

# KENYA BANKERS ECONOMIC BULLETIN

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**The Centre for Research on  
Financial Markets and Policy®**



**KENYA BANKERS**  
ASSOCIATION



CENTRE FOR RESEARCH ON  
FINANCIAL MARKETS AND POLICY®

**About this Report**

This *Bulletin* reviews Kenya's economic performance in the second quarter of 2023, drawing on the recent performance and developments to provide perspectives on the year's outlook. The *Bulletin* covers trends in selected activities in the real economy, government fiscal operations, public debt, inflation and interest rates, the balance of payments and exchange rate, activity at the Nairobi Securities Exchange and banking sector performance.

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The Centre for Research on Financial Markets and Policy® was established by the Kenya Bankers Association in 2012 to offer an array of research, commentary, and dialogue regarding critical policy matters that impact on financial markets in Kenya. The Centre sponsors original research, provides thoughtful commentary, and hosts dialogues and conferences involving scholars and practitioners on key financial market issues. Through these activities, the Centre acts as a platform for intellectual engagement and dialogue between financial market experts, the banking sector and the policy makers in Kenya. It therefore contributes to an informed discussion that influences critical financial market debates and policies.



CENTRE FOR RESEARCH ON  
FINANCIAL MARKETS AND POLICY®

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## FOREWORD

## From the CEO's Desk

It is my pleasure to present the 40th issue of the *Kenya Bankers Economic Bulletin*, highlighting the developments shaping Kenya's economy. This edition provides a detailed analysis of key developments in the macroeconomic environment, including inflation, sectoral performance, credit growth, and the external sector.

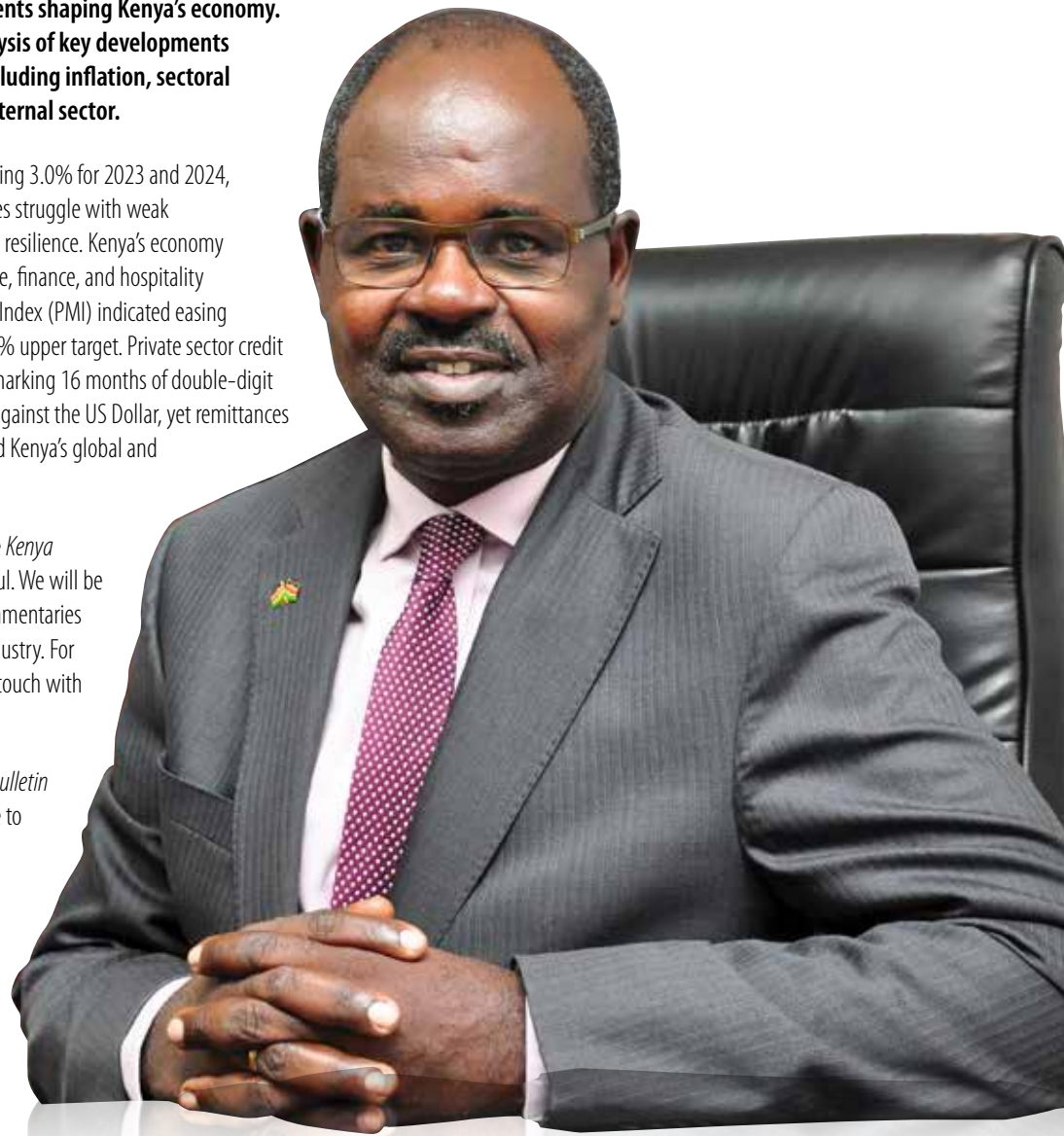
Global growth is slowing, with the IMF projecting 3.0% for 2023 and 2024, down from 3.5% in 2022. Advanced economies struggle with weak manufacturing, while emerging markets show resilience. Kenya's economy grew by 5.4% in Q2 2023, driven by agriculture, finance, and hospitality rebounds. However, the Purchasing Managers Index (PMI) indicated easing activity, while inflation breached the CBK's 7.5% upper target. Private sector credit surged to 12.1% year-on-year in June 2023, marking 16 months of double-digit growth. The Kenya Shilling weakened 17.9% against the US Dollar, yet remittances remained steady. Trade diversification bolstered Kenya's global and regional ties amid external sector volatility.

It is my hope that you will find this issue of the *Kenya Bankers Economic Bulletin* interesting and useful. We will be happy to consider for publications incisive commentaries on a topical issue of interest to the banking industry. For guidelines on such submissions, please get in touch with the Bulletin's Editor at [research@kba.co.ke](mailto:research@kba.co.ke).

We welcome feedback on the content of this *Bulletin* as we continually seek to improve its relevance to you.

**Dr. Habil Olaka**

Chief Executive Officer,  
Kenya Bankers Association



COMMENTARY

# Outlook: Managing Inflation Risks Amid Global and Domestic Pressures



By Samuel Tiriongo, PhD

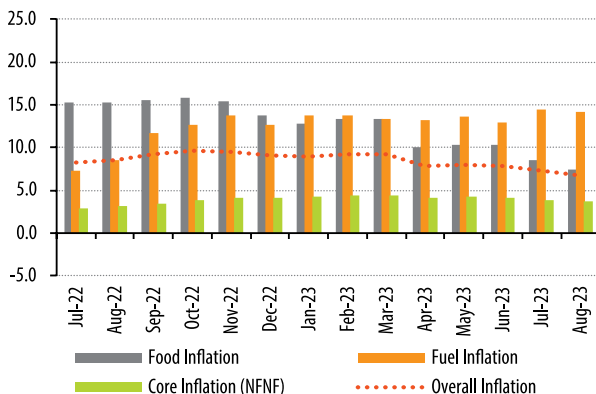
**A**mid a slight slowdown in inflationary pressure during the quarter, several risks point to potential inflationary increases in the coming months.

These include upward adjustments in fuel pump prices, depreciation of the exchange rate, and the anticipated impact of heavy rains on food production. The headline inflation in August declined to 6.7% from 7.3% in July (**Figure 1a**) on eased food prices and a moderation in core inflation over the period. As food inflation declined to 7.5% from 8.6% in July, core inflation dropped marginally to 3.7% from 3.8% over the period.

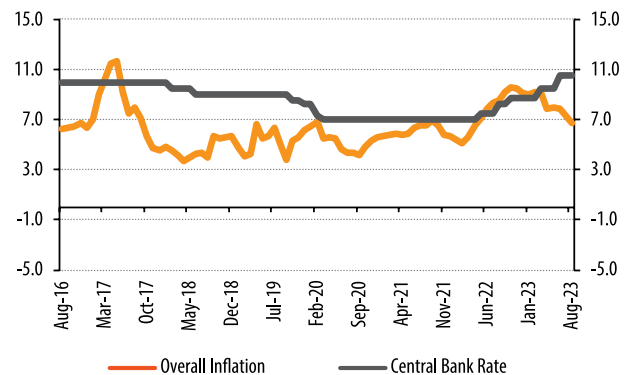


**Figure 1: Inflation Drivers and Policy Rate Dynamics**

**(a) Inflation versus Central bank rate (%)**



**(b) Inflation and its components components (%)**



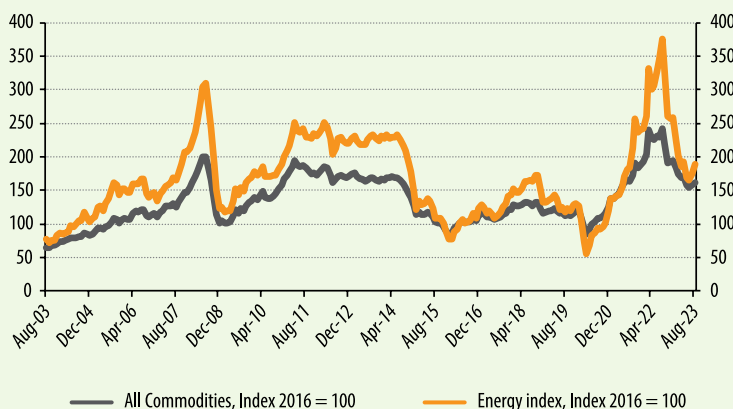


## “ Other risks to inflation include Russia’s suspension of its participation in the Black Sea Grain Initiative and the forecasted El Nino rains causing destruction of food produce in the fourth quarter

However, fuel inflation remained elevated at 14.2% in August reflecting sustained oil price pressures in the economy (Figure 1b). With the recent sharp upward adjustment by EPRA in local fuel pump prices in mid-August – driven by rising global oil prices (Figure 1c) with the Murban Crude oil prices edging up from US\$ 88.91 at end August to US\$ 95.04 per barrel on 27<sup>th</sup> September, local fuel price inflation is expected to increase, and potentially drive-up other commodity prices in the near to medium term given that oil is an intermediate good. Other risks to inflation include Russia’s suspension of its participation in the Black Sea Grain Initiative and the forecasted El Nino rains causing destruction of food produce in the fourth quarter of 2023.

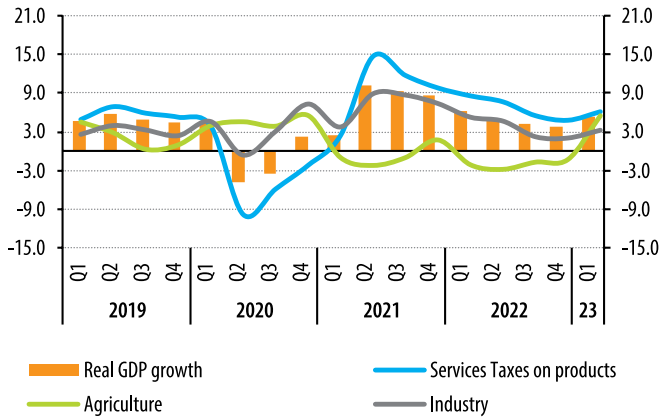
**Economic growth is projected to soften towards the end of 2023 on account of elevated cost of living and the adverse effects of new taxes on consumer demand, amidst the continuing implementation of fiscal consolidation.** Beyond the strong first quarter growth (Figure 2a), leading indicators of economic performance in the second and third quarters of 2023 show depressed activity. In particular, the Purchasing Managers’ Index™ (PMI™) remained below the 50.0 mark consistently after March; only showing a recovery of economic activity in August when the index stood at 50.6 (Figure 2b). The main factor behind the depressed activity is cited as elevated input prices. In addition, a tightening monetary policy impact on cost of credit and concerns of slowdown in consumption patterns with rising cost of living, as well as the implementation of fiscal consolidation by the Government to mitigate debt vulnerabilities, continue to pose risks to stronger economic growth prospects.

(c) Evolution of Global Commodity Prices

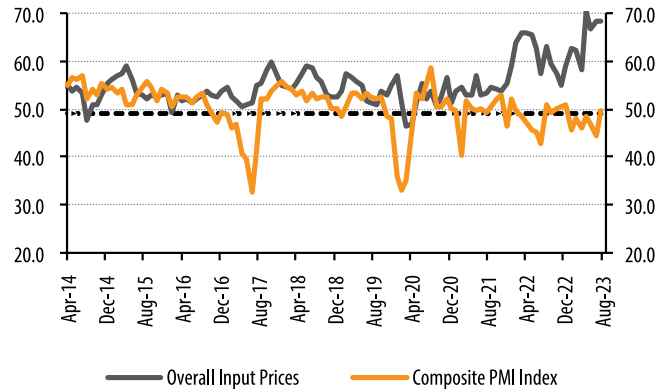


**Figure 2: Economic Growth Performance Indicators**

**(a) Sectoral and aggregate GDP Growth rates (%)**



**(b) Kenya Purchasing Managers's Index (PMI)**



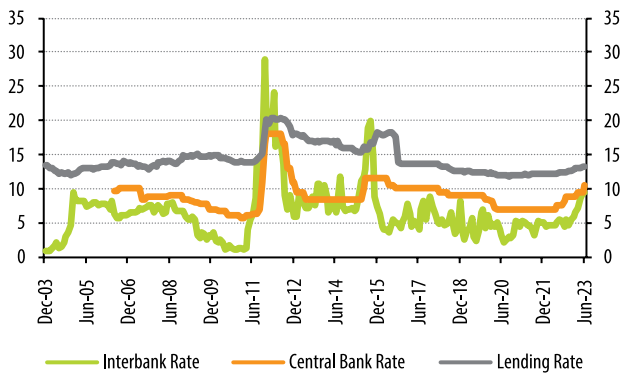
Source: KNBS and IHS Markit®

Interest rates continue to rise in response to the existing tight monetary policy stance. Higher interest rates are expected to raise the cost of funds and cost of credit, thereby moderate credit demand. The MPC gradually tightened the monetary policy stance since June 2022; raising the CBR from 7.5 percent to 10.5 percent over the period to early August 2023 (Figure 3b). The implication of this has been an increase in money market yields and an increase in interbank market rates. Banking sector average lending rates have also increased suggesting that the effects of the tight monetary policy continue to be felt in the credit market (See Figure 3a). During the MPC meeting on 9<sup>th</sup> August 2023, the

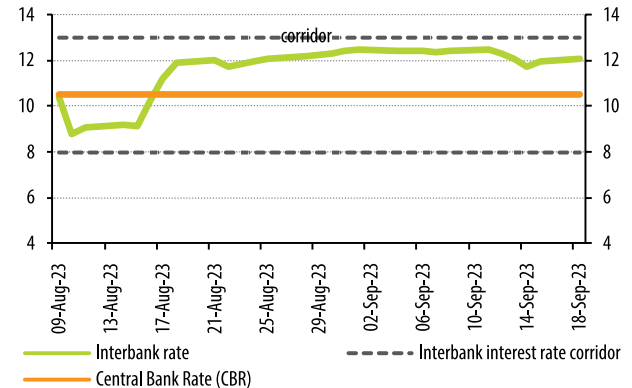
central bank introduced an interest rate corridor framework to guide monetary policy operations and market outcomes. The corridor provided for a targeting of the interbank rate to oscillate within basis points around the CBR, with the aim of enhancing the effectiveness of the bank's policy. This has been since achieved (Figure 3b). However, there remain concerns of weaker transmission of the policy signal from the interbank market to other longer term market interest rates, particularly the lending rates, that would otherwise effectively trigger the anticipated faster slowdown in credit supply.

**Figure 3: Trends in the Money Market Rates**

**(a) Interbank Rates, Lending Rates and CBR**



**(b) Interbank Rate within the interest rate**



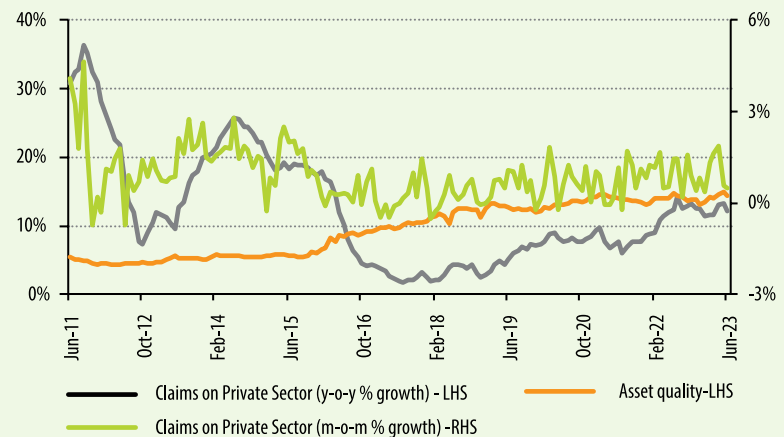
Source: Central Bank of Kenya

Despite elevated credit risk, private sector credit growth remains strong with delayed transmission of a tight monetary policy signal; continuing strong credit demand by customers to finance economic activities as the economy remains on the path of recovery from the depressing effects of COVID-19 in 2020 and 2021. Credit growth stood at double digits consistently since March 2022 reflecting strong financing of economic activities and recovery from the depressing effects of COVID-19 pandemic. Latest data shows that overall private sector credit growth in July 2023 stood at 10.3 percent; depicting a slowdown from 12.2 percent in June. The slowdown is partly attributed to the tightening monetary conditions and an elevated credit risk (**Figure 4a**).



A sectoral disaggregation of commercial banks' credit to the private sector in July showed that credit growth to agriculture (19.0%) was the strongest, followed by mining & quarrying activities (16.7%), transport and communication (16.4%), manufacturing (14.7%), consumer durables (12.9%) and business services (10.7%) (**Table 1**). The notable strong credit growth, in an environment of tightened monetary policy stance, reflect a weaker transmission of policy signals to lending rates. This is partly attributed to structural challenges associated with the restrictions in the implementation of risk-based credit pricing by banks.

**Figure 4: Trends in Private Sector Credit and Asset quality**



**Table 1: Sectoral Growth in Private Sector Credit**

Sector	Jul/22	Aug/22	Dec/22	Mar/23	Jun/23	Jul/23
Agriculture	10.8	19.2	22.3	14.9	18.6	19.0
Manufacturing	16.1	15.2	13.8	15.8	18.0	14.7
Trade	15.2	13.3	11.4	11.9	10.2	7.4
Building and construction	14.1	11.5	8.2	5.8	4.9	1.9
Transport & communications	27.0	13.5	23.5	17.4	19.8	16.4
Finance & insurance	2.8	1.2	7.6	28.4	29.7	35.4
Real estate	1.7	1.0	3.2	2.3	3.7	3.0
Mining and quarrying	78.6	97.2	31.3	83.2	24.0	16.7
Private households	7.6	7.8	8.2	7.2	8.4	7.0
Consumer durables	14.8	14.3	12.9	12.7	12.0	12.9
Business services	16.9	16.1	13.7	9.3	12.1	10.7
Other activities	69.8	60.8	41.8	11.9	8.7	0.5
Growth in credit to the private sector (%)	14.2	12.5	12.5	11.6	12.2	10.3

Source: Central Bank of Kenya



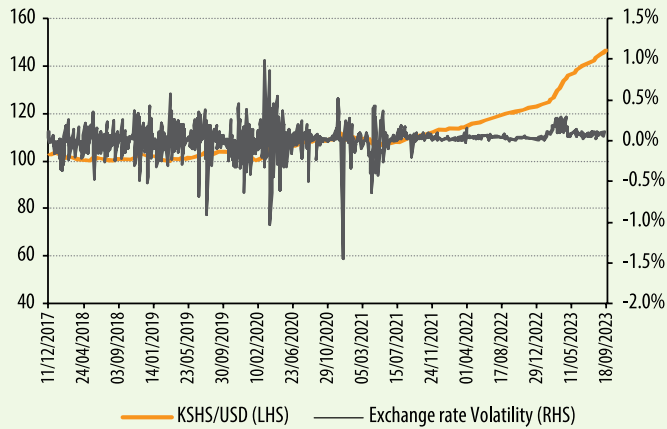
Kenya's external sector remains heavily exposed to the global shocks, and the effects of policy measures taken by advanced markets to tame inflationary pressures. These developments have been manifested fundamentally in exchange rate movements locally. The Shilling exchange rate to the US dollar continues on a stronger trend depreciation path (**Figure 5a**) driven partly by rising global interest rates that have made US dollar investments more attractive compared to the domestic Shilling investments and expectations by economic agents of a further depreciation in the near term. This is despite a trend narrowing of the cumulative overall current account deficit (**Figure 5b**).

Going forward, the risk of a reversal in the current account deficit may be driven by rising global oil prices, sustained high interest rates in advanced markets that continue to attract investors towards US dollar denominated investments. However, this depreciation continues to be tempered by resilient diaspora remittances inflows (**Figure 5c**) – which grew by 14.15% in the 12 months to August 2023 over a similar period to August 2022. The country's foreign exchange reserves have been moderate, standing at USD 6.96 billion as of 21 September 2023 (**Figure 5d**), which is equivalent to 3.80 months of import cover; just within CBK's minimum statutory requirement of 4.0 months of import cover.

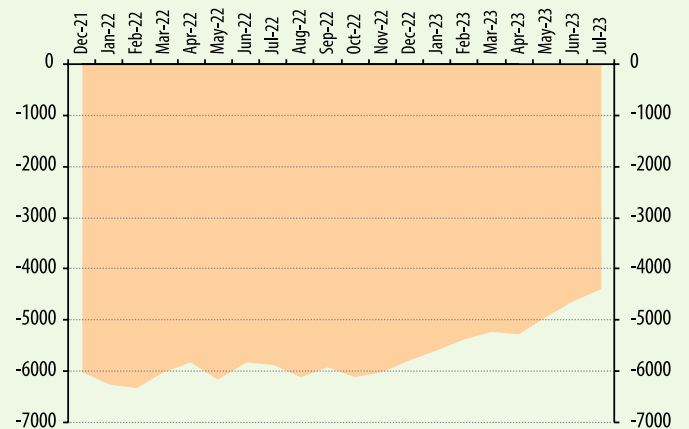


Figure 5: The external Sector

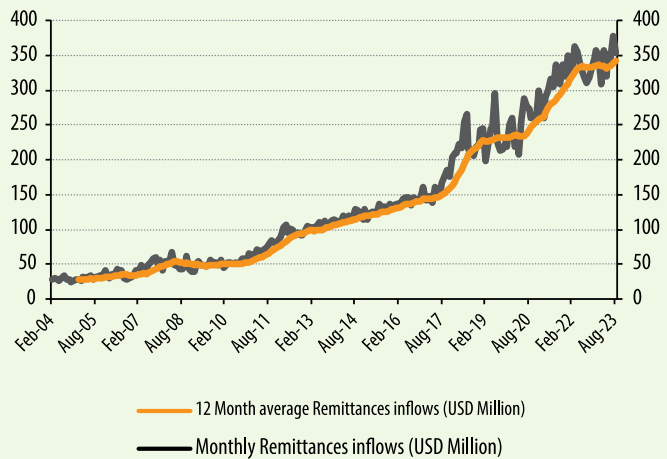
(a) Trends in KES/USD exchange rate



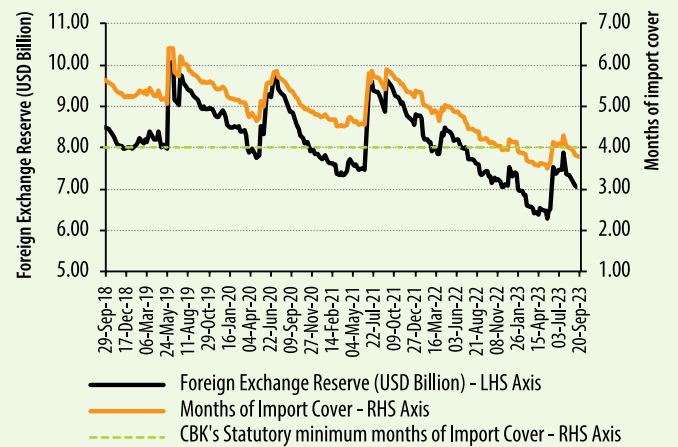
(b) Current Account



(c) Remittances flows



(d) Foreign Exchange Reserves



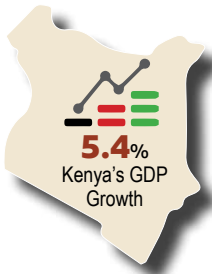
Source: Central Bank of Kenya

OUTLOOK

# State of the Economy

According to the World Economic Outlook<sup>1</sup>, the global economic outlook depicts a decelerating growth trajectory, with a revised projection of 3.0 percent for both 2023 and 2024, down from 3.5 percent in 2022 as had been predicted in the April 2023 World Economic Outlook (WEO).

This decline is mainly driven by Advanced economies as a result of manufacturing weaknesses, which affects overall GDP. On its part, Emerging markets exhibit stability despite regional disparities.



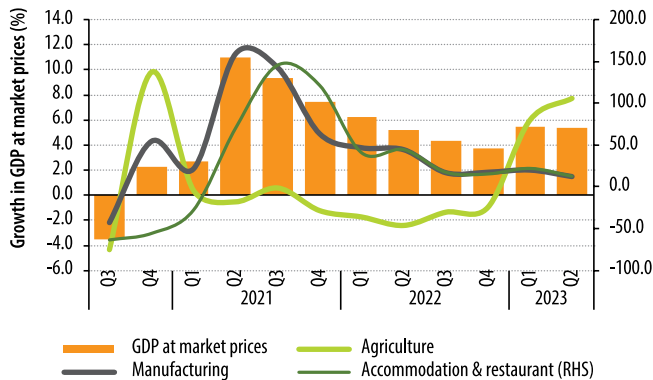
In Kenya, the domestic economy grew by 5.4 percent in the second quarter of 2023 compared to 5.2 percent growth recorded in the second quarter of 2022, mainly on account of rebound in the agricultural sector (7.7 percent), Financial and Insurance (13.5 percent); Accommodation and restaurant (12.2 percent). The manufacturing sector grew by (1.5 percent) (Figure 6a). The Forward-looking Purchasing Managers' Index (PMI) was less optimistic as it lay below the 50-mark during the second quarter 2023, thereby



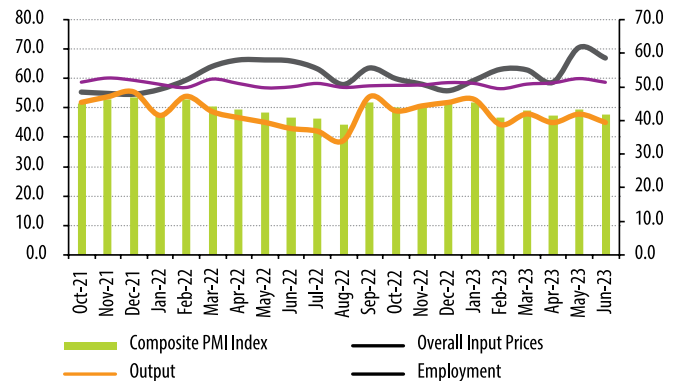
1. <https://www.imf.org/en/Publications/WEO/Issues/2023/07/10/world-economic-outlook-update-july-2023>

Figure 6: GDP Performance and Economic Outlook

(a) Domestic Economic performance



(b) Trends in PMI



Source: KNBS and IHS Markit®



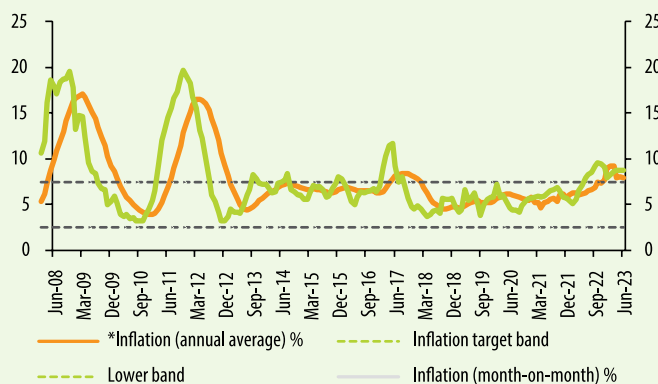
“ Inflationary pressure heightened during the quarter, with the overall inflation drifting above the Central Bank of Kenya upper target band of 7.5 percent

signalling softening in economic activity. The index pointed to a decline in the Input purchases and activity levels and persistent increase in the employment numbers. The overall input prices remained elevated during the quarter, to peak in May 2023, where it rose to 70.5 (Figure 6b).

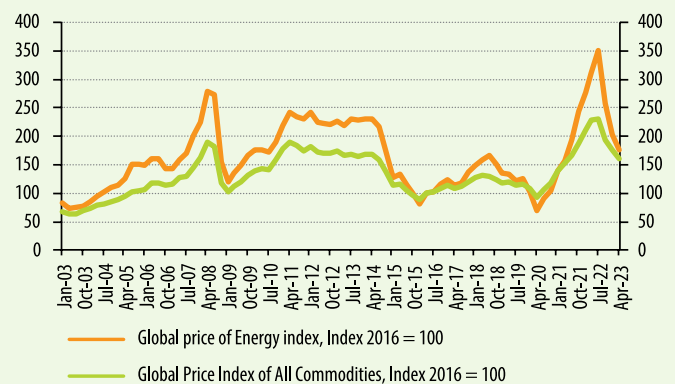
Inflationary pressure heightened during the quarter, with the overall inflation drifting above the Central Bank of Kenya upper target band of 7.5 percent (Figure 7a). The annual headline rose to 7.88 percent in June 2023. The high inflation is mainly attributed to the high food prices as a result drought conditions which constrained food production. Moreover, the food inflationary pressure was further exacerbated by spike in global commodities prices at the back of continued global spillovers from the Russia-Ukraine war (Figure 7b).

Figure 7: Trends in Inflation and Murban Crude oil prices

(a) Inflation trends



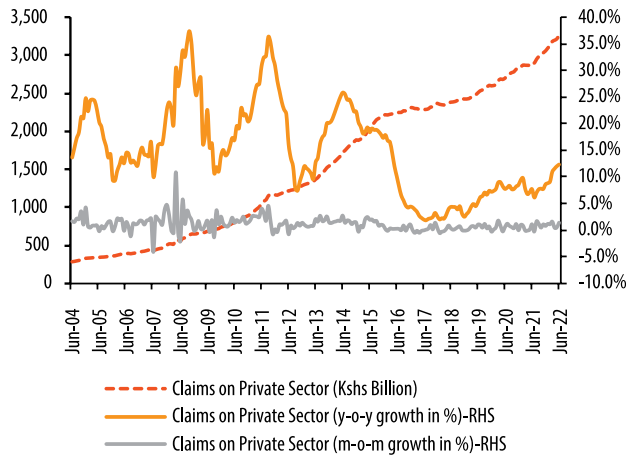
(b) Trends in Murban oil price



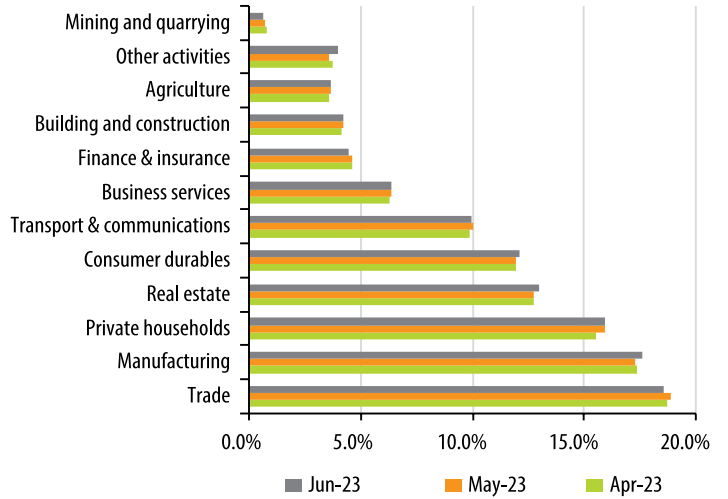
Source: Central bank of Kenya and Oil price.com

**Figure 8: Private Sector Credit and Growth Dynamics**

**(a) Private Sector Credit and Growth Dynamics**



**(b) Sectoral distribution of private sector credit in Q3**



Source: CBK



Credit extension to the private sector remained upbeat with banks' increased adoption of the risk-based credit pricing framework giving renewed impetus to double-digit credit growth. At 12.1 percent year-on-year credit growth in June 2023, credit to the private sector marked the sixteenth consecutive month that it has remained buoyant on the double-digit growth trajectory (**Figure 8a**). However, sectoral disparities in credit growth remains evident in the economy, as the trade, Manufacturing and private households registered a significant increase in the amount of credit allocation. In contrast, credit slowed in Building and construction, agriculture, Mining and quarrying (**Figure 8b**).

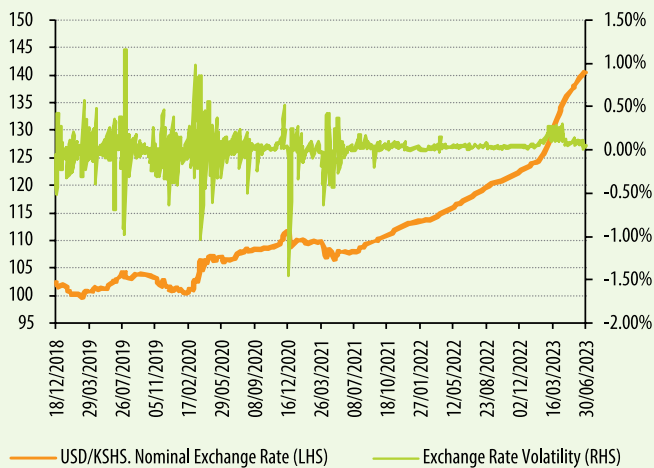
There was an increased demand for the US dollar in the economy. As a result, the Kenya Shilling weakened by 17.9 percent against the US Dollar to exchange at an average of Ksh.137.1 in the second quarter of 2023. In a similar period in 2022, the Kenya Shilling exchanged at 116.3 against the dollar (**Figure 9a**). Immigrant remittances was also lower compared to the receipts in a corresponding period in 2022. However, when the receipts are compared to the first quarter of 2023, it is a 0.27 percent growth; having risen from USD 1,015.6 million during the first quarter to USD 1,018.3 million in the second quarter of 2023 (**Figure 9b**).

The trade landscape continued to display a diverse and intricate web of dependencies, with strong trade relations with both the rest of the world and the African continent emerging strongly between Kenya and its trade partners. In terms of exports, the primary flow of goods head to a number of unspecified countries,

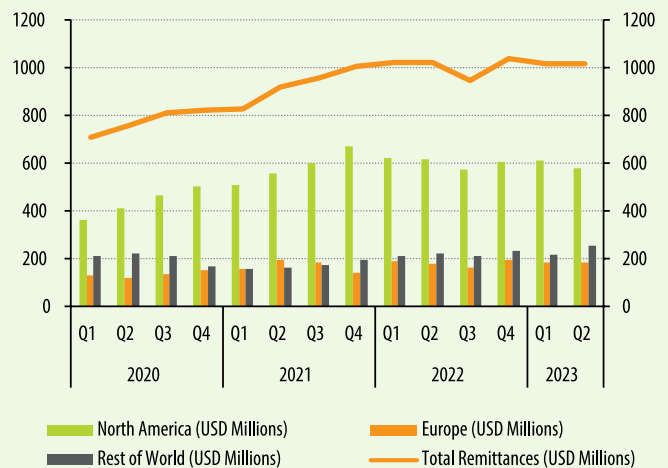


**Figure 9: Kenya Shilling -US Dollar Exchange Rate dynamics and Remittances inflow**

**(a) Kenya Shillings vs US Dollar Exchange Rate Dynamics**



**(b) Trends in remittances flow by regions**

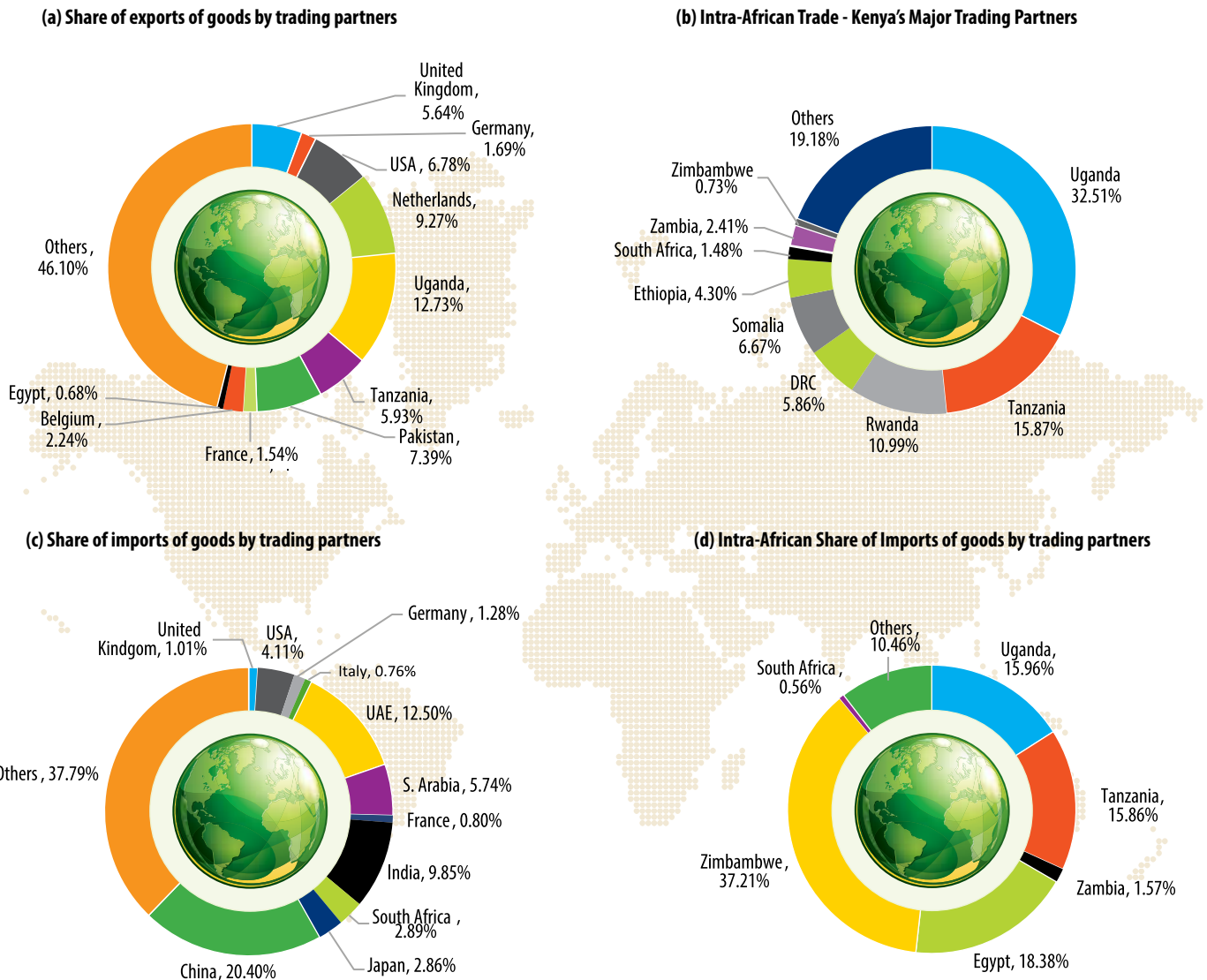


Source: CBK

as indicated by "Others" which accounted for a substantial 46.10 percent, thereby pointing to a diverse and broad spectrum of destinations for exported goods. Other export destinations are Netherlands at 12.73 percent, the USA at 6.78 percent, Pakistan at 7.39 percent, and Uganda at 5.93 percent. On the

flip side, the major distributors of imports are Others (37.79 percent), UAE (12.50 percent), followed by South Arabia at 5.74 percent. The United States contributes substantially with 4.11 percent, closely trailed by India at 9.85 percent (Figure 10).

**Figure 10: Kenya's Intra-African and Global Trade Developments**



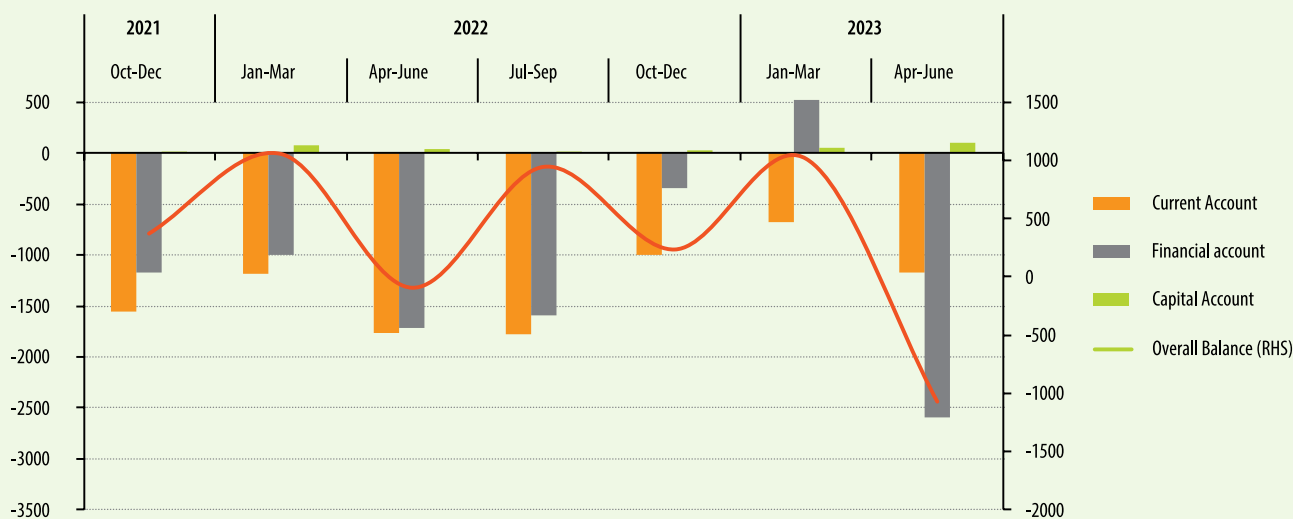
Source: CBK



In the second quarter of 2023, the overall balance of payments increased significantly to USD 1,075 million, marking a significant rise from the USD 94 million recorded in the same period in 2022. Simultaneously, the current account deficit decreased to USD 1,176 million, largely due to reduced import costs, despite a decline in

service receipts and remittances. Specifically, there was a net capital account inflow of USD 100 million in Q2 2023. The financial account saw a substantial increase in inflows, reaching USD 2,592 million, in contrast to the net inflows of USD 1,717 million during the second quarter of 2022 (**Figure 11**).

**Figure 11: Balance of the Payments Performance**



Source: CBK Quarterly Economic Review

# Sectoral Performance

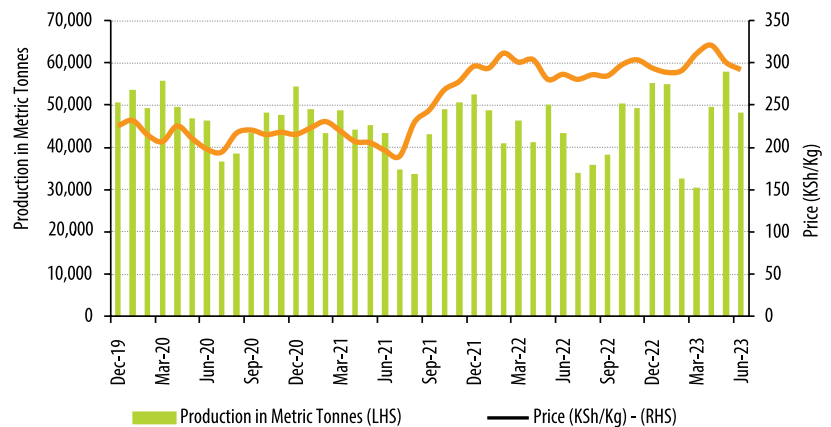
## Agriculture

**S**ustaining a dynamic agricultural sector remains pivotal for overall development due to its significant impact on increasing agricultural production and subsequent value addition in downstream industries. This generates considerable multiplier effects.

Despite erratic rainfall resulting from cessation of long rains in major regions and the onset of cold weather during the second quarter of 2023, tea production surged by 15.6 percent to 155,505 metric tonnes, a notable rise from the 134,533 metric tonnes produced during the corresponding period in 2022 (Figure 12). Similarly, the average tea auction price increased by 4.9 percent to ksh. 304 per kilogram, primarily influenced by the depreciation of the shilling against the US dollar. However, overall, the trend in tea prices has been declining since the second quarter of 2022 due to reduced demand, a consequence of the persisting global economic recession. This downturn, largely linked to the ongoing Russia-Ukraine crisis and recent armed conflict in Sudan, has notably impacted tea imports in several markets that typically trade Kenyan tea.

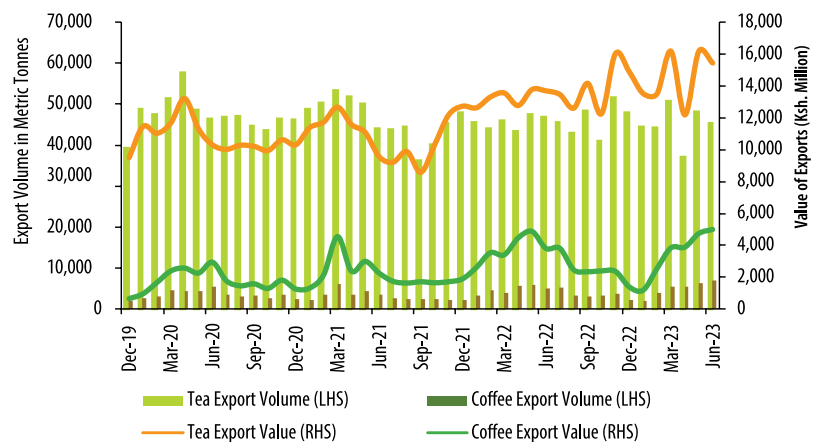
Tea and coffee export volume and values depicted interesting trends within the quarter. While the volume of tea exports decreased during the second quarter of 2023, the depreciation of the shilling against the US dollar resulted in a higher overall export value. More specifically, a total of 130,572 metric tonnes of tea were exported, amounting to a value of Ksh. 43,802 million in the second quarter of 2023, compared to 137,621 metric tonnes valued at Ksh. 40,239 million during the corresponding period in 2022. In terms of coffee exports, the quantity exported in second quarter of 2023 reached 18,866 metric tonnes, valued at Ksh. 13,641 million, as opposed to 16,597 metric tonnes valued at Ksh. 13,163 million during the corresponding quarter in 2022.

**Figure 12: Tea production and Price Movements**



Source: KNBS

**Figure 13: Value of Tea and Coffee Exports**



Source: KNBS

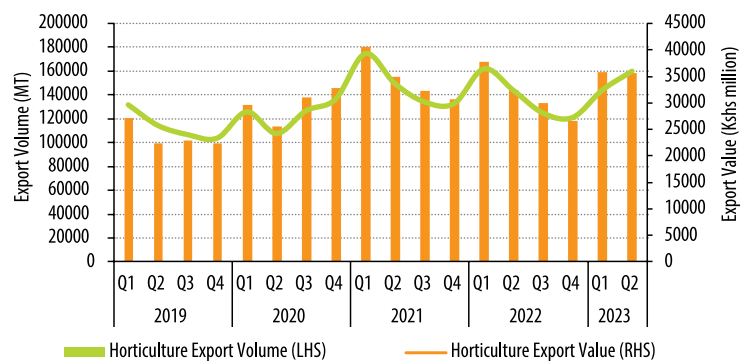


Horticulture exports showed growth in second quarter 2023, with a 9.8 percent rise in volume and an 11.2 percent increase in value compared to the corresponding period in 2022, signaling positive expansion in both export quantity and financial worth within the sector (Figure 14a).

The horticultural sector exhibited growth compared to the same quarter in 2022. This growth was evidenced by a 9.877 percent increase in the export volume, rising from 144,310.17 to 158,405.73, predominantly due to high demand for fruits and vegetables which increased by 186 percent and 80 percent respectively. Additionally, the export value surged by 11.22 percent, partly influenced by the strengthening US dollar (Figure 14b).

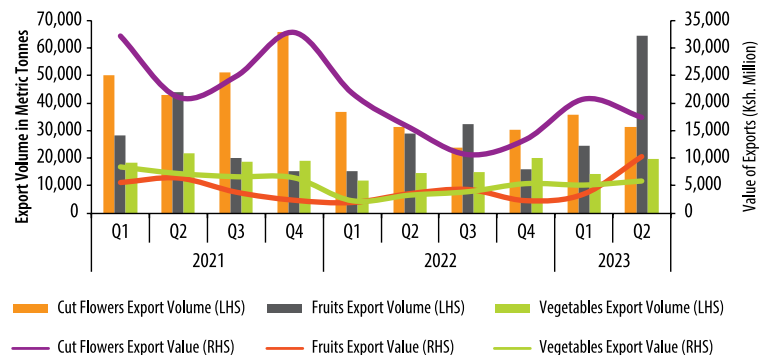
The export volumes of vegetables saw a substantial increase, rising from 14,626.72 metric tonnes in the second quarter of 2022 to 19,598.47 metric tonnes in second quarter of 2023. Correspondingly, the value of vegetable exports surged from KSh. 3,221.61 million to KSh. 5,789.22 million during the same periods. Fruits also experienced a noteworthy volume surge, climbing from 28,863.30 metric tonnes in second quarter of 2022 to 64,367.66 metric tonnes in the second quarter of 2023. Although cut flower exports decreased by 0.08 percent, the value expanded by 12.08 percent, partly due to the effects of strengthening US dollar.

**Figure 14a: Horticultural Exports**



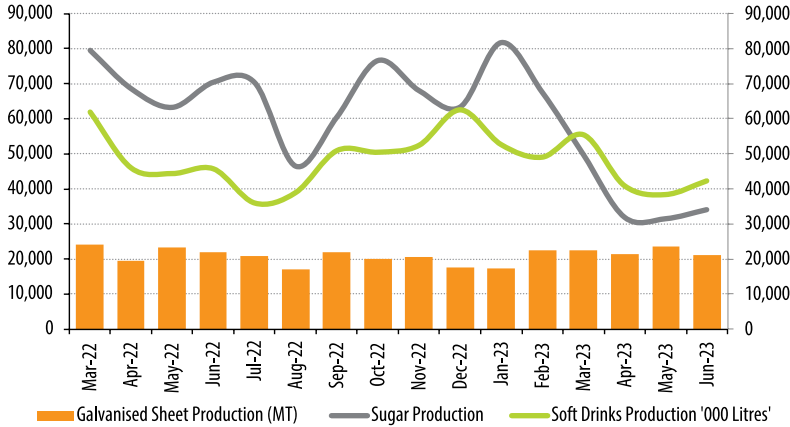
Source: KNBS

**Figure 14b: Cut Flowers, Vegetables and Fruits**

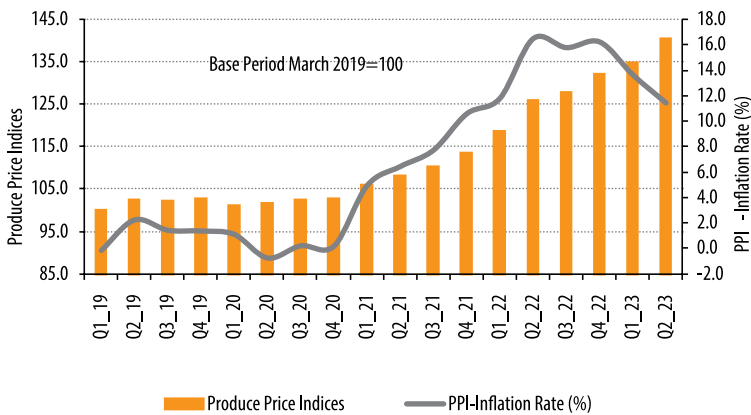


Source: KNBS

**Figure 15: Production in manufacturing sub-sectors**



**Figure 16: Producer Price Index**



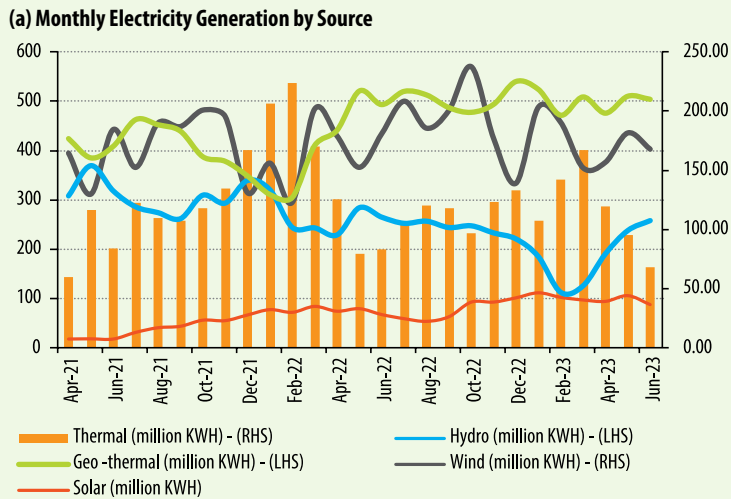
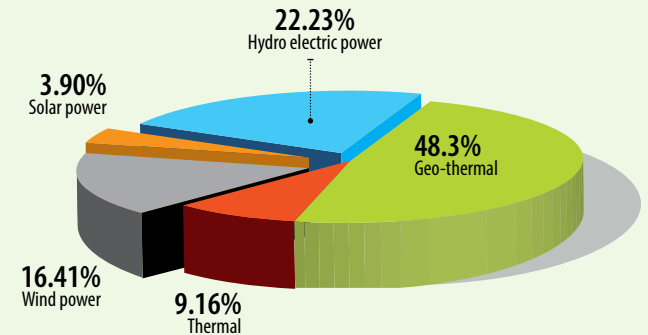
## Manufacturing

During the second quarter of 2023, the manufacturing sector expanded by 5.3 percent, displaying varying production levels across different subsectors (**Figure 15**). While sugar and soft drinks production declined, there was a modest 1.73 percent growth in galvanized sheet production. Additionally, milk consumption rose to 2,275,974 million litres in the second quarter of 2023, marking a 6.88 percent increase from a corresponding period in 2022.

## Producer Price Index

The Producer price Index (**Figure 16**) rose by 11.43 percent year-on-year in the second quarter 2023, from 126.0 in the second quarter 2022 to 140.4 in the second quarter 2023, on account of the continued growth in production costs.



**Figure 17: Monthly Electricity Generation by Source****(b) Proportion of total Electricity Generation by Source**

## Energy

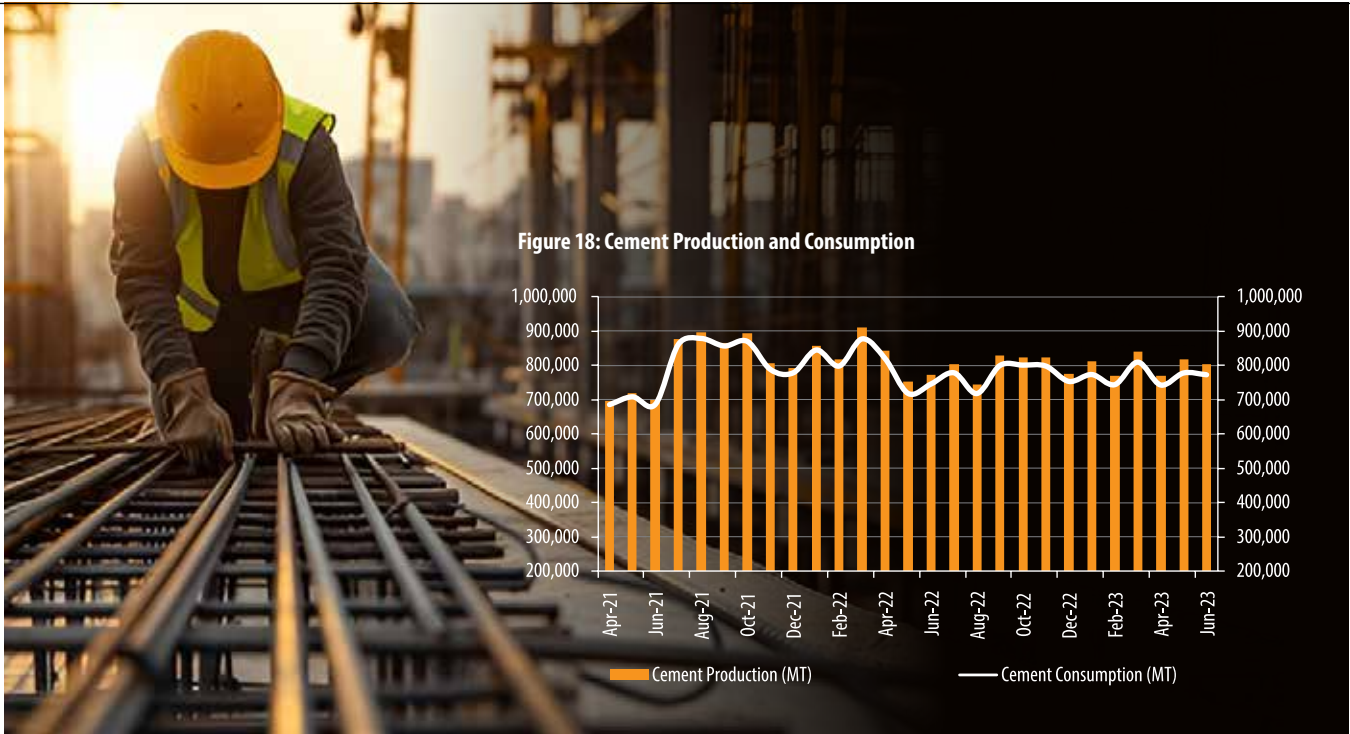
The total energy generated in the second quarter of 2023 declined by 1.28 percent, compared to the corresponding period in 2022. The latter dropped from 3,128.59 to 3,088.57 kilowatts. The decline is attributed to the general decline in hydroelectric power, which overshadowing the growths registered in geothermal and solar energy production (**Figure 17a**). Geothermal power constituted nearly half of the total energy produced during the quarter, closely followed by hydroelectric power, which accounted for 22.23 percent of the total electricity generated (**Figure 17b**).

Crude oil prices moderated slightly, with the Murban crude oil prices dropping to USD 75.2 per barrel by the end of the quarter (**Table 1**). On its part, the average domestic petrol pump prices and LPG gas prices remained elevated following the removal of fuel subsidies. By the end of the quarter, the super petrol was retailing at KES 182.6 per litre, while that of diesel and Kerosene were up to KES 168.0 and 162.0 per litre. The LPG (13 kgs) gas retailing at KES 3069.0 in June 2023 having dropped from 3101.9 in February 2023.

**Table 2: Average Monthly Crude Oil and Retail Fuel Prices**

	Jul-22	Aug-22	Sep-22	Oct-22	Nov-22	Dec-22	Jan-23	Feb-23	Mar-23	Apr-23	May-23	Jun-23
Murban crude oil (US\$/Barrel)	108.6	101.9	95.3	93.6	89.7	79.6	81.6	81.9	78.5	84.1	75.8	75.2
Super petrol (KSh/Litre)	159.9	159.9	180.1	179.1	178.1	178.1	178.1	178.1	180.1	180.1	183.3	182.6
Diesel (KSh/Litre)	140.9	140.9	165.9	163.9	162.9	162.9	162.9	162.9	162.9	162.9	169.1	168.0
Kerosene (KES/Litre)	128.9	128.9	148.9	147.9	146.9	146.9	146.9	146.9	146.9	146.9	161.8	162.2
LPG (13Kgs)	3100.7	3103.2	3106.7	3084.0	3004.8	2980.8	2961.9	3101.9	3137.7	3135.4	3125.4	3069.0

Source: ADNOC oil prices and KNBS



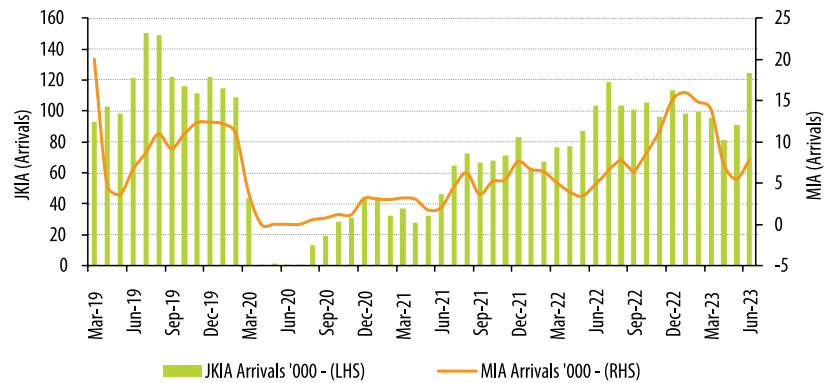
## Building and Construction

The building and construction sector showed modest growth, increasing by 2.6 percent. Cement production for the quarter reached 2,391,273 metric tonnes, up from 2,363,653 metric tonnes in the comparable period of 2022. Similarly, cement consumption recorded 0.4 percent growth during the quarter. This is equivalent to 2,292.3 thousand metric tonnes of cement consumed in the second quarter of 2023 (Figure 18).

## Tourism

Tourist arrivals showed a notable increase during the quarter, rising to 337,937 compared to 279,981 in the same period of 2022. Specifically, arrivals through the JKIA terminal amounted to 293,051, a significant rise from 267,769 in 2022 and 106,497 in 2021. Additionally, Mombasa International Airport (MIA) recorded arrivals of 44,886 (Figure 19).

Figure 19: Monthly Inbound Tourist Arrivals



Source: KNBS



# Government Revenue and Expenditure

**T**he revenue collected in the fiscal year 2022/23 grew to KSh 679.4 billion, having been driven by increased tax and non-tax revenues, as external grants declined. The revenue-expenditure grew to KSh 267 billion (Figure 20).

In terms of the revenue structure, the income tax has remained the major source of government revenue since it accounted for 45.2 percent of total revenue, having grown its share by 0.3 percentage. The VAT increased by 0.3 percent, while the shares of import taxes, excise taxes and other tax revenues declined by 0.2 percentage points, 0.3 percentage points, and 0.2 percentage points, respectively (Figure 21).

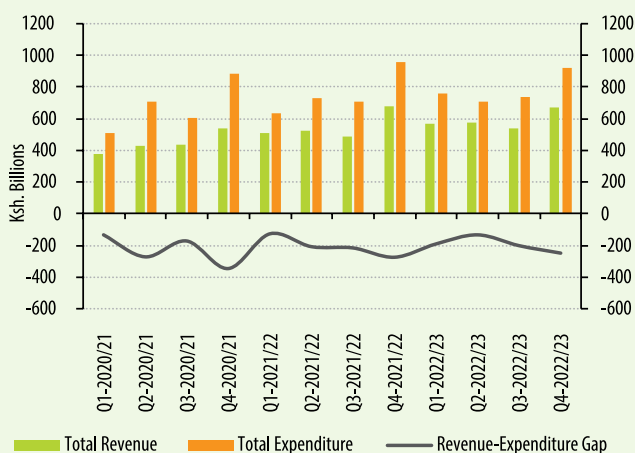
The total government expenditure, illustrated by Figure 22, indicates that during the final quarter of FY

2022/2023, recurrent expenditure accounted for 63.2 percent of total expenditure, compared 67.6 percent in a similar quarter in the FY 2021/2022. The development expenditure, on its part, accounted for 18.1 percent of the total government expenditure in FY 2022/2023. The breakdown of the recurrent expenditure revealed that Salaries and wages accounted for 14.1 percent with domestic interest payment accounting for 17.0 percent. Foreign interest repayments and pension payments each accounted for 4.2 and 1.9 percent, respectively, of the total recurrent expenditure.



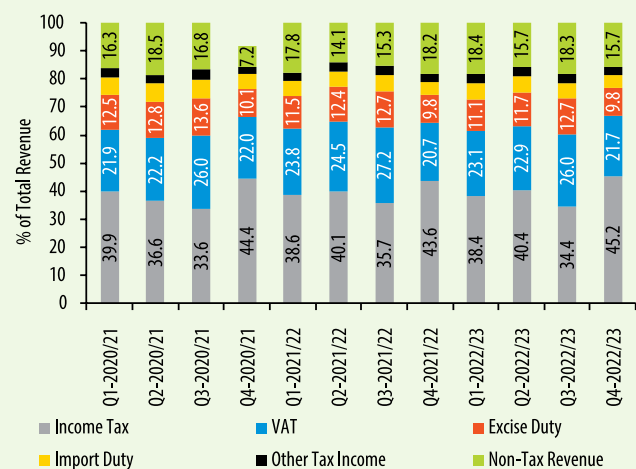
**Income tax remained Kenya's top revenue source at 45.2%, while recurrent expenditure dominated spending at 63.2% in FY 2022/2023.**

**Figure 20: Quarterly Revenue-Expenditure Gap**

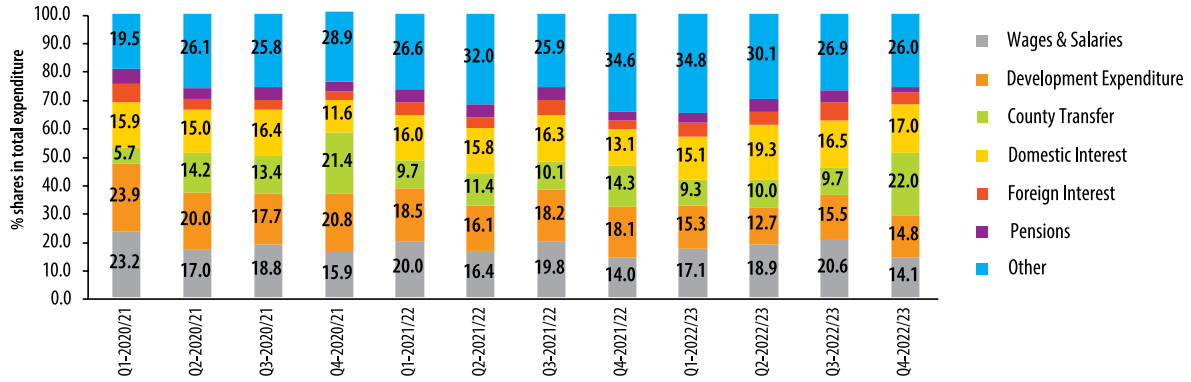


Source: CBK

**Figure 21: Quarterly Revenue Structure**



**Figure 22: Quarterly Expenditure Structure**



Source: Central Bank of Kenya

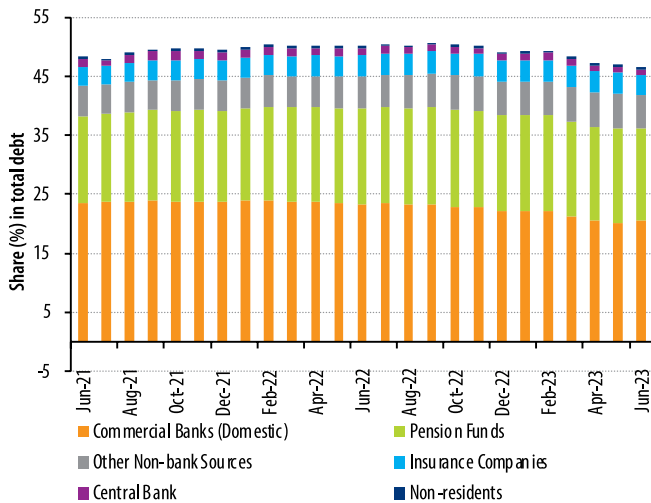
## Government Deficit Financing and Public Debt

During the fourth quarter of the fiscal year 2022/23, Kenya witnessed an overall 8.5 percent increase in its public and publicly guaranteed debt. This growth was a result of a 4.3 percent rise in domestic debt and a more significant 12.4 percent surge in external debt. The escalation in domestic debt was primarily due to the increased adoption of Treasury bonds, constituting a

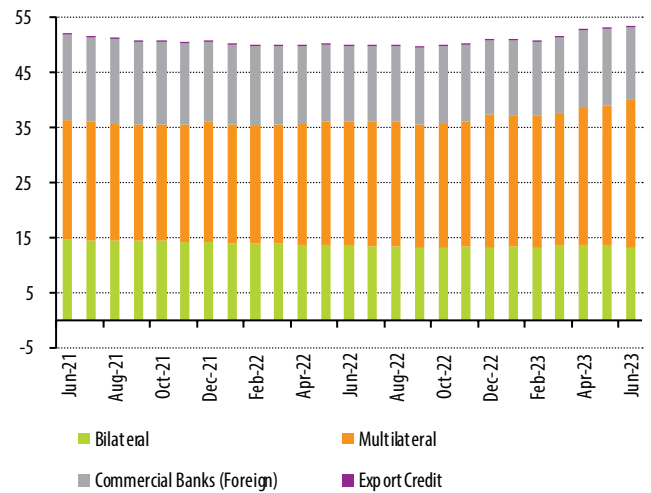
substantial 97.7 percent of the total domestic debt. The external debt increased by 12.4 percent, largely influenced by financial disbursements from the International Development Association (IDA) and fluctuations in exchange rates (Figure 23).

**Figure 23: External and Domestic Debt and its Composition**

**(a) Domestic Debt**



**(b) External Debt**



Source: Central Bank of Kenya

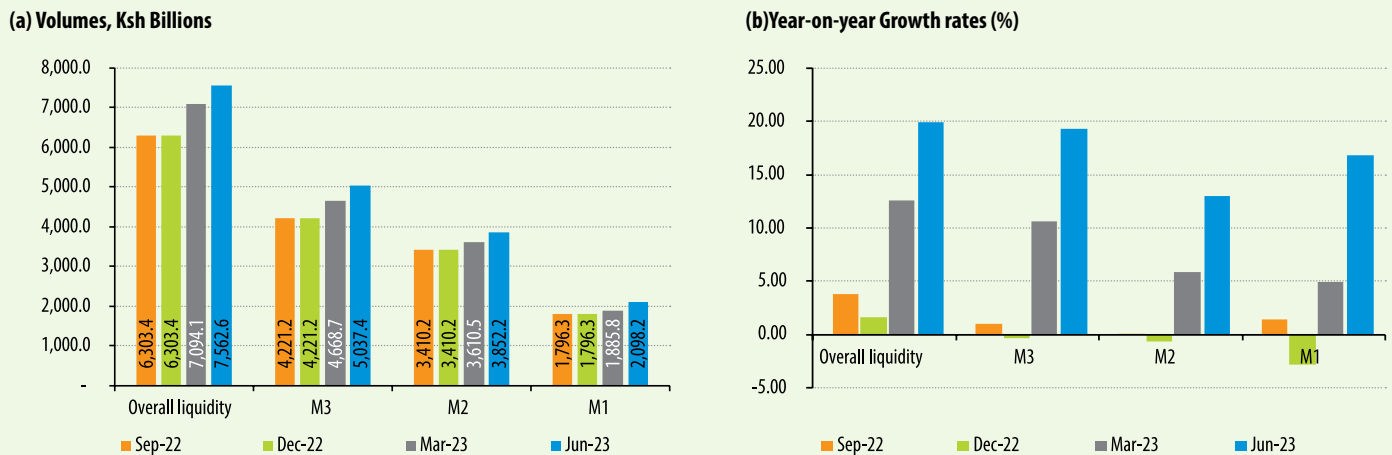


## Money Supply

In the second quarter of 2023, the broad money supply (M3) grew by 7.9 percent, a significant increase from the 3.0 percent in the preceding quarter. This rise was primarily driven by growths in deposits, notably in the corporate sector, which was bolstered by substantial government payments, ongoing

robust business activities, and increased energy sector deposits. The overall liquidity was up by 14.07 percent on a year-on-year basis to close the quarter at Ksh. 7,562.60 billion, up from Ksh. 6,629.80 billion recorded in a similar period in 2022 (**Figure 24**).

**Figure 24: Trends in Monetary Aggregates**



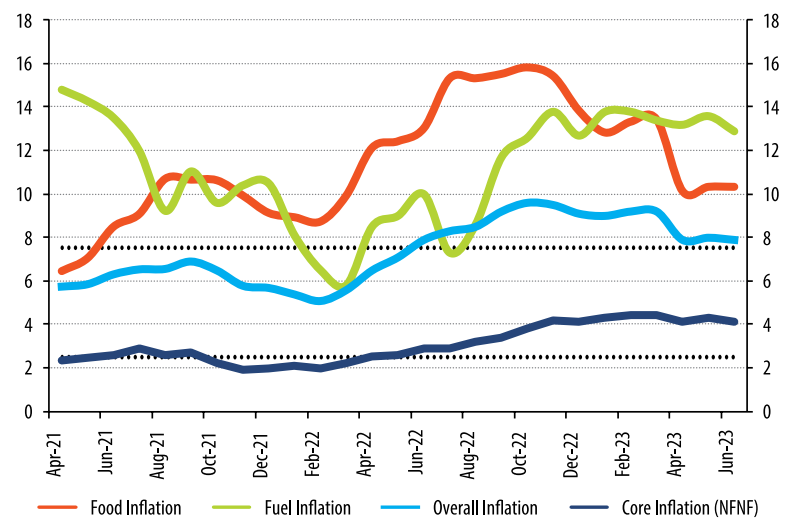
Source: CBK



## Inflation

Inflationary pressure softened, as overall inflation decreased to 7.9 percent in the second quarter of 2023, down from 9.1 percent in the first quarter (**Figure 25**). The reduction was primarily influenced by a decline in food prices, with food inflation dropping to 10.2 percent from the previous quarter's 13.2 percent. This decline was supported by domestic seasonal factors and a decrease in international food prices. However, fuel inflation, although reduced, remained relatively high at 13.2 percent, attributed largely to the conclusion of the fuel subsidy program. Non-food non-fuel (NFNF) inflation also declined to 4.2 percent from 4.4 percent in the preceding quarter, showcasing subdued demand pressures within the economy. The influence of heightened food prices continued to diminish, remaining the primary driver but contributing less to overall inflation, decreasing to 3.9 percentage points from 4.9 percentage points in the previous quarter. Both fuel and NFNF inflation made a slightly lesser contribution to overall inflation, dropping to 2.8 percentage points.

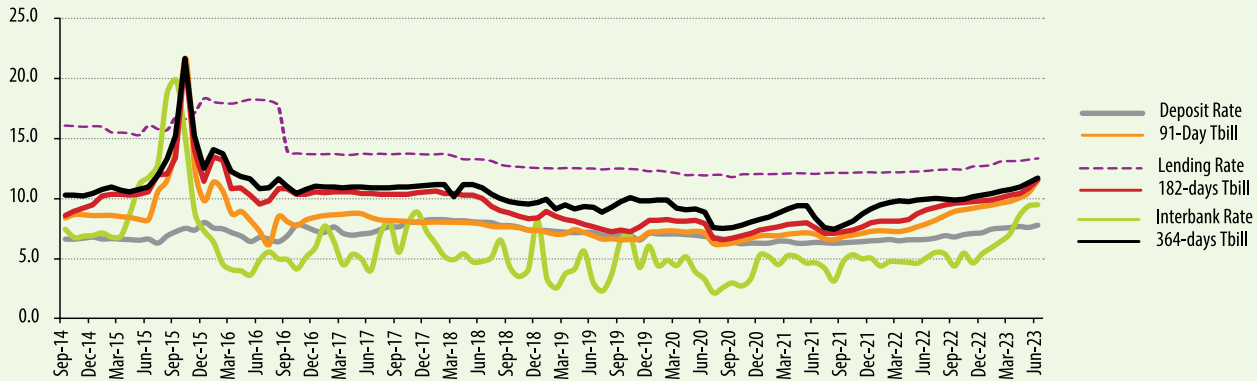
**Figure 25: Inflation Dynamics**



Source: Central Bank of Kenya



**Figure 26: Interest Rates Dynamics**



Source: Central Bank of Kenya

## Interest Rates

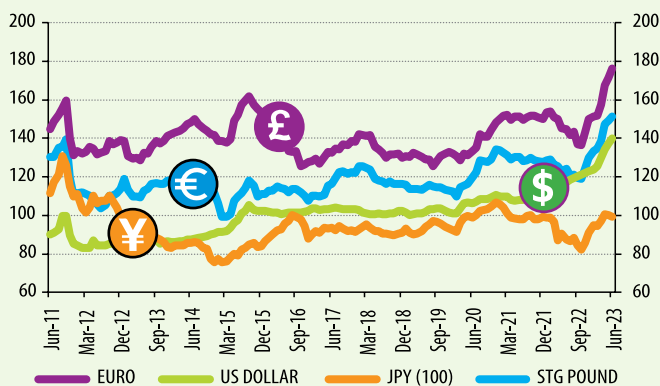
As depicted in **Figure 26**, short-term interest rates, average lending and deposit rates increased following the tightening of monetary policy. The average interbank interest rate rose to 9.48 percent in June 2023 from 7.05 percent in March 2023 and 5.06 percent in June 2022. Similarly, the average 91-day Treasury bill rate rose to 11.49 percent in June 2023 from 9.76 percent in March 2023 and 7.9 percent in June 2022. The average 182-day Treasury bill rate increased to 11.54 percent from 10.25 percent in March 2023. The weighted average lending rate rose to 13.31 percent in June 2023 from 13.09 percent in March 2023, while the weighted average deposit rate increased to 7.82 percent from 7.60 percent in March 2023.

## Exchange Rates

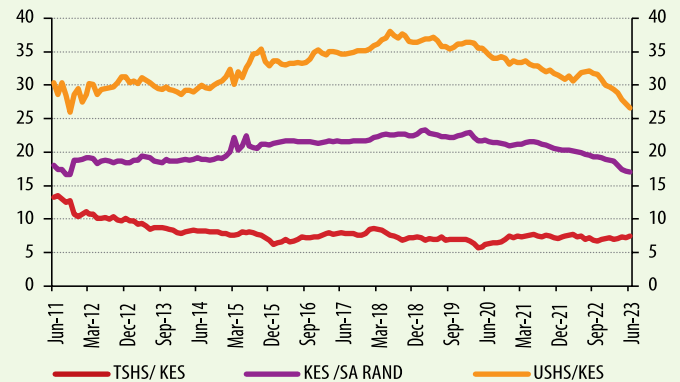
Throughout the second quarter of 2023, the foreign exchange market witnessed considerable pressure as the Kenyan shilling continued its depreciation against the US dollar. The shilling depreciated by 17.9 percent, averaging 137.1 against the dollar. This depreciation was driven by the escalating demand for dollars, especially among importers. There was also a mild depreciation against the Sterling Pound and the Euro. In contrast, the shilling displayed strength against Japanese Yen (**Figure 27a**). Within the East African Community (EAC), the Kenyan shilling gained ground against all the Ugandan shilling, Tanzanian shilling and the South African rand (**Figure 27b**).

**Figure 27: Exchange Rate Developments**

### (a) Major currencies



### (b) EAC region currencies



Source: Central Bank of Kenya

## Capital Markets

The capital market, as indicated by the market indices and market capitalization, dipped in performance during the second quarter 2023 (Figure 28a). All major indices registered consistent decreases, portraying a bearish trend. The NASI (2008=100) Points exhibited significant volatility in the quarter, and declined from 107.63 in April 2023 to 103.69 in May 2023, before rising to 107.00 in June 2023. This general drop during the quarter suggested a reduction in market performance. Similarly, the NSE 25 Share Index reflected a downward trend akin to the NASI. Starting at 2855.03 points in April 2023, this index also showcased a noticeable decline, reaching 2728.89 points by

June 2023. This decline is a pointer to a negative trend in the market for the top 25 listed companies. The NSE 20 Share Index was equally consistent with a declining trajectory that is akin to the other two indices. Overall, the market capitalization exhibited a declining trend from 1676.09 April 2023 to 1614.55 in May 2023, before rising to 1666.29 in June 2023 (Figure 28b). The equity turnover and total shares traded also declined by 67.9 percent and 29.6 percent (Figure 28c), respectively. The volume of contracts traded in the derivative markets declined further to 694 (Figure 2d).

Figure 28 a: Trends in Nairobi Securities Exchange Leading Indicators

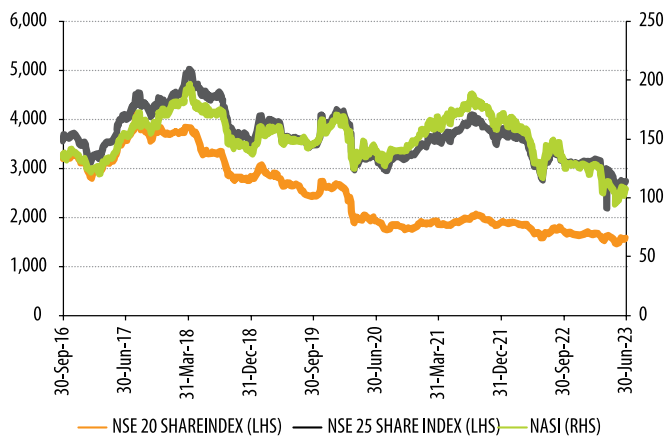


Figure 28 b: Trends in Market capitalization and Equities turnover

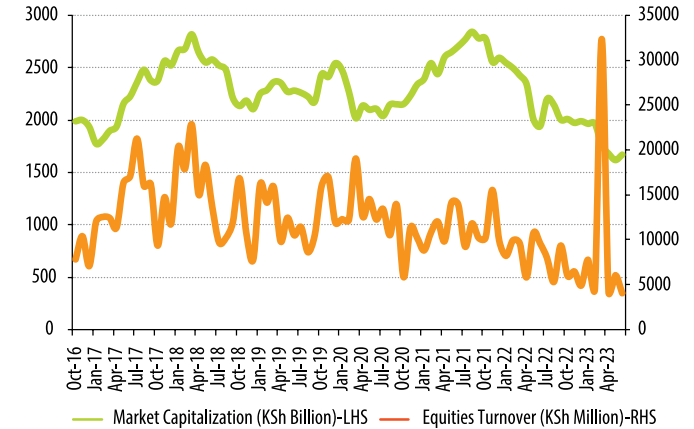


Figure 28 c: Trends in Number of shares traded

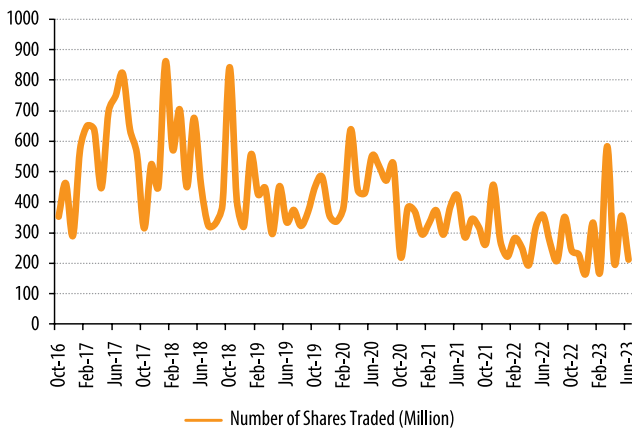
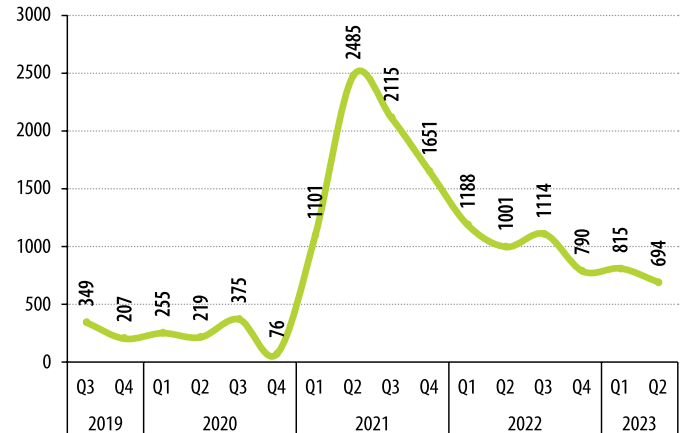


Figure 28 d: Trends in Number of derivative contracts



Source: Nairobi Securities Exchange

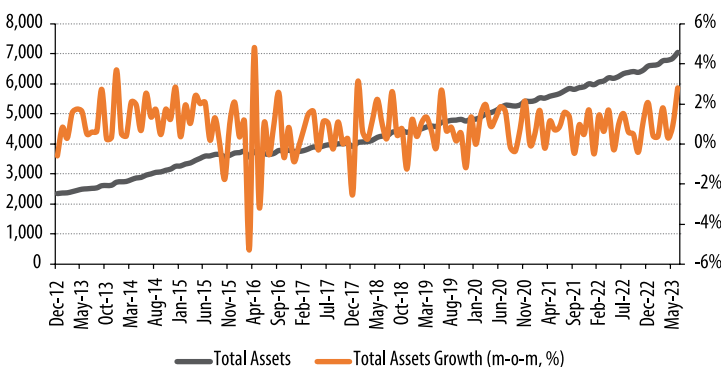


## Banking Sector Performance



**D**uring the second quarter of 2023, the banking sector in Kenya recorded significant growth, across several metrics. The total assets was up by 4.1 percent; rising to Ksh.7,052.4 billion from Ksh.6,771.7 billion in March 2023 (Figure 25).

Figure 25: Total Assets



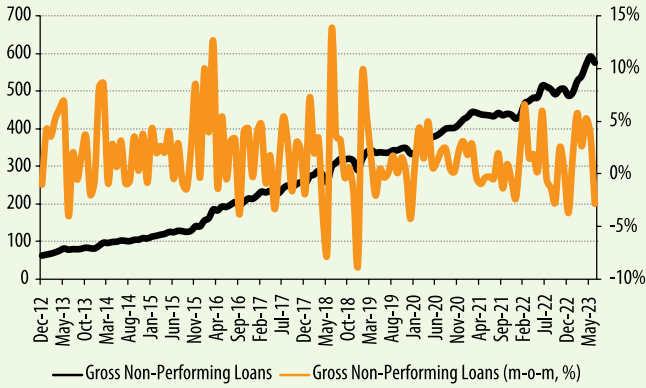
Simultaneously, the sector’s loan book expanded by 3.3 percent, up to Ksh.3,980.5 billion, with substantial growth observed in services sectors and manufacturing.

However, there was a rise in the Gross Non-Performing Loans (NPLs) to Ksh.576.1 billion (Figure 26 a). Consequently, this led to deterioration in asset quality. The gross NPLs to gross loans ratio rose to 14.47 percent in June 2023, up from 13.26 percent in December 2022 (Figure 26 b), mainly because of delayed payments experienced in the key sectors of the economy.

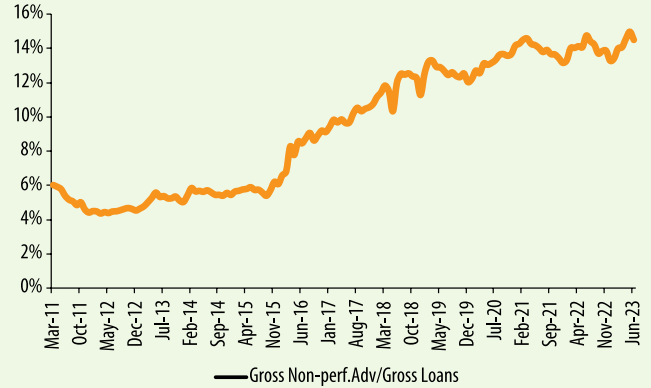


**Figure 30. The performance of the banking sector**

**(a) Gross Non-performing Loans**



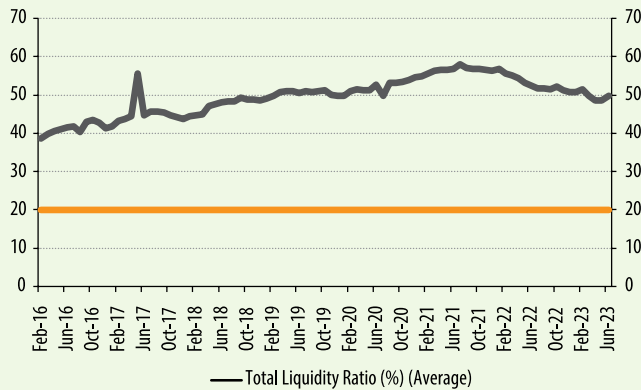
**(b) Asset Quality**



Source: Central Bank of Kenya

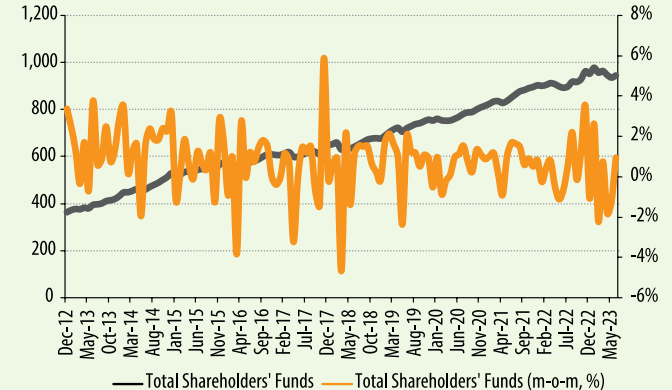
Liquidity on its part, declined to 49.7 percent in the second quarter of 2023 (Figure 27). Even so, it was still above the 20.0 percent regulatory threshold. The total shareholders’ fund, grew from KSh 893.0 billion in the second quarter of 2022 to KSh 945.10 billion at the end of the second quarter of 2023, indicating a substantial 5.83 percent increase (Figure 28).

**Figure 27: Total Liquidity Ratio**



Source: Central Bank of Kenya

**Figure 28: Total shareholders’ Funds**





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