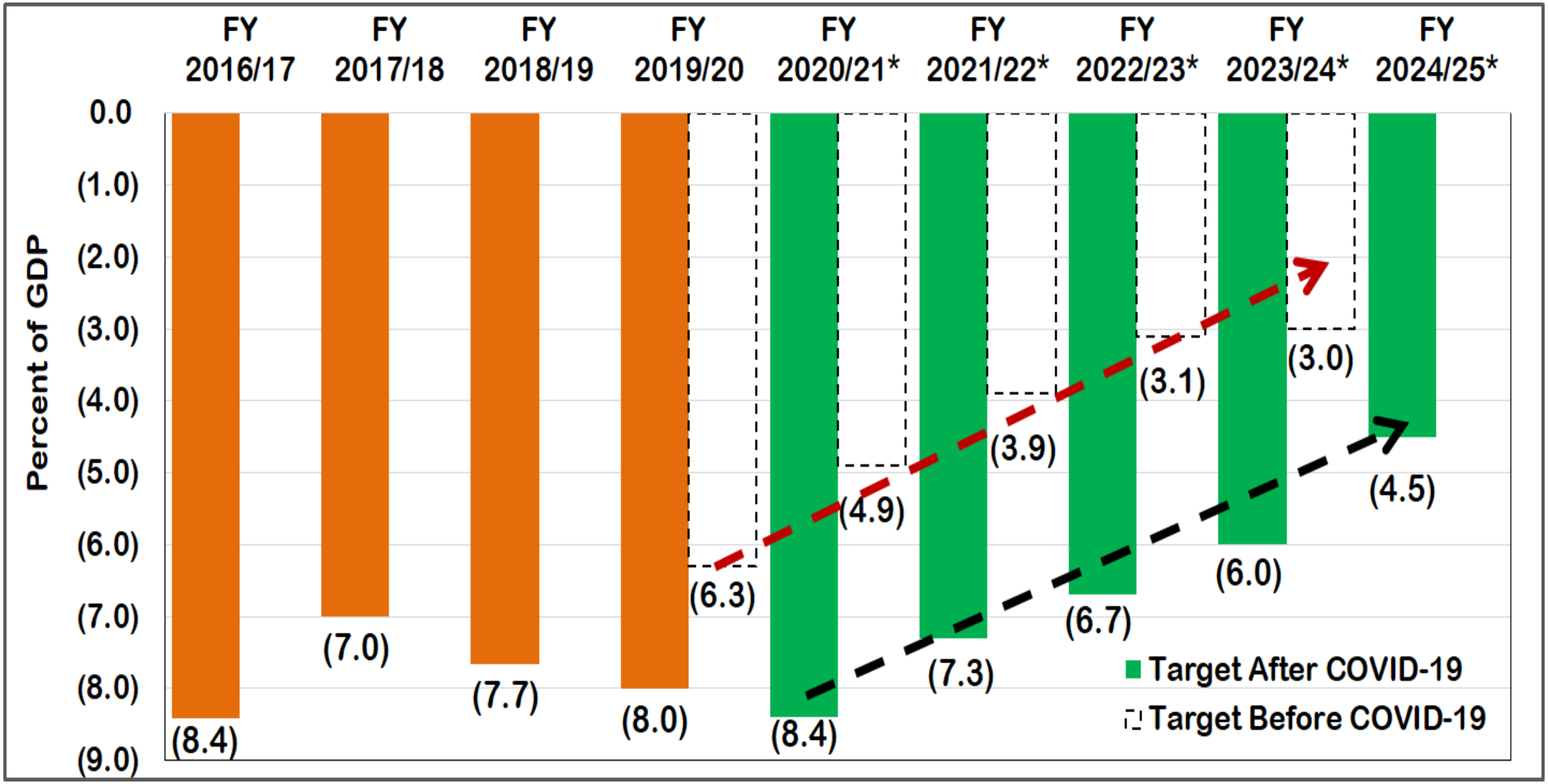
	2018	2019	2020	2021	2022	2023	2024	2025
Sectors	Act	Act	Proj.	Proj	Proj	Proj	Proj	Proj
Primary sector	**5.8**	**3.5**	**4.0**	**4.7**	**4.9**	**6.1**	**5.6**	**5.1**
Agriculture,forestry and fishing	6.1	3.6	4.1	4.8	5.0	6.2	5.7	5.2
Mining and Quarrying	2.7	2.5	2.9	2.6	3.1	3.3	3.7	3.7
Secondary sector	**5.6**	**4.8**	**3.0**	**4.4**	**3.2**	**4.6**	**4.6**	**4.5**
Manufacturing	4.3	3.2	2.7	3.9	2.7	4.3	4.1	4.1
Electricity and Water supply	8.0	7.0	4.3	6.0	5.6	6.5	6.3	5.9
Construction	6.9	6.4	2.9	4.6	2.9	4.3	4.5	4.4
Tertiary Sector	**6.7**	**6.7**	**1.8**	**5.8**	**5.5**	**6.1**	**6.5**	**6.5**
Trade, hotels and restaurant	8.2	7.2	-0.4	4.2	5.1	7.0	7.8	7.5
Wholesale and Retail trade	6.9	6.6	3.1	6.2	5.6	7.1	7.3	7.1
Accomodation and Restaurants	16.4	10.4	-18.7	-9.1	0.6	5.8	11.9	11.1
Transport and Storage	8.5	7.8	0.7	4.9	5.7	5.5	5.3	4.9
Information and Communication	11.3	9.0	8.0	11.3	11.2	10.7	11.2	11.5
Financial & Insurance	5.3	6.6	4.2	6.2	5.0	5.4	5.2	5.1
Real estate	4.1	5.3	0.7	4.4	3.7	4.2	4.5	5.1
Other services	4.9	5.3	0.7	5.2	4.3	4.7	5.3	5.6
Public administration	6.7	8.1	4.2	7.2	5.8	6.7	6.7	6.9
Professional, Admin & Support Services	5.9	4.9	2.7	4.5	4.0	3.8	4.1	4.0
Education	5.8	5.4	-2.0	6.3	4.6	5.2	6.3	6.5
Health	4.4	5.8	6.7	6.2	6.5	6.9	7.1	7.2
Other \1	4.9	5.1	3.0	4.5	4.2	4.1	4.1	4.1
Less: FISM	1.0	6.2	1.1	1.0	2.3	2.6	1.7	1.9
All industries at basic prices	**6.4**	**5.5**	**2.6**	**5.4**	**5.0**	**5.9**	**6.0**	**5.9**
Taxes less subsidies	5.6	4.4	2.7	5.0	5.3	5.3	5.6	6.3
GDP at Market Prices	**6.3**	**5.4**	**2.6**	**5.3**	**5.0**	**5.8**	**5.9**	**5.9**

4d. Medium Term Fiscal Framework FY 2021/22-2024/25, %of GDP

	FY 2018/19	FY 2019/20	FY 2020/21	FY 2021/22	FY 2022/23	FY 2023/24	FY 2024/25
	Act.		Budget	Projections			
A.Total Revenue and External Grants	18.5	17.3	16.6	15.6	15.2	14.9	13.8
Total revenue incl A-I-A	18.3	17.1	15.8	15.0	14.6	14.3	13.1
External Grants	0.2	0.2	0.5	0.4	0.3	0.3	0.3
B. Total Expenditure and Net lending	26.2	25.3	24.8	22.7	21.7	20.6	18.6
Recurrent Expenditure	16.5	16.2	16.2	15.1	14.2	13.4	12.1
Development Expenditure	5.8	5.9	5.2	4.5	4.6	4.7	4.2
County Allocation	3.9	3.2	3.3	3.0	2.8	2.5	2.3
Contigency fund	0.0	0.0	0.0	0.0	0.0	0.0	0.0
C. Fiscal Deficit Excl Grants	(7.9)	(8.2)	(8.9)	(7.7)	(7.1)	(6.3)	(4.8)
D. Fiscal Deficit incl Grants	(7.7)	(8.0)	(8.4)	(7.3)	(6.7)	(6.0)	(4.5)
E. Total Financing	7.8	7.8	8.4	7.3	6.7	6.0	4.5

- In the FY 2021/22, total revenue incl. grants as % of GDP is projected at **15.6%** and expenditures at **22.7%** of GDP which gives a deficit of **7.3% of GDP.**

4e: Fiscal Consolidation: Fiscal deficit as percent of GDP is projected at 8.4% of GDP in FY2020/21 ,7.3% of GDP in FY 2021/22 and 4.5% of GDP in FY 2024/25.



- The fiscal deficit were revised upwards taking into consideration the effect of COVID-19

5a. Support Measures against adverse effects of COVID-19 Pandemic on Kenyans and Industry

- Reduction of tax rates Granted 100% tax relief for persons earning gross monthly income of up to Ksh.24,000; Reduction of PAYE and corporation income tax rates from 30% to 25% and VAT rate from 16% to 14% ***(Fiscal support of Ksh 172.0 billion or 1.5% of GDP)***
- Reduced turnover tax rate from 3% to 1% to cushion MSMEs
- Initiated cash transfer programme to vulnerable persons distributed via M-pesa
- The Government also established COVID-19 Emergency Response Fund to receive voluntary pay donations and contributions from well-wishers towards COVID-19 Pandemic.
- Scaling up efforts to contain Locust invasion
- Provision of food and non-food necessities and relocating families affected by floods to higher ground and public schools

5b. The 8-Point Economic Stimulus Programme

- To enhance economic activity, the Government (in addition to the fiscal measures already implemented through reduction of tax rates) will in the FY 2020/21 Budget implement an 8 Point Economic Stimulus Programme - to cushion citizens and businesses from the further adverse effects of Pandemic.

- Ksh 56.6 billion **(or 0.5 percent of GDP)** has been set aside in FY 2020/21 for 8 Point Economic Stimulus Programme to support targeted activities

- This include: Improving Infrastructure; Improving Education Outcomes; Enhancing Liquidity to Businesses; Improving Health Outcomes; Agriculture and Food Security; Tourism Promotion; Improving Environment, Water and Sanitation and Supporting Manufacturing Sector.
- Roll out on Post Covid 19 Economic Recovery strategy

6. *Potential* Risks: The macroeconomic outlook is not without risks from both external and domestic sources

- COVID-19 Pandemic has caused an unprecedented human and health crisis globally precipitating economic crisis through:
  - Disrupting production and reducing demand sharply;
  - Plummeting growth in advanced and emerging market economies and tighter global financial conditions will have spill over effects to developing countries
- Internally, public expenditure pressures – wage and recurrent related expenditures
- Locust invasion threatening our food basket
- Unfavourable weather shocks (drought/floods) that adversely impact on agricultural output, energy generation and infrastructural developments

THANK **YOU**